

*Proposed International Public Sector Accounting
Standard*

Financial Instruments: Disclosures



**International Federation
of Accountants**

REQUEST FOR COMMENTS

The International Public Sector Accounting Standards Board, an independent standard-setting body within the International Federation of Accountants (IFAC), approved this Exposure Draft, “Financial Instruments: Disclosures,” for publication in April 2009. The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form.

Please submit your comments, preferably by email, so that they will be received by July 31, 2009. All comments will be considered a matter of public record. Comments should be addressed to:

Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street, 4th Floor
Toronto, Ontario M5V 3H2 CANADA

Email responses should be sent to: edcomments@ifac.org and stepheniefox@ifac.org

Copies of this exposure draft may be downloaded free-of-charge from the IFAC website at <http://www.ifac.org>.

Copyright © April 2009 by the International Federation of Accountants (IFAC). All rights reserved. Permission is granted to make copies of this work provided that such copies are for use in academic classrooms or for personal use and are not sold or disseminated and provided that each copy bears the following credit line: “*Copyright © April 2009 by the International Federation of Accountants (IFAC). All rights reserved. Used with permission of IFAC. Contact permissions@ifac.org for permission to reproduce, store or transmit this document.*” Otherwise, written permission from IFAC is required to reproduce, store or transmit, or to make other similar uses of, this document, except as permitted by law. Contact permissions@ifac.org.

ACKNOWLEDGMENT

This International Public Sector Accounting Standard is drawn primarily from International Financial Reporting Standard (IFRS) 7, “Financial Instruments: Disclosures” published by the International Accounting Standards Board (IASB). Extracts from IFRS 7 are reproduced in this publication of the International Public Sector Accounting Standards Board of the International Federation of Accountants with the permission of the International Accounting Standards Committee Foundation (IASCF).

The approved text of International Financial Reporting Standards (IFRS) is that published by the IASB in the English language, and copies may be obtained directly from IASB Publications Department, 30 Cannon Street, London EC4M 6XH, United Kingdom.

E-mail: publications@iasb.org

Internet: <http://www.iasb.org>

IFRSs, IASs, Exposure Drafts and other publications of the IASB are copyright of the IASCF.

“IFRS,” “IAS,” “IASB,” “IASCF,” “International Accounting Standards” and “International Financial Reporting Standards,” are trademarks of the IASCF and should not be used without the approval of the IASCF.

Financial Instruments

The IPSASB Strategy on Accounting for Financial Instruments

Background and Approach to these Exposure Drafts

1. IPSAS 15, “Financial Instruments; Disclosure and Presentation” was issued in December 2001. It was drawn primarily from International Accounting Standard (IAS) 32 (revised 1998), “Financial Instruments: Disclosure and Presentation” published by the International Accounting Standards Board (IASB).
2. Since that time, the IASB has issued revised standards on financial instruments, specifically IAS 32, “Financial Instruments: Presentation,” IAS 39, “Financial Instruments: Recognition and Measurement, and IFRS 7, “Financial Instruments: Disclosures.” In the absence of comparable IPSASs, entities applying IPSASs have had to rely upon the hierarchy in IPSAS 3, “Accounting Policies, Changes in Accounting Estimates and Errors” to develop accounting policies for the recognition and measurement of financial instruments This would generally lead to applying the revised IASB standards.
3. The IPSASB considers this an unsatisfactory situation for the public sector and firmly believes that having a comprehensive and robust set of accrual based accounting standards is crucial for the public sector, including standards for financial instruments.
4. In early 2007, the IPSASB agreed a detailed work program for IFRS convergence and committed to achieving converged IPSASs by December 31, 2009 that will be substantially converged with IFRSs approved as of December 31, 2008. The current global economic crisis and worldwide government interventions have increased the urgency for this convergence.
5. ED 37, ED 38 and ED 39 are the culmination of that work to develop IPSASs based on IAS 32, “Financial Instruments: Presentation” , IAS 39, “Financial Instruments: Recognition and Measurement”, and IFRS 7, “Financial Instruments: Disclosures” respectively. The exposure drafts were developed based on the version of the related IFRS at December 31, 2008. In addition, ED 38 includes two of the August 2008 proposed improvements although not adopted as at December 31, 2008 and changes approved by the IASB to IFRS 7 in February 2009 have been reflected in ED39.
6. The IPSASB’s approach in developing these exposure drafts has been to minimize changes to the IASB standards as far as possible. Application guidance has been developed for ED 37 and ED 38 on financial guarantees provided for nil or nominal consideration and concessionary loans. Additional disclosures on concessionary loans are proposed in ED 39. Other changes have been made to reflect the style and terminology of the IPSASs to ensure consistency with other IPSASs. In addition, the IPSASB notes that when final IPSASs on financial instruments are approved, existing IPSAS 15 will be withdrawn..

Strategy for Addressing Public Sector Issues

7. Approval of these EDs, leading to IPSASs to address financial instruments in the public sector, is just the beginning of a process by which the IPSASB will ultimately develop guidance that addresses further public sector specific issues. Some of these issues could

include the reporting entity and consolidations, non-contractual items with the characteristics of financial instruments, certain non-exchange transactions and accounting for financial instruments from a central bank perspective.

8. The IPSASB has established a joint Task Force with the IMF, to work with governments that have intervened in the current global economic crisis and help develop transparency and consistency in public sector financial reporting of recent interventions. The objective is not to develop standards but to assist governments and to ensure consistent, transparent accounting. The IPSASB sees this as a key initiative to support governments around the world at this crucial time.
9. The IPSASB recognizes that the IASB has a current project to undertake, on an accelerated basis, the replacement of existing financial instruments standards, including IAS 39 Financial Instruments: recognition and measurement with a common and globally accepted standard that would address issues arising from the financial crisis in a comprehensive manner. The IPSASB will be following this project closely, and any other in the future, and anticipates considering amendments and public sector specific issues for possible introduction in 2011-2012.

Conclusion

10. These three Exposure Drafts are being published as an integrated package. The IPSASB has issued two versions of each exposure draft; a 'clean' version that reflects how the final standard is proposed to appear; and a second version that is "marks up" the related IFRS to show the proposed changes made. The IPSASB hopes this will assist respondents in focusing on the amendments from the related IFRS and therefore will make it easier to respond.
11. To make it possible for the IPSASB to meet its target for convergence by December 31, 2009, the IPSASB's meeting schedule for 2009 has been modified to allow for a fourth IPSASB meeting in December 2009.
12. The IPSASB looks forward to receiving comments from interested parties on ED 37, ED 38 and ED 39. In view of the tight timetable for approving these proposed IOPSASs, the IPSASB stresses the importance of making comments by the comment deadline of July 31, 2009 to ensure that the IPSASB may fully consider those comments.

Objective

The objective of this Exposure Draft is to propose disclosure requirements for financial assets, financial liabilities and net assets/equity, the risks associated with holding financial instruments, and the entity's strategy for mitigating those risks.

Request for Comments

The IPSASB invites comments on all the proposals in the Exposure Draft. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

Specific Matter for Comment

The IPSASB considered all of the required disclosures in IFRS 7 to assess whether any disclosures should be deleted for public sector specific reasons. Examples of disclosures specifically considered include sensitivity analyses and collateral. The IPSASB concluded that there is no public sector specific reason to depart from the requirements of IFRS 7 by deleting any disclosures. Do you agree?

INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARD XX (ED 39)
FINANCIAL INSTRUMENTS: DISCLOSURES

CONTENTS

	Paragraph
Introduction	IN1– IN8
Objective	1–2
Scope	3–7
Classes of Financial Instruments and Level of Disclosure	8
Significance of Financial Instruments for Financial Position and Financial Performance	9-36
Statement of Financial Position	10-22
Categories of Financial Assets and Financial Liabilities	10
Financial Assets or Financial Liabilities at Fair Value through Surplus or Deficit	11-13
Reclassification	14-15
Derecognition	16
Collateral	17-18
Allowance Account for Credit Losses	19
Compound Financial Instruments with Multiple Embedded Derivatives	20
Defaults and Breaches	21-22
Statement of Financial Performance	23
Items of Revenue, Expense, Gains or Losses	23
Other Disclosures	24-36
Accounting Policies	24
Hedge Accounting	25-27
Fair Value	28-35
Concessionary Loans	36
Nature and Extent of Risks Arising from Financial Instruments	37-48
Qualitative Disclosures	39
Quantitative Disclosures	40-48
Credit Risk	42-44
Financial Assets that are either Past Due or Impaired	43

Collateral and other Credit Enhancements Obtained	44
Liquidity Risk	45
Market Risk	46-48
Sensitivity Analysis	46-47
Other Market Risk Disclosures	48
Effective Date and Transition	49-52
Appendix A: Defined terms	
Appendix B: Application Guidance	
Appendix C: Amendments to Other IPSASs	
Basis for Conclusions	
Implementation Guidance	
Comparison with IFRS 7	

International Public Sector Accounting Standard XX(ED 39), “Financial Instruments: Disclosures” (IPSAS XX) is set out in paragraphs 1–52 and Appendices A–C. All the paragraphs have equal authority except as noted otherwise. IPSAS XX (ED39) should be read in the context of its objective, the Basis for Conclusions, and the “Preface to International Public Sector Accounting Standards”. IPSAS 3, “Accounting Policies, Changes in Accounting Estimates and Errors” provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Introduction

Reasons for issuing the IPSAS

- IN1. The Standard prescribes disclosure requirements for financial instruments and is drawn from IFRS 7, “Financial Instruments: Disclosures” (including final and proposed amendments published up to December, 31 2008).
- IN2. In recent years, the techniques used by entities for measuring and managing exposure to risks arising from financial instruments have evolved and new risk management concepts and approaches have gained acceptance. In addition, many public and private sector initiatives have proposed improvements to the disclosure framework for risks arising from financial instruments.
- IN3. The International Public Sector Accounting Standards Board (IPSASB) believes that users of financial statements need information about an entity’s exposure to risks and how those risks are managed. Such information can influence a user’s assessment of the financial position and financial performance of an entity or of the amount, timing and uncertainty of its future cash flows. Greater transparency regarding those risks allows users to make more informed judgments about risk and return.

Main features of the IPSAS

- IN4. IPSAS XX (ED 39) applies to all risks arising from all financial instruments, except those instruments listed in paragraph 3. IPSAS XX (ED 39) applies to all entities, including entities that have few financial instruments (e.g. a government department whose only financial instruments are accounts receivable and accounts payable) and those that have many financial instruments (e.g. a financial institution most of whose assets and liabilities are financial instruments). However, the extent of disclosure required depends on the extent of the entity’s use of financial instruments and of its exposure to risk.
- IN5. IPSAS XX (ED 39) requires disclosure of:
- (a) The significance of financial instruments for an entity’s financial position, financial performance and cash flows. These disclosures incorporate many of the requirements previously in IPSAS 15.
 - (b) Qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk. The qualitative disclosures describe management’s objectives, policies and processes for managing those risks. The quantitative disclosures provide information about the extent to which the entity is exposed to risk, based on information provided internally to the entity’s key management personnel. Together, these disclosures provide an overview of the entity’s use of financial instruments and the exposures to risks they create.
- IN6. IPSAS XX (ED 39) includes in Appendix B mandatory application guidance that explains how to apply the requirements in IPSAS XX (ED 39). IPSAS XX (ED 39) is accompanied by non-mandatory Implementation Guidance that describes how an entity might provide the disclosures required by IPSAS XX (ED 39).

- IN7. IPSAS XX (ED 39) supersedes the disclosure requirements of IPSAS 15.
- IN8. IPSAS XX (ED 39) is effective for annual periods beginning on or after Month, Day, Year. Earlier application is encouraged.

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 end of the reporting period, and how the entity manages those risks.
2. The principles in this Standard complement the principles for recognizing, measuring and presenting financial assets and financial liabilities in IPSAS XX (ED 37), "Financial Instruments: Presentation" and IPSAS XX (ED 38), "Financial Instruments: Recognition and Measurement".

Scope

3. This Standard shall be applied by all entities to all types of financial instruments, except:
 - (a) Those interests in subsidiaries, associates or joint ventures that are accounted for in accordance with IPSAS 6, "Consolidated and Separate Financial Statements", IPSAS 7, "Investments in Associates" or IPSAS 8, "Interests in Joint Ventures". However, in some cases, IPSAS 6, IPSAS 7 or IPSAS 8 permits an entity to account for an interest in a controlled entity, associate or joint venture using IPSAS XX (ED 38); in those cases, entities shall apply the requirements of this Standard. Entities shall also apply this Standard to all derivatives linked to interests in subsidiaries, associates or joint ventures unless the derivative meets the definition of an equity instrument in IPSAS XX (ED 37).
 - (b) Employers' rights and obligations arising from employee benefit plans, to which IPSAS 26, "Employee Benefits" applies.
 - (c) Rights and obligations arising under insurance contracts. However, this Standard applies to:
 - (i) Financial guarantee contracts issued through non-exchange transactions; and
 - (ii) Derivatives that are embedded in insurance contracts if IPSAS XX (ED 38) requires the entity to account for them separately.
 - (iii) An issuer shall apply this Standard to financial guarantee contracts issued through an exchange transaction if the issuer applies IPSAS XX (ED 38) in recognizing and measuring the contracts, but shall apply the international or national standard dealing with insurance contracts if the issuer elects to apply those standards in recognizing and measuring them

Notwithstanding (i) and (iii) above, an entity may apply this Standard to other financial instruments that take the form of insurance contracts which involve the transfer of financial risk.

- (d) Financial instruments, contracts and obligations under share-based payment transactions to which the relevant international or national accounting standard dealing with share based payment applies, except for contracts within the scope of paragraphs 4 – 6 of IPSAS XX (ED 38), to which that Standard applies.
 - (e) Instruments that are required to be classified as equity instruments in accordance with paragraphs 15 and 16 or paragraphs 17 and 18 of IPSAS XX (ED 37).
4. This Standard applies to recognized and unrecognized financial instruments. Recognized financial instruments include financial assets and financial liabilities that are within the scope of IPSAS XX (ED 38). Unrecognized financial instruments include some financial instruments that, although outside the scope of IPSAS XX (ED 38), are within the scope of this Standard (such as some loan commitments).
 5. This Standard applies to contracts to buy or sell a non-financial item that are within the scope of IPSAS XX (ED 38) (see paragraphs 4 – 6 of IPSAS XX (ED 38)).
 6. **This Standard applies to all public sector entities other than Government Business Enterprises.**
 7. The Preface to International Public Sector Accounting Standards issued by the International Public Sector Accounting Standards Board (IPSASB) explains that GBEs apply International Financial Reporting Standards, which are issued by the International Accounting Standards Board (IASB).

Classes of financial instruments and level of disclosure

8. When this Standard requires disclosures by class of financial instrument, an entity shall 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 shall provide sufficient information to permit reconciliation to the line items presented in the statement of financial position.

Significance of financial instruments for financial position and financial performance

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

Statement of financial position

Categories of financial assets and financial liabilities

10. The carrying amounts of each of the following categories, as defined in IPAS XX (ED 38), shall be disclosed either in the statement of financial position or in the notes:
 - (a) Financial assets at fair value through surplus or deficit, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with IPSAS XX (ED 38);
 - (b) Held-to-maturity investments;

- (c) Loans and receivables;
- (d) Available-for-sale financial assets;
- (e) Financial liabilities at fair value through surplus or deficit, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with IPSAS XX (ED 38); and
- (f) Financial liabilities measured at amortized cost.

Financial assets or financial liabilities at fair value through surplus or deficit

11. If the entity has designated a loan or receivable (or group of loans or receivables) as at fair value through surplus or deficit, it shall disclose:
- (a) The maximum exposure to credit risk (see paragraph 42(a)) of the loan or receivable (or group of loans or receivables) at the end of the reporting period.
 - (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.
12. If the entity has designated a financial liability as at fair value through surplus or deficit in accordance with paragraph 10 of IPSAS XX (ED 38), it shall 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 AG4); 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.

13. The entity shall disclose:

- (a) The methods used to comply with the requirements in paragraphs 11(c) and 12(a).
- (b) If the entity believes that the disclosure it has given to comply with the requirements in paragraph 11(c) or 12(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

14. If the entity has reclassified a financial asset (in accordance with paragraphs 60 - 63 of IPSAS XX (ED 38)) as one measured:

- (a) At cost or amortized cost, rather than at fair value; or
- (b) At fair value, rather than at cost or amortized cost,

it shall disclose the amount reclassified into and out of each category and the reason for that reclassification.

15. If the entity has reclassified a financial asset out of the fair value through surplus or deficit category in accordance with paragraph 55 or 57 of IPSAS XX (ED 38) or out of the available-for-sale category in accordance with paragraph 58 of IPSAS XX (ED38), it shall disclose:

- (a) The amount reclassified into and out of each category;
- (b) For each reporting period until derecognition, the carrying amounts and fair values of all financial assets that have been reclassified in the current and previous reporting periods;
- (c) If a financial asset was reclassified in accordance with paragraph 55, the rare situation, and the facts and circumstances indicating that the situation was rare;
- (d) For the reporting period when the financial asset was reclassified, the fair value gain or loss on the financial asset recognized in surplus or deficit or in net assets/equity in that reporting period and in the previous reporting period;

- (e) For each reporting period following the reclassification (including the reporting period in which the financial asset was reclassified) until derecognition of the financial asset, the fair value gain or loss that would have been recognized in surplus or deficit or in net assets/equity if the financial asset had not been reclassified, and the gain, loss, revenue and expense recognized in surplus or deficit; and
- (f) The effective interest rate and estimated amounts of cash flows the entity expects to recover, as at the date of reclassification of the financial asset.

Derecognition

16. 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 17 – 39 of IPSAS XX (ED 38)). The entity shall 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 recognize all of the assets, the carrying amounts of the assets and of the associated liabilities; and
 - (d) When the entity continues to recognize 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 recognize, and the carrying amount of the associated liabilities.

Collateral

17. An entity shall 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 paragraph 39(a) of IPSAS XX (ED 38); and
 - (b) The terms and conditions relating to its pledge.
18. 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 shall 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

19. When financial assets are impaired by credit losses and the entity records the impairment in a separate account (e.g. 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 shall disclose a reconciliation of changes in that account during the period for each class of financial assets.

Compound financial instruments with multiple embedded derivatives

20. If an entity has issued an instrument that contains both a liability and an equity component (see paragraph 33 of IPSAS XX (ED 37)) and the instrument has multiple embedded derivatives whose values are interdependent (such as a callable convertible debt instrument), it shall disclose the existence of those features.

Defaults and breaches

21. For *loans payable* recognized at the end of the reporting period, an entity shall 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 end of the reporting period; and
 - (c) Whether the default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorized for issue.
22. If, during the period, there were breaches of loan agreement terms other than those described in paragraph 21, an entity shall disclose the same information as required by paragraph 21 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 end of the reporting period).

Statement of financial performance

Items of revenue, expense, gains or losses

23. An entity shall disclose the following items of revenue, expense, gains or losses either in the statement of financial performance or in the notes:
- (a) Net gains or net losses on:
 - (i) Financial assets or financial liabilities at fair value through surplus or deficit, 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 IPSAS XX (ED 38);
 - (ii) Available-for-sale financial assets, showing separately the amount of gain or loss recognized in net assets/equity during the period and the amount reclassified from net assets/equity and recognized directly in surplus or deficit for the period;
 - (iii) Held-to-maturity investments;
 - (iv) Loans and receivables; and

- (v) Financial liabilities measured at amortized cost;
- (b) Total interest revenue and total interest expense (calculated using the effective interest method) for financial assets or financial liabilities that are not at fair value through surplus or deficit;
- (c) Fee revenue 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 surplus or deficit; 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 revenue on impaired financial assets accrued in accordance with paragraph AG130 of IPSAS XX (ED 38); and
- (e) The amount of any impairment loss for each class of financial asset.

Other Disclosures

Accounting policies

24. In accordance with paragraph 132 of IPSAS 1 “Presentation of Financial Statements”, 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

25. An entity shall disclose the following separately for each type of hedge described in IPSAS XX (ED 38) (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 end of the reporting period; and
 - (c) The nature of the risks being hedged.
26. For cash flow hedges, an entity shall disclose:
- (a) The periods when the cash flows are expected to occur and when they are expected to affect surplus or deficit;
 - (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 recognized in net assets/equity during the period;

- (d) The amount that was reclassified from net assets/equity and included in surplus or deficit for the period, showing the amount included in each line item in the statement of financial performance; and
 - (e) The amount that was removed from net assets/equity 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.
27. An entity shall 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 recognized in surplus or deficit that arises from cash flow hedges; and
 - (c) The ineffectiveness recognized in surplus or deficit that arises from hedges of net investments in foreign operations.

Fair value

28. Except as set out in paragraph 34 for each class of financial assets and financial liabilities (see paragraph 8), an entity shall disclose the fair value of that class of assets and liabilities in a way that permits it to be compared with its carrying amount.
29. In disclosing fair values, an entity shall group financial assets and financial liabilities into classes, but shall offset them only to the extent that their carrying amounts are offset in the statement of financial position.
30. An entity shall disclose for each class of financial instruments 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. If there has been a change in valuation technique, the entity shall disclose that change and the reasons for making it.
31. To make the disclosures required by paragraph 32 an entity shall classify fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy shall have the following levels:
- (a) Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
 - (b) Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as price) or indirectly (i.e. derived from prices) (Level 2); and
 - (c) Inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3).

The level in the fair value hierarchy within which the fair value measurement is categorized in its entirety shall be determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. For this purpose, the significance of an input is assessed against the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a Level 3 measurement. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability.

32. For fair value measurements recognized in the statement of financial position an entity shall disclose for each class of financial instruments:
- (a) The level in the fair value hierarchy into which the fair value measurements are categorized in their entirety, segregating fair value measurements in accordance with the levels defined in paragraph 31.
 - (b) Any significant transfers between Level 1 and Level 2 of the fair value hierarchy and the reasons for those transfers. Transfers into each level shall be disclosed and discussed separately from transfers out of each level. For this purpose, significance shall be judged with respect to surplus or deficit, and total assets or total liabilities.
 - (c) For fair value measurements in Level 3, a reconciliation from the beginning balances to the ending balances, disclosing separately changes during the period attributable to the following:
 - (i) Total gains or losses for the period recognized in surplus or deficit, and a description of where they are presented in the statement of financial performance;
 - (ii) Total gains or losses recognized in net assets/equity;
 - (iii) Purchases, sales, issues and settlements (each type of movement disclosed separately); and
 - (iv) Transfers into or out of Level 3 (e.g. transfers attributable to changes in the observability of market data) and the reasons for those transfers. For significant transfers, transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3.
 - (d) The amount of total gains or losses for the period in (c)(i) above included in surplus or deficit that are attributable to gains or losses relating to those assets and liabilities held at the end of the reporting period and a description of where those gains or losses are presented in the statement of financial performance.
 - (e) For fair value measurements in Level 3, if changing one or more of the inputs to reasonably possible alternative assumptions would change fair value significantly, the entity shall state that fact and disclose the effect of those changes. The entity shall disclose how the effect of a change to a reasonably possible alternative assumption was calculated. For this purpose, significance shall be judged with respect to surplus

or deficit, and total assets or total liabilities, or, when changes in fair value are recognized in net assets/equity, total equity.

An entity shall present the quantitative disclosures required by this paragraph in tabular format unless another format is more appropriate.

33. If the market for a financial instrument is not active, an entity establishes its fair value using a valuation technique (see paragraphs AG105–AG111 of IPSAS XX (ED 38)). 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 AG107 of IPSAS XX (ED 38) 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 shall disclose, by class of financial instrument:
 - (a) Its accounting policy for recognizing that difference in surplus or deficit to reflect a change in factors (including time) that market participants would consider in setting a price (see paragraph AG108 of IPSAS XX (ED 38)); and
 - (b) The aggregate difference yet to be recognized in surplus or deficit at the beginning and end of the period and a reconciliation of changes in the balance of this difference.
34. 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 IPSAS XX (ED 38) because its fair value cannot be measured reliably;
 - (c) For a contract containing a discretionary participation feature if the fair value of that feature cannot be measured reliably.
35. In the cases described in paragraph 34(b) and (c), an entity shall 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 derecognized, that fact, their carrying amount at the time of derecognition, and the amount of gain or loss recognized.

Concessionary Loans

36. Concessionary loans are granted by entities on below market terms. Examples of concessionary loans granted by entities include loans to developing countries, small farms, student loans granted to qualifying students for tertiary education and housing loans granted to low income families. For concessionary loans granted an entity shall disclose:
- (a) A reconciliation between the opening and closing carrying amounts of the loans, including:
 - (i) Nominal value of new loans granted during the period;
 - (ii) The fair value adjustment on initial recognition;
 - (iii) Loans repaid during the period;
 - (iv) Impairment losses recognized;
 - (v) Any increase during the period in the discounted amount arising from the passage of time; and
 - (vi) Other changes.
 - (b) Nominal value of the loans at the end of the period;
 - (c) The purpose and terms of the various types of loans; and
 - (d) Valuation assumptions.

Nature and extent of risks arising from financial instruments

37. **An entity shall 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 end of the reporting period.**
38. The disclosures required by paragraphs 39–48 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

39. For each type of risk arising from financial instruments, an entity shall disclose:
- (a) The exposures to risk and how they arise;
 - (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

40. For each type of risk arising from financial instruments, an entity shall disclose:

- (a) Summary quantitative data about its exposure to that risk at the end of the reporting period. This disclosure shall be based on the information provided internally to key management personnel of the entity (as defined in IPSAS 20, “Related Party Disclosures”), for example the entity’s governing body or chief executive officer.
 - (b) The disclosures required by paragraphs 42-48, to the extent not provided in (a), unless the risk is not material (see paragraphs 45–47 of IPSAS 1 for a discussion of materiality).
 - (c) Concentrations of risk if not apparent from (a) and (b).
41. If the quantitative data disclosed as at the end of the reporting period are unrepresentative of an entity’s exposure to risk during the period, an entity shall provide further information that is representative.

Credit risk

42. An entity shall disclose by class of financial instrument:
- (a) The amount that best represents its maximum exposure to credit risk at the end of the reporting period without taking account of any collateral held or other credit enhancements (e.g. netting agreements that do not qualify for offset in accordance with IPSAS XX (ED 37));
 - (b) In respect of the amount disclosed in (a), a description of collateral held as security and other credit enhancements;
 - (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.

Financial assets that are either past due or impaired

43. An entity shall disclose by class of financial asset:
- (a) An analysis of the age of financial assets that are past due as at the end of the reporting period but not impaired;
 - (b) An analysis of financial assets that are individually determined to be impaired as at the end of the reporting period, 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

44. 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 (e.g.

guarantees), and such assets meet the recognition criteria in other Standards, an entity shall 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

45. An entity shall disclose:

- (a) A maturity analysis for non-derivative financial liabilities (including issued financial guarantee contracts) that shows the remaining contractual maturities.
- (b) A maturity analysis for derivative financial liabilities. The maturity analysis shall include the remaining contractual maturities for those derivative financial liabilities for which contractual maturities are essential for an understanding of the timing of the cash flows (see paragraph AG14).
- (c) A description of how it manages the liquidity risk inherent in (a) and (b).

Market risk

Sensitivity analysis

46. Unless an entity complies with paragraph 47, it shall disclose:

- (a) A sensitivity analysis for each type of market risk to which the entity is exposed at the end of the reporting period, showing how surplus or deficit and net assets/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.

47. If an entity prepares a sensitivity analysis, such as value-at-risk, that reflects interdependencies between risk variables (e.g. 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 46. The entity shall 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

48. When the sensitivity analyses disclosed in accordance with paragraph 46 or 47 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 shall disclose that fact and the reason it believes the sensitivity analyses are unrepresentative.

Effective date and transition

49. An entity shall apply this International Public Sector Accounting Standard for annual financial statements covering periods beginning on or after Month XX, 20XX. Earlier application is encouraged. If an entity applies this Standard for a period beginning before Month XX, 20XX, it shall disclose that fact.
50. An entity shall not apply this International Public sector Accounting Standard before Month, Day, Year, unless it also applies IPSAS XX (ED 37) and IPSAS XX (ED 38).
51. When an entity adopts the accrual basis of accounting, as defined by International Public Sector Accounting Standards, for financial reporting purposes, subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.
52. If an entity applies this Standard for annual periods beginning before Month, Day, Year, it need not present comparative information for the disclosures required by paragraphs 37–48 about the nature and extent of risks arising from financial instruments.

Appendix A

Defined Terms

This appendix is an integral part of the IPSAS.

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 that are settled by delivering cash or another financial asset.
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 9 of IPSAS XX (ED 37) or paragraph 10 of IPSAS XX (ED 38) and are used in the IPSAS with the meaning specified in IPSAS XX (ED 37) and IPSAS XX (ED 38).

- Amortized 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 asset or financial liability at fair value through surplus or deficit
- Financial asset or financial liability held for trading
- Financial guarantee contract
- Financial instrument
- Financial liability
- 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 the IPSAS.

Classes of financial instruments and level of disclosure (paragraph 8)

- AG1. Paragraph 8 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 8 are determined by the entity and are, thus, distinct from the categories of financial instruments specified in IPSAS XX (ED 38) (which determine how financial instruments are measured and where changes in fair value are recognized).
- AG2. In determining classes of financial instrument, an entity shall, at a minimum:
- (a) Distinguish instruments measured at amortized cost from those measured at fair value.
 - (b) Treat as a separate class or classes those financial instruments outside the scope of this Standard.
- AG3. An entity decides, in the light of its circumstances, how much detail it provides to satisfy the requirements of this Standard, 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 shall not obscure important information by including it among a large amount of insignificant detail. Similarly, an entity shall 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 financial performance

Financial liabilities at fair value through surplus or deficit (paragraphs 12 and 13)

- AG4. If an entity designates a financial liability as at fair value through surplus or deficit, paragraph 12(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 12(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 12(a).

Other disclosure – accounting policies (paragraph 24)

AG5. Paragraph 24 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 surplus or deficit:
 - (i) The nature of the financial assets or financial liabilities the entity has designated as at fair value through surplus or deficit;
 - (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 paragraph 10, 13 or 14 of IPSAS XX (ED 38) for such designation. For instruments designated in accordance with paragraph (b)(i) of the definition of a financial asset or financial liability at fair value through surplus or deficit in IPSAS XX (ED 38), 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 (b)(ii) of the definition of a financial asset or financial liability at fair value through surplus or deficit in IPSAS XX (ED 38), that disclosure includes a narrative description of how designation at fair value through surplus or deficit 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 40 of IPSAS XX (ED 38)).
- (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 19).
- (e) How net gains or net losses on each category of financial instrument are determined (see paragraph 23(a)), for example, whether the net gains or net losses on items at fair value through surplus or deficit include interest or revenue from dividends or similar distributions.
- (f) The criteria the entity uses to determine that there is objective evidence that an impairment loss has occurred (see paragraph 23(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 42(d)).
- (h) For financial guarantee contracts at no or nominal consideration, where no fair value can be determined, disclosure of the circumstances that result in a provision being recognized in accordance with IPSAS 19.

Paragraph 137 of IPSAS 1 also requires entities to disclose, in the summary of significant accounting policies or other notes, the judgments, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognized in the financial statements.

Nature and extent of risks arising from financial instruments (paragraphs 37-48)

AG6. The disclosures required by paragraphs 37-48 shall 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 40)

AG7. Paragraph 40(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 shall disclose information using the method or methods that provide the most relevant and reliable information. IPSAS 3, “Accounting Policies, Changes in Accounting Estimates and Errors” discusses relevance and reliability.

- AG8. Paragraph 40(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 judgment taking into account the circumstances of the entity. Disclosure of concentrations of risk shall include:
- (a) A description of how management determines concentrations;
 - (b) A description of the shared characteristic that identifies each concentration (e.g. 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 42(a))

- AG9. Paragraph 42(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 IPSAS XX (ED 37); and
 - (b) Any impairment losses recognized in accordance with IPSAS XX (ED 38).
- AG10. 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, e.g. 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 end of the reporting period 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 recognized 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 recognized as a liability.

Quantitative liquidity risk disclosures (paragraphs 40(a) and 45(a) and (b))

AG11. In accordance with paragraph 40(a) an entity discloses summary quantitative data about its exposure to liquidity risk on the basis of the information provided internally to key management personnel. An entity shall explain how those data are determined. If the outflows of cash (or another financial asset) included in those data could either:

- (a) Occur significantly earlier than indicated in the data, or
- (b) Be for significantly different amounts from those indicated in the data (e.g. for a derivative that is included in the data on a net settlement basis but for which the counterparty has the option to require gross settlement),

the entity shall state that fact and provide quantitative information that enables users of its financial statements to evaluate the extent of this risk unless that information is included in the contractual maturity analyses required by paragraph 45(a) or (b).

AG12. In preparing the maturity analyses required by paragraph 45(a) and (b), an entity uses its judgment 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.

AG13. In complying with paragraph 45(a) and (b), an entity shall not separate an embedded derivative from a hybrid (combined) instrument. For such an instrument, an entity shall apply paragraph 45(a).

AG14. Paragraph 45(b) requires an entity to disclose a quantitative maturity analysis for derivative financial liabilities that shows remaining contractual maturities if the contractual maturities are essential for an understanding of the timing of the cash flows. For example, this would be the case for:

- (a) An interest rate swap with a remaining maturity of five years in a cash flow hedge of a variable rate financial asset or liability.
- (b) All loan commitments.

AG15. Paragraph 45(a) requires an entity to disclose maturity analyses for financial liabilities that show the remaining contractual maturities for some financial liabilities. In this disclosure:

- (a) When a counterparty has a choice of when an amount is paid, the liability is allocated to the earliest period in which the entity can be required to pay. For example, financial liabilities that an entity can be required to repay on demand (e.g. demand deposits) are included in the earliest time band.
- (b) 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.

- (c) For issued financial guarantee contracts the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

AG16. The contractual amounts disclosed in the maturity analyses as required by paragraph 45(a) and (b) 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 (e.g. 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 statement of financial position because the amount in that statement is based on discounted cash flows. When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting period. 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 end of the period.

AG17. Paragraph 45(c) requires an entity to describe how it manages the liquidity risk inherent in the items disclosed in the quantitative disclosures required in paragraph 39(a) and (b). An entity shall disclose a maturity analysis of financial assets it holds for managing liquidity risk (e.g. financial assets that are readily saleable or expected to generate cash inflows to meet cash outflows on financial liabilities), if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk.

AG18. Other factors that an entity might consider in providing the disclosure required in paragraph 39(c) include, but are not limited to, whether the entity:

- (a) Has committed borrowing facilities (e.g. commercial paper facilities) or other lines of credit (e.g. stand-by credit facilities) that it can access to meet liquidity needs;
- (b) Holds deposits at central banks to meet liquidity needs;
- (c) Has very diverse funding sources;
- (d) Has significant concentrations of liquidity risk in either its assets or its funding sources;
- (e) Has internal control processes and contingency plans for managing liquidity risk;
- (f) Has instruments that include accelerated repayment terms (e.g. on the downgrade of the entity's credit rating);
- (g) Has instruments that could require the posting of collateral (e.g. margin calls for derivatives);

- (h) Has instruments that allows the entity to choose whether it settles its financial liabilities by delivering cash (or another financial asset) or by delivering its own shares; or
- (i) Has instruments that are subject to master netting agreements.

Market Risk—Sensitivity Analysis (Paragraphs 46 and 47)

AG19. Paragraph 46(a) requires a sensitivity analysis for each type of market risk to which the entity is exposed. In accordance with paragraph AG3, 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.

AG20. Paragraph 46(a) requires the sensitivity analysis to show the effect on surplus or deficit and net assets/equity of reasonably possible changes in the relevant risk variable (e.g. prevailing market interest rates, currency rates, equity prices or commodity prices). For this purpose:

- (a) Entities are not required to determine what the surplus or deficit for the period would have been if relevant risk variables had been different. Instead, entities disclose the effect on surplus or deficit and net assets/equity at the end of the reporting period assuming that a reasonably possible change in the relevant risk variable had occurred at the end of the reporting period 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 surplus or deficit (ie 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 surplus or deficit and net assets/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.

AG21. 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 surplus or deficit and net assets/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 surplus or deficit and net assets/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 shall 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.

AG22. Paragraph 47 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 47(a) by disclosing the type of value-at-risk model used (e.g. whether the model relies on Monte Carlo simulations), an explanation about how the model works and the main assumptions (e.g. 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.

AG23. An entity shall provide sensitivity analyses for the whole of its operations, but may provide different types of sensitivity analysis for different classes of financial instruments.

Interest rate risk

AG24. *Interest rate risk* arises on interest-bearing financial instruments recognized in the statement of financial position (e.g. loans and receivables and debt instruments issued) and on some financial instruments not recognized in the statement of financial position (e.g. some loan commitments).

Currency risk

AG25. *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 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.

AG26. A sensitivity analysis is disclosed for each currency to which an entity has significant exposure.

Other price risk

- AG27. *Other price risk* arises on financial instruments because of changes in, for example, commodity prices or equity prices. To comply with paragraph 46, 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.
- AG28. Two examples of financial instruments that give rise to equity price risk are (a) a holding of equities in another entity and (b) an investment in a trust that 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.
- AG29. In accordance with paragraph 46(a), the sensitivity of surplus or deficit (that arises, for example, from instruments classified as at fair value through surplus or deficit and impairments of available-for-sale financial assets) is disclosed separately from the sensitivity of net assets/equity (that arises, for example, from instruments classified as available for sale).
- AG30. Financial instruments that an entity classifies as equity instruments are not remeasured. Neither surplus or deficit nor net assets/equity will be affected by the equity price risk of those instruments. Accordingly, no sensitivity analysis is required.

Appendix C

Amendments to other IPSASs

The amendments in this appendix shall be applied for annual financial statements covering periods beginning on or after Month Day Year. If an entity applies this Standard for an earlier period, these amendments shall be applied for that earlier period (deleted text is struck through and new text is underlined).

IPSAS 1 - Presentation of Financial Statements**Paragraph 75 is amended as follows:**

75. Information about expected dates of realization of assets and liabilities is useful in assessing the liquidity and solvency of an entity. ~~IPSAS 15, “Financial Instruments: Disclosure and Presentation”~~ IPSAS XX (ED 39), “Financial Instruments: Disclosures” requires disclosure of the maturity dates of financial assets and financial liabilities. Financial assets include trade and other receivables and financial liabilities include trade and other payables. Information on the expected date of recovery and settlement of non-monetary assets and liabilities such as inventories and provisions is also useful, whether or not assets and liabilities are classified as current or non-current.

Paragraph 129(d)(ii) is amended as follows:

129. (d) (ii) Non-financial disclosures, e.g. the entity’s financial risk management objectives and policies (see ~~IPSAS 15~~ IPSAS XX (ED 39)).
148. The disclosure of some of the key assumptions that would otherwise be required in accordance with paragraph 140 is required by other Standards. For example, IPSAS 19 requires disclosure, in specified circumstances, of major assumptions concerning future events affecting classes of provisions. ~~IPSAS 15~~ IPSAS XX (ED 39) requires disclosure of significant assumptions applied in estimating fair values of financial assets and financial liabilities that are carried at fair value. IPSAS 17 requires disclosure of significant assumptions applied in estimating fair values of revalued items of property, plant and equipment.

A new heading and paragraphs are inserted after paragraph 148 as follows:**Capital**

148A. An entity shall disclose information that enables users of its financial statements to evaluate the entity’s objectives, policies and processes for managing capital.

148B. To comply with paragraph 148A, the entity discloses the following:

- (a) Qualitative information about its objectives, policies and processes for managing capital, including (but not limited to):
- (i) A description of what it manages as capital;

- (ii) When an entity is subject to externally imposed capital requirements, the nature of those requirements and how those requirements are incorporated into the management of capital; and
- (iii) How it is meeting its objectives for managing capital.
- (b) Summary quantitative data about what it manages as capital. Some entities regard some financial liabilities (e.g. some forms of subordinated debt) as part of capital. Other entities regard capital as excluding some components of equity (e.g. components arising from cash flow hedges).
- (c) Any changes in (a) and (b) from the previous period.
- (d) Whether during the period it complied with any externally imposed capital requirements to which it is subject.
- (e) When the entity has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

These disclosures shall be based on the information provided internally to the entity's key management personnel.

148C. An entity may manage capital in a number of ways and be subject to a number of different capital requirements. For example, a conglomerate may include entities that undertake insurance activities and banking activities, and those entities may also operate in several jurisdictions. When an aggregate disclosure of capital requirements and how capital is managed would provide useful information or distorts a financial statement user's understanding of an entity's capital resources, the entity shall disclose separate information for each capital requirement to which the entity is subject.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, the proposed International Public Sector Accounting Standards.

Introduction

- BC1. This Basis for Conclusions summarizes the International Public Sector Accounting Standards Board's (IPSASB) considerations in reaching the conclusions in IPSAS XX (ED 39), "Financial Instruments: Disclosures". As this IPSAS is based on IFRS 7, "Financial Instruments: Disclosures" issued by the International Accounting Standards Board (IASB), the Basis for Conclusions outlines only those areas where IPSAS XX (ED 39) deviates from the main requirements of IFRS 7.
- BC2. This project on financial instruments is noted as a key part of the IPSASB's convergence program which aims to converge IPSASs with International Financial Reporting Standards (IFRSs).
- BC3. In developing this IPSAS, the IPSASB agreed to retain the existing text of IFRS 7 wherever consistent with existing IPSASs, except to deal with any public sector specific issues which result in adding or deleting disclosures.
- BC4. In September 2007 the IASB issued amendments to IAS 1, "Presentation of Financial Statements" which introduced a new component into the presentation of financial statements called "comprehensive income". As the IPSASB has not yet considered this, along with some of the other amendments proposed in IAS 1, those amendments have not been included in IPSAS XX (ED 39).

Concessionary Loans

- BC5. Concessionary loans are granted to or received by an entity on below market terms. Examples of concessionary loans granted by entities include loans to developing countries, small farms, student loans granted to qualifying students for tertiary education and housing loans granted to low income families. Such loans are a feature of the public sector and are often made to implement a government's or other public sector entity's social policies. The intention of a concessionary loan at the outset is to provide or receive resources on below market terms. For this reason the IPSASB concluded that more comprehensive disclosures are required by public sector entities in respect of concessionary loans and have included additional disclosure requirements in respect of concessionary loans.

**GUIDANCE ON IMPLEMENTING IPSAS XX (ED 39),
“FINANCIAL INSTRUMENTS: DISCLOSURES”**

CONTENTS

	Paragraphs
Introduction	IG1–IG4
Materiality.....	IG3–IG4
Classes of Financial Instruments and Level of Disclosure	IG5–IG6
Significance of Financial Instruments for Financial Position and Financial Performance	IG7–IG16
Financial Liabilities at Fair Value through Surplus or Deficit	IG7–IG11
Defaults and Breaches.....	IG12
Total Interest Expense.....	IG13
Fair Value.....	IG14–IG16
Nature and Extent of Risks Arising from Financial Instruments	IG17–IG40
Qualitative Disclosures	IG17–IG19
Quantitative Disclosures	IG20–IG40
Credit Risk	IG23–IG31
Collateral and Other Credit Enhancements Pledged	IG24
Credit Quality.....	IG25–IG27
Financial Assets that are either Past Due or Impaired	IG28–IG31
Market Risk.....	IG32–IG40
Other Market Risk Disclosures.....	IG37–IG40
Transition	IG41
Appendix	

Implementation Guidance IPSAS XX (ED 39), “Financial Instruments: Disclosures”

This guidance accompanies, but is not part of, IPSAS XX (ED 39).

Introduction

- IG1. This guidance suggests possible ways to apply some of the disclosure requirements in ED 39. The guidance does not create additional requirements.
- IG2. For convenience, each disclosure requirement in the Standard 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. IPSAS 1, “Presentation of Financial Statements” notes that a specific disclosure requirement in an IPSAS need not be satisfied if the information is not material. IPSAS 1 defines materiality as follows:

Omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments made 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 nature or size of the item, or a combination of both, could be the determining factor.

- IG4. IPSAS 1 also explains that definition as follows:

Assessing whether an omission or misstatement could influence decisions of users, and so be material, requires consideration of the characteristics of those users. ‘Users are assumed to have a reasonable knowledge of the public sector and economic activities and accounting and a willingness to 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 and evaluating decisions.’

Classes of Financial Instruments and Level of Disclosure (Paragraphs 8 and AG1–AG3)

- IG5. Paragraph AG3 states that ‘an entity decides in the light of its circumstances how much detail it provides to satisfy the requirements of this Standard, 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. Paragraph 29(c) of IPSAS 1 requires an entity to ‘provide additional disclosures when compliance with the specific requirements in IPSASs is insufficient to enable users to

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 Financial Performance (Paragraphs 9-35, AG4 and AG5)

Financial liabilities at fair value through surplus or deficit (paragraphs 12(a)(i) and AG4)

- IG7. The following example illustrates the calculation that an entity might perform in accordance with paragraph AG4 of Appendix B of the Standard.
- IG8. On January 1, 20X1, an entity issues a 10-year bond with a par value of CU150,000 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 LIBOR as its observable (benchmark) interest rate. At the date of inception of the bond, LIBOR is 5 per cent. At the end of the first year:
 - (a) LIBOR has decreased to 4.75 per cent.
 - (b) The fair value for the bond is CU153,811, consistent with an interest rate of 7.6 per cent.*
- 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 LIBOR 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:

<p>[paragraph AG4(a)]</p> <p>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.</p> <p>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.</p>	<p>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.</p> <p>Because the observed (benchmark) interest rate (LIBOR) is 5 per cent, the instrument-specific component of the internal rate of return is 3 per cent.</p>
<p>[paragraph AG(b)]</p> <p>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</p>	<p>The contractual cash flows of the instrument at the end of the period are:</p> <ul style="list-style-type: none"> • Interest: CU12,000^a per year for

* This reflects a shift in LIBOR 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.

<p>period and (ii) the instrument-specific component of the internal rate of return as determined in accordance with paragraph AG4(a).</p>	<p>each of years 2–10.</p> <ul style="list-style-type: none"> Principal: CU150,000 in year 10. <p>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 LIBOR rate, plus the 3 per cent instrument-specific component.</p> <p>This gives a present value of CU152,367.^b</p>
<p>[paragraph AG4(c)]</p> <p>The difference between the observed market price of the liability at the end of the period and the amount determined in accordance with paragraph AG4(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.</p>	<p>The market price of the liability at the end of the period is CU153,811.^c</p> <p>Thus, the entity discloses CU1,444, which is CU153,811 – CU152,367, as the increase in fair value of the bond that is not attributable to changes in market conditions that give rise to market risk.</p>
<p>a $CU150,000 \times 8\% = CU12,000$</p>	
<p>b $PV = [CU12,000 \times (1 - (1 + 0.0775)^{-9})/0.0775] + CU150,000 \times (1 + 0.0775)^{-9}$</p>	
<p>c $market\ price = [CU12,000 \times (1 - (1 + 0.076)^{-9})/0.076] + CU150,000 \times (1 + 0.076)^{-9}$</p>	

Defaults and breaches (paragraphs 21 and 22)

IG12. Paragraphs 21 and 22 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 IPSAS 1.

Total interest expense (paragraph 23(b))

IG13. Total interest expense disclosed in accordance with paragraph 23(b) is a component of the finance costs, which paragraph 102(b) of IPSAS 1 requires to be presented separately in the statement of financial performance. The line item for finance costs may also include amounts associated with non-financial liabilities.

Fair value (paragraphs 30-33)

IG14. IPSAS XX (ED 39) requires disclosures about the level in the fair value hierarchy in which fair value measurements are categorized for assets and liabilities measured in the statement of financial position. A tabular format is required unless another format is more

appropriate. An entity might disclose the following for assets to comply with paragraph 32(a). (Disclosure of comparative information is also required, but is not included in the following example.)

Assets measured at fair value				
Description	Dec 31 20X2	Fair value measurement at end of the reporting period using:		
		Level 1	Level 2	Level 3
		CU million	CU million	CU million
Financial assets at fair value through surplus or deficit				
Trading securities	100	40	55	5
Trading derivatives	39	17	20	2
Available-for-sale financial assets				
Equity investments	75	30	40	5
Total	214	87	115	12

(Note: For liabilities, a similar table might be presented.)

- IG15. IPSAS XX (ED 39) requires a reconciliation from beginning to ending balances for those assets and liabilities that are measured in the statement of financial position at fair value based on a valuation technique for which any significant input is not based on observable market data (Level 3). A tabular format is required unless another format is more appropriate. An entity might disclose the following for assets to comply with paragraph 32(b). (Disclosure of comparative information is also required, but is not included in the following example.)

Assets measured at fair value based on Level 3	Fair value measurement at the end of the reporting period			Total
	Financial assets at fair value through surplus or deficit		Available-for-sale financial assets	
	Trading securities	Trading derivatives	Equity investments	
	CU million	CU million	CU million	
Opening balance	6	5	4	15
Total gains or losses in surplus or deficit in net assets/equity	(2)	(2)	-	(4)
Purchases, issues and settlements (net)	1	2	2	5
Issues	-	-	-	-
Settlements	-	(1)	-	(1)
Transfers into and/or out of Level 3	-	(2)	-	(2)
Closing balance	5	2	5	12
Total gains or losses for the period included in surplus or deficit for assets held at the end of the reporting period	(1)	(1)	-	(2)
(Note: For liabilities, a similar table might be presented.)				
Gains or losses included in surplus or deficit for the period (above) are presented in revenue as follows:				
Total gains or losses included in surplus or deficit for the period	Revenue			(4)
Total gains or losses for the period included in surplus or deficit for assets held at the end of the reporting period				(2)
(Note: For liabilities, a similar table might be presented.)				

IG16. The fair value at initial recognition of financial instruments that are not traded in active markets is determined in accordance with paragraph AG107 of IPSAS XX (ED 38). 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 recognized in surplus or deficit in subsequent periods in accordance with IPSAS XX (ED 38) 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 AG108 of IPSAS XX (ED 38)). Paragraph 33 requires disclosures in these circumstances. An entity might disclose the following to comply with paragraph 33:

Background

On January 1 20X1 an entity purchases for CU15 million financial assets that are not traded in an active market. The entity has only one class of such financial assets.

The transaction price of CU15 million 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 CU14 million, which differs from fair value by CU1 million.

The entity has existing differences of CU5 million at January 1 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 included in this example].

Differences may arise between the fair value at initial recognition (which, in accordance with IPSAS XX (ED 38), 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 IPSAS XX (ED 38), 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 recognized in surplus or deficit are as follows:

	Dec 31 X2	Dec 31 X1
	CU million	CU million
Balance at beginning of year	5.3	5.0
New transactions	–	1.0
Amounts recognized in surplus or deficit 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 37-48 and AG6-AG30)

Qualitative disclosures (paragraph 39)

IG17. The type of qualitative information an entity might disclose to meet the requirements in paragraph 39 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 organization 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.

IG18. 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.

IG19. In accordance with paragraph 39(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 40-48 and AG7-AG30)

IG20. Paragraph 40 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 realize 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.

- IG21. In accordance with paragraph AG8, 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.
- IG22. When quantitative information at the end of the reporting period is unrepresentative of the entity's exposure to risk during the period, paragraph 41 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 42-44, AG9 and AG10)

- IG23. Paragraph 42 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 42(b))

- IG24. Paragraph 42(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 IPSAS XX (ED 37));

- (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 42(c))

- IG25. Paragraph 42(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.
- IG26. 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.
- IG27. 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 43)

- IG28. 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.
- IG29. 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.
- IG30. Paragraph 43(a) requires an analysis by class of the age of financial assets that are past due but not impaired. An entity uses its judgment 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.

IG31. Paragraph 43(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.

Market risk (paragraphs 46-48 and AG19-AG30)

IG32. Paragraph 46(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 (i.e. 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 (e.g. 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 46(a) requires the sensitivity analysis to show the effect on surplus or deficit and net assets/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 revenue and expense;

- (b) Other line items of surplus or deficit (such as trading gains and losses); and
- (c) When applicable, net assets/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 46(a):

Interest rate risk

At December 31, 20X2, if interest rates at that date had been 10 basis points lower with all other variables held constant, surplus for the year would have been CU1.7 million (20X1—CU2.4 million) higher, arising mainly as a result of lower interest expense on variable borrowings, and other revenue would have been CU2.8 million (20X1—CU3.2 million) 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, surplus would have been CU1.5 million (20X1—CU2.1 million) lower, arising mainly as a result of higher interest expense on variable borrowings, revenue would have been CU3.0 million (20X1—CU3.4 million) lower, arising mainly as a result of a decrease in the fair value of fixed rate financial assets classified as available for sale. Surplus 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 December 31, 20X2, if the CU had weakened 10 per cent against the US dollar with all other variables held constant, surplus for the year would have been CU2.8 million (20X1—CU6.4 million) lower, revenue would have been CU1.2 million (20X1—CU1.1 million) higher. Conversely, if the CU had strengthened 10 per cent against the US dollar with all other variables held constant, surplus would have been CU2.8 million (20X1—CU6.4 million) higher, revenue would have been CU1.2 million (20X1—CU1.1 million) lower. The lower foreign currency exchange rate sensitivity in surplus in 20X2 compared with 20X1 is attributable to a reduction in foreign currency denominated debt. Net assets/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.

Paragraph 38(a) requires disclosure of a maturity analysis of liabilities.

Other market risk disclosures (paragraph 48)

IG37. Paragraph 48 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, e.g. options that remain out of (or in) the money for the chosen change in the risk variable;
- (b) Financial assets are illiquid, e.g. 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 (e.g. the options);
- (b) The effect on surplus or deficit 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 (e.g. 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 IG38(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 IG38(c), additional disclosure might include:

- (a) The nature of the security (e.g. entity name);
- (b) The extent of holding (e.g. 15 per cent of the issued shares);
- (c) The effect on surplus or deficit; and
- (d) How the entity hedges the risk.

Comparison with IFRS 7

IPSAS XX (ED 39), “Financial Instruments: Disclosures” is drawn primarily from IFRS 7, “Financial Instruments: Disclosures” (originally issued in 2005, including amendments to December 31, 2008). The main differences between IPSAS XX (ED 39) and IFRS 7 are as follows:

- IPSAS XX (ED 39) contains requirements related to concessionary loans. IFRS 7 does not require such disclosures.
- In certain instances, IPSAS XX (ED 39) uses different terminology from IFRS 7. The most significant examples are the use of the terms “revenue,” “statement of financial performance” and “net assets/equity” in IPSAS XX (ED 39). The equivalent terms in IFRS 7 are “income,” “statement of comprehensive income” and “equity.”



International Federation of Accountants

545 Fifth Avenue, 14th Floor, New York, NY 10017 USA

Tel +1 (212) 286-9344 Fax +1(212) 286-9570 www.ifac.org