

# HKAS 32, HKAS 39 and HKFRS 7 (Part 2)

10 October 2008



**Nelson Lam 林智遠**  
MBA MSc BBA ACA ACIS CFA CPA(Aust.)  
CPA(US) FCCA FCPA(Practising) MSCA

© 2006-08 Nelson

1

## Today's Agenda



### Derivatives

- Accounting for derivatives and embedded derivatives

### Derecognition

- Derecognition is allowed if conditions are met

### Hedging

- Type of hedge and hedge accounting

### Presentation (IAS 32)

- Presentation of financial instruments, incl. to separate financial liabilities from equity

### Disclosure (IFRS 7)

- Disclosure of the significance and nature of risks arising from financial instruments

© 2006-08 Nelson

2

# Today's Agenda



## Derivatives

- Accounting for derivatives and embedded derivatives

# Derivative & Embedded Derivative

## Derivative

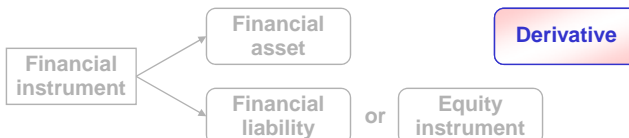
⇒ is a financial instrument or other contract within the scope of IAS 39 with all 3 of the following characteristics:

Value change based on an underlying

Little or no initial net investment

Settled at a future date

- its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable (sometimes called the 'underlying');
- it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and
- it is settled at a future date.



# Derivative & Embedded Derivative

Example

## Derivative

Typical example:

- Future and forward
- Swap and options

Value change based on an underlying

Little or no initial net investment

Settled at a future date

Type of contract	Underlying variable
Interest Rate Swap	Interest rates
Currency Swap (Foreign Exchange Swap)	Currency rates
Commodity Swap	Commodity prices
Equity Swap	Equity prices (equity of another entity)
Credit Swap	Credit rating, credit index or credit price
Total Return Swap	Total fair value of the reference asset and interest rates
Purchased or Written Treasury Bond Option	Interest rates
Purchased or Written Currency Option	Currency rates
Currency Futures/Forward	Currency rates
Commodity Futures/Forward	Commodity prices
Equity Forward	Equity prices

© 2006-08 Nelson

5

# Derivative & Embedded Derivative

## Derivative

- What is the initial measurement and subsequent measurement on derivative?

### Initial measurement

- Similar to other financial assets and liabilities
  - Fair value plus transaction cost, except for those classified at fair value through profit or loss
- But, a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument) is classified as fair value through profit or loss
  - Implies fair value only

### Subsequent measurement

- As above, derivative, other than a financial guarantee contract or a designated and effective hedging instrument, is
  - classified and measured at fair value through profit or loss

© 2006-08 Nelson

6

# Derivative & Embedded Derivative

## Case

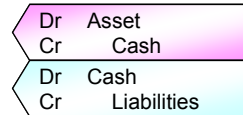
Ping An Insurance (Group) Co. of China, Ltd.



• Accounting report 2006

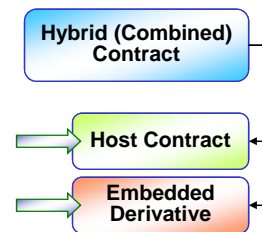
Derivative financial instruments

- Derivative financial instruments include
  - options embedded in convertible bonds purchased by the Group,
  - derivatives embedded in certain insurance contracts,
  - interest rate swaps and futures,
  - credit default swaps,
  - cross currency swaps,
  - forward currency contracts, and
  - options on interest rates, currencies and equities, etc.
- Derivative financial instruments are classified as held for trading
  - unless they are designated as effective hedging instruments.
- All derivatives are carried
  - as assets when the fair values are positive and
  - as liabilities when the fair values are negative.



# Derivative & Embedded Derivative

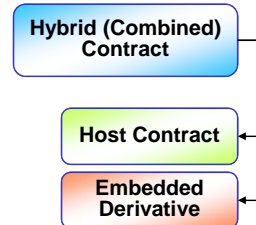
- A holder of a hybrid (combined) instrument is required to evaluate whether the embedded derivative should be separately accounted for in accordance with IAS 39.
- A hybrid instrument includes
  - a non-derivative host contract and
  - an embedded derivative with the effect that some of the cash flows of the hybrid instrument vary in a way similar to a stand-alone derivative.
- However, a derivative that is attached to a financial instrument but is contractually transferable independently of that instrument, or has a different counterparty from that instrument, is not an embedded derivative, but a separate financial instrument.



# Derivative & Embedded Derivative

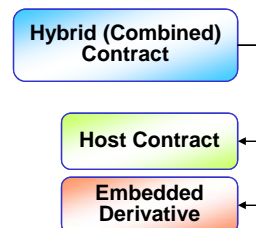
## Example

- Examples of contract with embedded derivative include:
  1. A call, put, or prepayment option embedded in a host debt contract.
  2. An option or automatic provision to extend the remaining term to maturity of a debt instrument.
  3. Equity-indexed interest or principal payments embedded in a host debt instrument.
  4. Commodity-indexed interest or principal payments embedded in a host debt instrument.
  5. An equity conversion feature embedded in a convertible debt instrument.

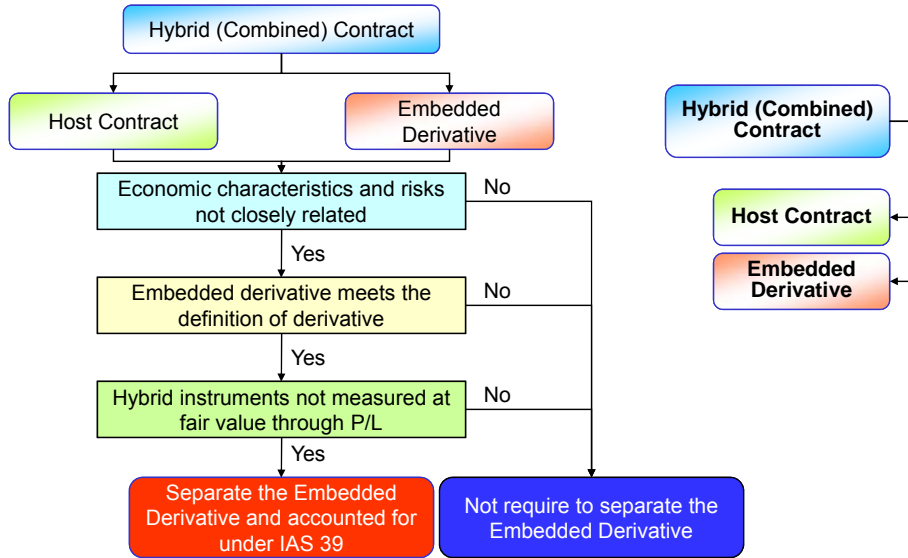


# Derivative & Embedded Derivative

- IAS 39 requires an entity to separate an embedded derivative from the host contract and account for such embedded derivative as a derivative if, and only if:
  1. the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract;
  2. a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and
  3. the hybrid instrument is not measured at fair value with changes in fair value recognised in profit or loss (i.e. a derivative that is embedded in a financial asset or financial liability at fair value through profit or loss is not separated).

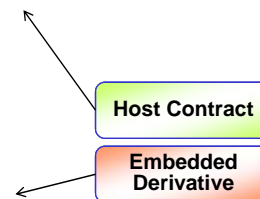


# Derivative & Embedded Derivative



# Derivative & Embedded Derivative

- If an embedded derivative is separated, the host contract is accounted for
  - under IAS 39 if it is a financial instrument, and
  - in accordance with other appropriate accounting standards if it is not a financial instrument.
- IAS 39 does not address whether an embedded derivative is presented separately on the face of the financial statements.
- The separated embedded derivative is similar to a simple derivative to be accounted for in the same manner as other derivatives.



## Derivative & Embedded Derivative

- If a contract contains one or more embedded derivatives, an entity may designate the entire hybrid (combined) contract as a financial asset or financial liability at fair value through profit or loss unless:

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

Hybrid (Combined)  
Contract

## Derivative & Embedded Derivative

- If an entity is required by IAS 39 to separate an embedded derivative from its host contract, but is unable to measure the embedded derivative separately (either at acquisition or subsequently),
  - the entity is required to designate the entire hybrid contract as at fair value through profit or loss.

Hybrid (Combined)  
Contract

# Derivative & Embedded Derivative

## Example

### Capital protection bond, guarantee fund or bond with index-linked interest

Can a bond with a fixed payment at maturity and a fixed maturity date be classified as a held-to-maturity investment if the bond's interest payments are indexed to the price of a commodity or equity, and the entity has the positive intention and ability to hold the bond to maturity?

Yes, but .....

- The commodity-indexed or equity-indexed interest payments result in an embedded derivative that is separated and accounted for as a derivative at fair value (IAS 39.11).
- IAS 39.12 (stated at fair value through profit or loss) is not applicable
  - since it should be straightforward to separate the host debt investment (the fixed payment at maturity) from the embedded derivative (the index-linked interest payments).

## Today's Agenda



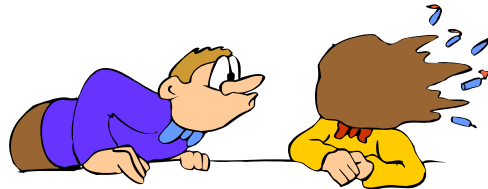
### Derecognition

- Derecognition is allowed if conditions are met



## Derecognition of Financial Asset

- Derecognition is the removal of a previously recognised financial asset or financial liability from an entity's balance sheet.
  - Derecognition of an asset or a liability is originally a simple concept.
- Practically, it is not that simple for financial assets and financial liabilities.
  - Even a financial asset or a financial liability had been transferred, either or both the risk and reward and control of the financial asset or the obligation of the financial liability might have not been transferred.
  - IAS 39 sets out detailed derecognition criteria and requirements on financial assets and financial liabilities separately.



© 2006-08 Nelson

Sourced from *Intermediate Financial Reporting (2008)* by Nelson Lam and Peter Lau

17

## Derecognition of Financial Asset

- The general derecognition criteria in accordance with IAS 39 require an entity to derecognise a financial asset when, and only when:
  1. the contractual rights to the cash flows from the financial asset expire; or
  2. the entity transfers the financial asset that meet the conditions set out in IAS 39 (i.e. "asset transfer test") and the transfer qualifies for derecognition in accordance with IAS 39 (i.e. the "risks and rewards test", and the "control test")

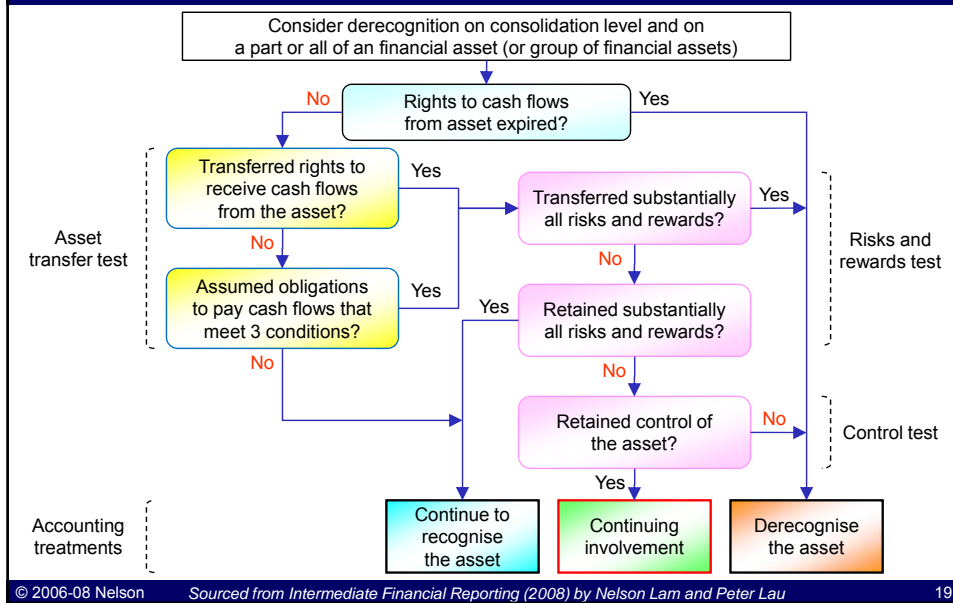


© 2006-08 Nelson

Sourced from *Intermediate Financial Reporting (2008)* by Nelson Lam and Peter Lau

18

# Derecognition of Financial Asset



# Derecognition of Financial Asset

## Example

- a) an unconditional sale of a financial asset;
- b) a sale of a financial asset together with an option to repurchase the financial asset at its fair value at the time of repurchase; and
- c) a sale of a financial asset together with a put or call option that is deeply out of the money (i.e. an option that is so far out of the money it is highly unlikely to go into the money before expiry).

Transferred substantially all risks and rewards?

Retained substantially all risks and rewards?

- a) a sale & repurchase transaction where the repurchase price is a fixed price or a sale price plus a lender's return;
- b) a securities lending agreement
- c) a sale of a financial asset together with a total return swap that transfers the market risk exposure back to the entity
- d) a sale of a financial asset together with a deep in-the-money put/call option
- e) a sale of short-term receivables in which the entity guarantees to compensate the buyer for any credit losses

## Derecognition of Financial Asset

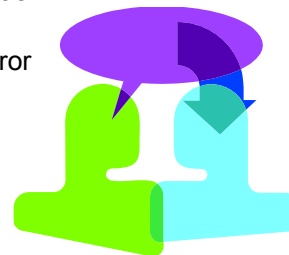
- By applying the risks and rewards test together with the control test on a derecognition transaction:

Findings of risks & rewards test and control test	Corresponding accounting treatments
1. Transfers substantially all the risks and rewards of ownership	Transfer qualified for derecognition <ul style="list-style-type: none"> <li>To derecognise the financial asset</li> <li>To recognise separately as assets/liabilities any rights &amp; obligations created/retained in the transfer</li> </ul>
2. Retains substantially all the risks and rewards of ownership	Transfer not qualified for derecognition <ul style="list-style-type: none"> <li>To continue to recognise the financial asset</li> </ul>
3. Neither transfers nor retains substantially all the risks and rewards of ownership and not retained control	Transfer qualified for derecognition <ul style="list-style-type: none"> <li>To derecognise the financial asset</li> <li>To recognise separately as assets/liabilities any rights &amp; obligations created/retained in the transfer</li> </ul>
4. Neither transfers nor retains substantially all the risks and rewards of ownership but retained control	Continuing involvement <ul style="list-style-type: none"> <li>To continuously recognise the financial asset to the extent of its continuing involvement in the asset</li> <li>To recognise an associate liability</li> </ul>

## Derecognition of Financial Asset

### Requirements for All Transfers

- If a transferred asset continues to be recognised,
  - the asset and the associated liability cannot be offset.
- Similarly, the entity is not allowed to offset any income arising from the transferred asset with any expense incurred on the associated liability.
- If a transferor provides non-cash collateral (such as debt or equity instruments) to the transferee,
  - the accounting for the collateral by the transferor and the transferee depends on whether the transferee has the right to sell or repledge the collateral and on whether the transferor has defaulted.



## Derecognition of Financial Liability

- An entity is required to remove a financial liability (or a part of a financial liability) from its balance sheet (i.e. derecognise a financial liability) when, and only when, it is extinguished.
  - IAS 39 explains that a financial liability is extinguished
    - when the obligation specified in the contract is discharged or cancelled or expires.
- A financial liability or part of it is extinguished when the debtor either:
  1. discharges the liability or part of it by paying the creditor, normally with cash, other financial assets, goods or services; or
  2. is legally released from primary responsibility for the liability (or part of it) either by process of law or by the creditor.



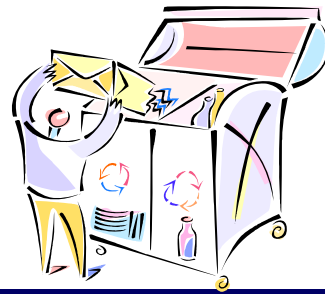
## Derecognition of Financial Liability

- When there is an exchange between an existing borrower and lender of debt instruments with substantially different terms or a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor),
  - such an exchange of debt instruments or substantial modification of terms is accounted for as:
    - an extinguishment of the original financial liability and
    - the recognition of a new financial liability.



## Derecognition of Financial Liability

- The recognition of a new financial liability
  - implies that the new liability is measured at fair value plus transaction costs at the date of extinguishment.
- The difference between
  - the carrying amount of a financial liability (or part of it) extinguished or transferred to another party and
  - the consideration paid, including any non-cash assets transferred or liabilities assumed,is recognised in profit or loss.



## Today's Agenda



Hedging

- Type of hedge and hedge accounting

# Hedging – Introduction

A Hedge under IAS 39 involves 2 components

Hedging Instrument

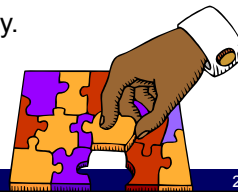
Hedged Item

- Strict conditions must be fulfilled before **Hedge Accounting** can be used.
- But even qualified, an entity can also choose not to use it, but .....

IAS 39 sets out **Hedge Accounting** which recognises the offsetting effects on profit or loss of changes in the fair values of these 2 components.

**Hedge Accounting** seeks to match the 2 sides of a **Hedging Relationship**, so as

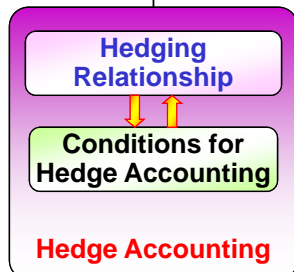
- to ensure both sides are offset and
- not to affect the income statements from one side only.



# Hedging – Introduction

Hedging Instrument

Hedged Item

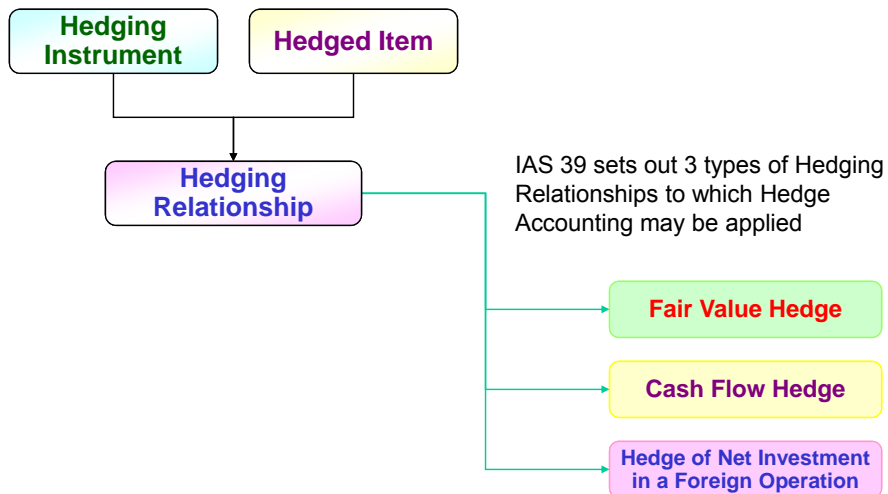


IAS 39

- defines and restricts the items qualified as
  - **Hedging Instruments** and
  - **Hedged Items**
- Sets out the types of **Hedge Relationship**
- Requires **Conditions for Hedge Accounting** must be fulfilled to qualify a hedge accounting
- Sets out the **Hedge Accounting**

If there is a designated **Hedging Relationship**, accounting for gain or loss on the **Hedging Instruments** and **Hedged Item** shall follow **Hedge Accounting**.

# Hedging – Hedge Relationship



# Hedging – Hedge Relationship

## Fair Value Hedge

A hedge of the exposure to changes in fair value of

- a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such items

that is attributable to a particular risk and could affect P/L

## Cash Flow Hedge

A hedge of the exposure to variability in cash flows that

- is attributable to a particular risk associated with a recognised asset or liability, or a highly probable forecast transaction and
- could affect profit or loss

A hedge of the foreign currency risk of a firm commitment may be accounted for

- as a fair value hedge or as a cash flow hedge

## Hedge of Net Investment in a Foreign Operation

Hedge of a net investment in a foreign operation is as defined in IAS 21 *The Effects of Changes in Foreign Exchange Rates*

# Hedging – Hedge Relationship

Example

Fair Value Hedge

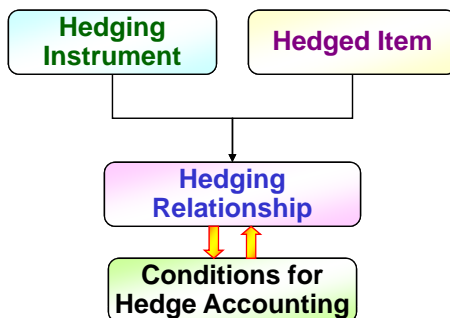
Cash Flow Hedge

Hedge of Net Investment  
in a Foreign Operation

Determine the classification for the following hedge:

- Entity A has a floating rate bond and enters into an interest rate swap by receiving fixed and paying float
- Entity B has a fixed rate bond and enters into an interest rate swap by receiving float and paying fixed
- Entity C issues a floating rate bond and enters into an interest rate swap by paying fixed and receiving float
- Entity D issues a floating rate bond and buys an interest rate cap

# Hedging – Hedge Accounting Conditions



A **Hedging Relationship** qualifies for **Hedge Accounting** if and only if all the **Conditions for Hedge Accounting** are met



## Hedging – Hedge Accounting Conditions

All 5 Conditions for Hedge Accounting must be met:

Formal documentation  
at inception

Highly effective and  
consistent with originally  
documented risk

Forecasted transaction  
to be highly probable  
(for cash flow hedge)

Hedge effectiveness can  
be reliably measured

Ongoing-assessed and  
actually highly effective

Conditions for  
Hedge Accounting

## Hedging – Hedge Accounting Conditions

Formal documentation  
at inception

- At the inception of the hedge, there is formal designation and documentation of:
  - the hedging relationship and
  - the entity's risk management objective and strategy for undertaking the hedge.
- That documentation shall include:
  - identification of the hedging instrument,
  - the hedged item or transaction,
  - the nature of the risk being hedged and
  - how the entity will assess
    - the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk.

Hedge  
Effectiveness

## Hedging – Hedge Accounting Conditions

For Cash Flow Hedges,

- a forecast transaction that is the subject of the hedge
  - must be highly probable and
  - must present an exposure to variations in cash flows that could ultimately affect profit or loss.

Forecasted transaction to be highly probable (for cash flow hedge)

## Hedging – Hedge Accounting Conditions

Measurable and highly effective hedge from the beginning to the end .....

Highly effective and consistent with originally documented risk

The hedge is **expected** to be **highly effective** in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, **consistently with the originally documented risk management strategy** for that particular hedging relationship.

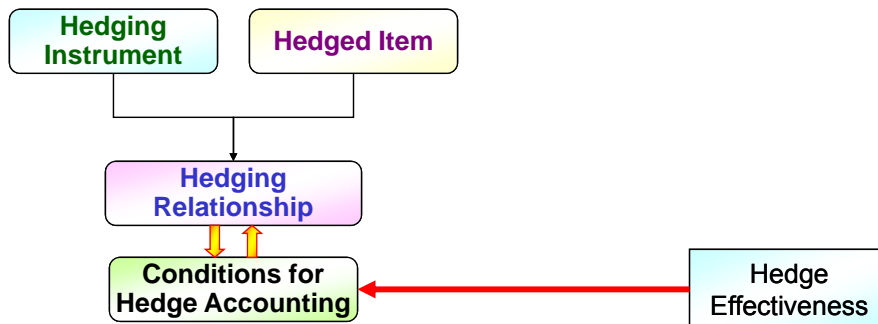
Hedge effectiveness can be reliably measured

The effectiveness of the hedge can be reliably measured, i.e. *the fair value or cash flows of the hedged item* that are attributable to the hedged risk and *the fair value of the hedging instrument* can be reliably measured.

Ongoing-assessed and actually highly effective

The hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated.

## Hedging – Assess Hedge Effectiveness



- **Hedge effectiveness** is the degree to which
  - changes in the fair value or cash flows of the hedged item that are attributable to a hedged risk
  - are offset by changes in the fair value or cash flows of the hedging instrument.

© 2006-08 Nelson

37

## Hedging – Assess Hedge Effectiveness

A hedge is regarded as **highly effective** only if both of the following conditions are met:

- Inception and Ongoing**  
Prospective testing
- a) At the inception of the hedge and in subsequent periods
- the hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated.
- Actual results**  
Retrospective testing
- b) The actual results of the hedge are within a range of 80% – 125%.
- Effectiveness is assessed, at a minimum, at the time an entity prepares its
- annual financial statements or
  - interim financial statements.

© 2006-08 Nelson

38

## Hedging – Assess Hedge Effectiveness

- The actual hedge effectiveness measurement may be based on either:
  - A period by period basis, or
  - A cumulative basis
- Such basis should be established in the hedge documentation and properly followed afterward.
- If a cumulative basis is used, hedge accounting will not be ceased even the hedge is not effective for a particular period.

Actual results

b) The actual results of the hedge are within a range of 80% – 125%.

Retrospective testing

Hedging Instrument

→ Gain is \$125

Hedged Item

→ Loss is \$100

- The degree of offset can be measured by either
  - $\$125 \div \$100$ , which is 125%, or
  - $\$100 \div \$125$ , which is 80%

within 80% to 125% range

## Hedging – Assess Hedge Effectiveness

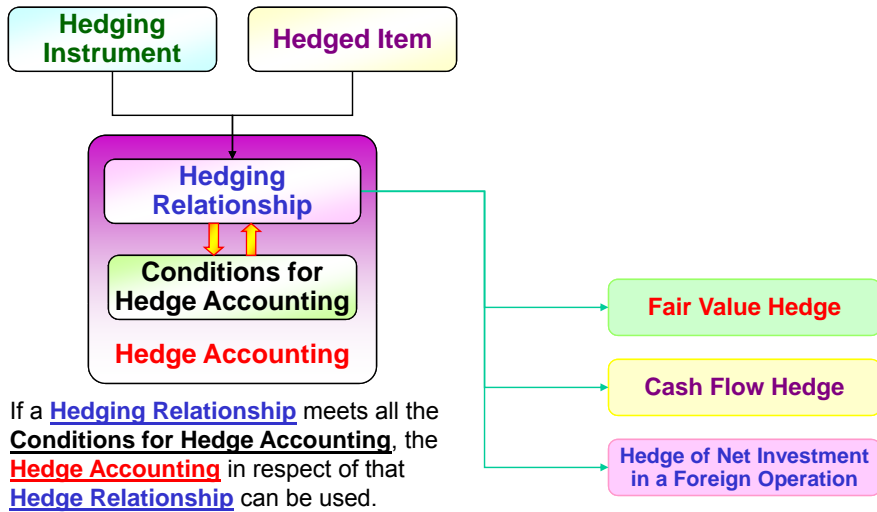
Case



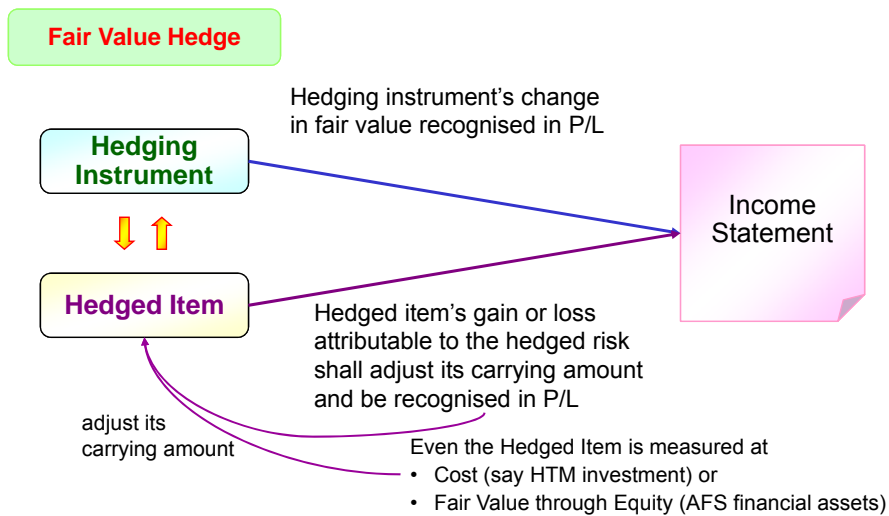
2005 Annual Financial Statements

- To qualify for hedge accounting, HSBC requires that at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective (prospective effectiveness). Actual effectiveness (retrospective effectiveness) must also be demonstrated on an ongoing basis.
- The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method an HSBC entity adopts for assessing hedge effectiveness will depend on its risk management strategy.
- For prospective effectiveness,
  - the hedging instrument must be expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated.
- For actual effectiveness,
  - the changes in fair value or cash flows must offset each other in the range of 80 per cent to 125 per cent for the hedge to be deemed effective.
- Hedge ineffectiveness is recognised in the income statement in 'Net trading income'.

# Hedging – Hedge Accounting



# Hedging – Hedge Accounting



## Hedging – Hedge Accounting

### Example

#### Interest Rate Swap on A Fixed Rate Financial Asset

- Company A purchases a bond that
  - has a principal amount of \$1 million at a fixed interest rate of 6% per year.
  - is classified as an available-for-sale financial asset.
  - has a fair value of \$1 million.
- The company enters into an interest rate swap.
  - It exchanges the fixed interest rate payments it receives on the bond for floating interest rate payments, in order to offset the risk of a decline in fair value.
  - It designates and documents the swap as a hedging instrument.
  - The swap has a fair value of zero at the inception of hedge.
- Assuming
  - The market interest rates have increased to 7% and the fair value of the bond will have decreased to \$960,000.
  - The fair value of the swap has increased by \$40,000.

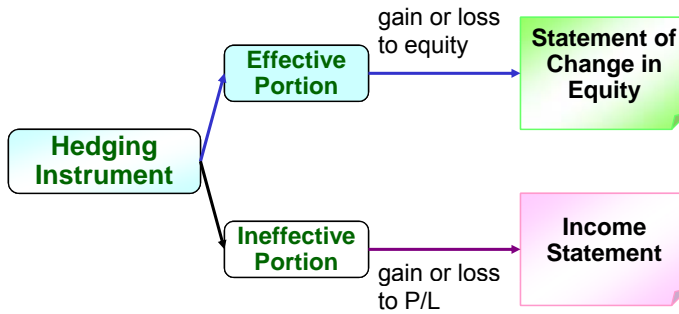
## Hedging – Hedge Accounting

### Example

- The instrument is classified as available-for-sale, therefore the decrease in fair value would normally be recorded directly in reserves.
- However, since the instrument is a Hedged Item in a Fair Value Hedge, this change in fair value of the instrument is recognised in profit or loss, as follows:
  - Dr Income statement                      \$40,000
  - Cr Available-for-sale financial asset    \$40,000
- While the swap is a derivative, it is measured at fair value with changes in fair value recognised in profit or loss.
  - Dr Swap receivables                      \$40,000
  - Cr Income statement                      \$40,000
- The changes in fair value of the Hedged Item and the Hedging Instrument exactly offset each other:
  - the hedge is 100% effective and the net effect on profit or loss is zero.

# Hedging – Hedge Accounting

## Cash Flow Hedge



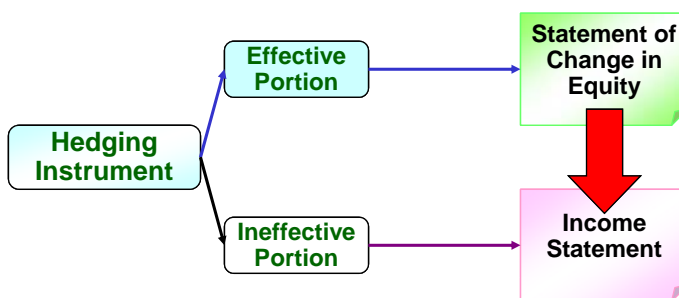
How's the treatment, if it is .....

Hedge of a forecast transaction resulting in recognition of **Financial Asset or Financial Liability**

Hedge of forecast transaction resulting in recognition of **Non-Financial Asset or Non-Financial Liability**

# Hedging – Hedge Accounting

## Cash Flow Hedge



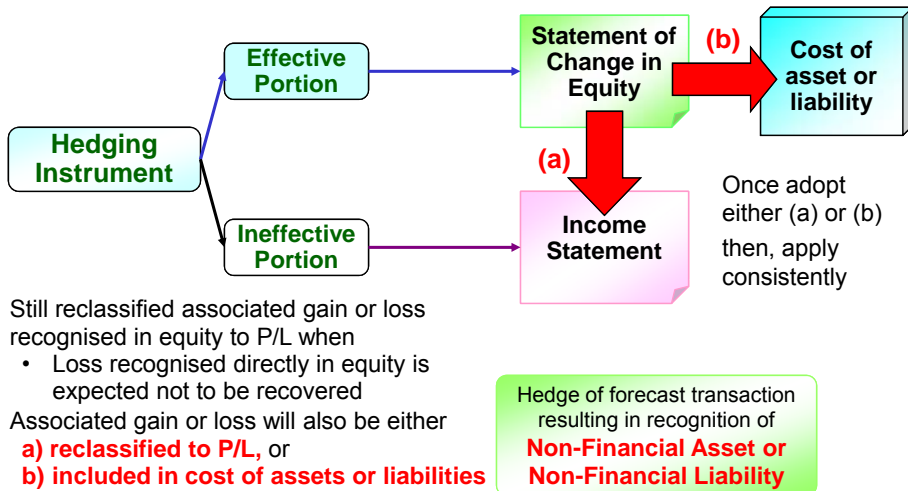
Hedge of a forecast transaction resulting in recognition of **Financial Asset or Financial Liability**

Reclassified associated gain or loss recognised in equity to P/L in case of

- Final recognition of financial assets or financial liabilities, or
- Loss recognised directly in equity is expected not to be recovered

# Hedging – Hedge Accounting

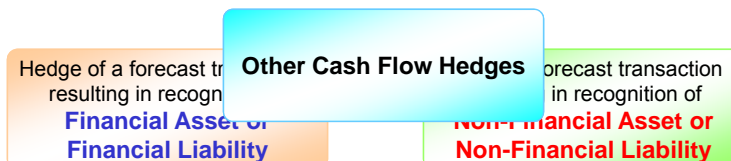
## Cash Flow Hedge



# Hedging – Hedge Accounting

## Cash Flow Hedge

- For cash flow hedges other than those discussed
  - amounts that had been recognised directly in equity shall be recognised in profit or loss in the same period(s) during which the hedged forecast transaction affects P/L (for example, when a forecast sale occurs).





# Hedging – Hedge Accounting

Example

## Hedge of Forecast Transaction

- Entity A trades in UK mainly in UK Sterling.
  - It expects to purchase a machine for 1 million Euros in one year from 1 May 2006.
  - In order to offset the risk of increases in the Euro rate, Entity A enters into a forward contract to purchase 1 million Euros in 1 year for a fixed amount (£650,000).
  - The forward contract is designated as a Cash Flow Hedge.
  - At inception, the forward contract has a fair value of zero.
- At the year-end of 31 October 2006
  - the Euro has appreciated and the value of 1 million Euros is £660,000.
  - The fair value of the forward contract rises to £10,000.
  - The machine will still cost 1 million Euros so the company concludes that the hedge is 100% effective.

# Hedging – Hedge Accounting

Example

- The entire change in the fair value of the hedging instrument is recognised directly in reserves.
 

Dr Forward contract	£10,000	
Cr Reserves		£10,000
- The forward contract is settled with no further change in the exchange rate:
 

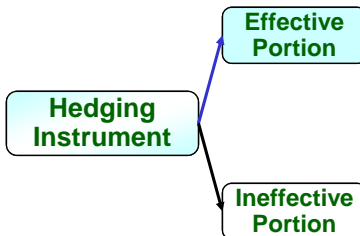
Dr Cash	£10,000	
Cr Forward contract		£10,000
- The company purchases the machine for 1 million euros and makes the following journal entry:
 

Dr Machine	£660,000	
Cr Accounts Payable		£660,000
- The gain of £10,000 recognised in reserve (equity) should either
  - be reclassified from equity into P/L, or
  - be reclassified from equity and included in the initial carrying amount of the machine (for non-financial assets or liabilities only)
  - once this policy is chosen, it must be used consistently

How to treat this amount finally?

# Hedging – Hedge Accounting

Hedge of Net Investment  
in a Foreign Operation



Including a hedge of a monetary item that is accounted for as part of the net investment, shall be accounted for similarly to **Cash Flow**

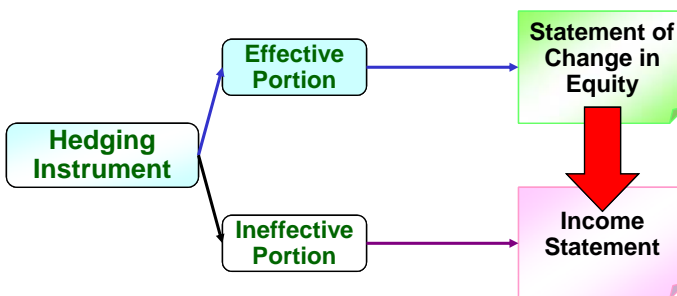
**Hedges:**

- a) the portion of the gain or loss on the **Hedging Instrument** that is determined to be an **effective hedge** shall be **recognised directly in equity** through the statement of changes in equity; and
- b) the **ineffective portion** shall be **recognised in profit or loss**.

The gain or loss on the hedging instrument relating to the effective portion of the hedge that has been recognised directly in equity shall be recognised in profit or loss on disposal of the foreign operation.

# Hedging – Hedge Accounting

Hedge of Net Investment  
in a Foreign Operation



Recognise in P/L  
on disposal of the  
foreign operation

## Hedge – Cease Hedge Accounting

An entity shall discontinue prospectively the **Hedge Accounting** if:

- a) the hedging instrument expires or is sold, terminated or exercised;
- b) the hedge no longer meets the **Conditions for Hedge Accounting**;
- c) the entity revokes the designation; or
- d) in case of a **Cash Flow Hedge**, the forecast transaction that is hedged is no longer expected to occur.

When the **Hedge Accounting** is discontinued (for **Cash Flow Hedge**), the cumulative gain or loss on the **Hedging Instrument** that remains recognised directly in equity shall:

- a) remain separately recognised in equity until the forecast transaction occurs; or
- b) be recognised in profit or loss if the forecast transaction is no longer expected to occur.

## Today's Agenda



### Presentation (IAS 32)

- Presentation of financial instruments, incl. to separate financial liabilities from equity

# IAS 32 – Presentation

Presentation from the perspective of the issuer on

Liability and equity

Compound financial instruments

Treasury shares

Interests, dividends, losses and gains

Offsetting

- The issuer of a financial instrument shall classify the instrument, or its component parts, on initial recognition as
  - a financial liability,
  - a financial asset or
  - an equity instrumentin accordance with
  - the substance of the contractual arrangement and
  - the definitions of a financial liability, a financial asset and an equity instrument. (*assess the substance*)

# IAS 32 – Presentation

Case

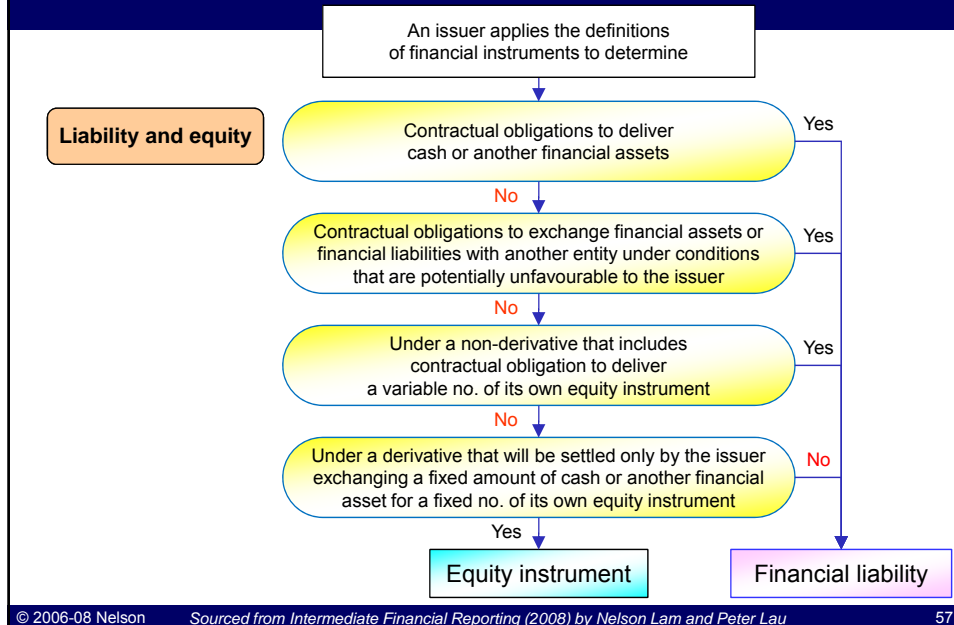


Annual report of 2005 sets out that it has probably had the following shares:

- Preference shares carry a mandatory coupon
- Preference shares are redeemable on a specific date or at the option of the shareholder
- Preference shares are redeemable at the option of the shareholder

How do you classify and present the above items?

## IAS 32 – Presentation



## IAS 32 – Presentation

Presentation from the perspective of the issuer on

**Compound financial instruments**

**Compound financial instrument** is an instrument containing both a liability and an equity component

- **IAS 32**
  - applies only to issuers of non-derivative compound financial instruments and
  - does not deal with compound financial instruments from the perspective of holders.
- **IAS 39**
  - deals with the separation of embedded derivatives from the perspective of holders of compound financial instruments that contain debt and equity features.

# IAS 32 – Presentation

Presentation from the perspective of the issuer on

Compound financial instruments



## Evaluation and Initial Classification

- The issuer of a non-derivative financial instrument shall evaluate the terms of the financial instruments
  - to determine whether it contains both a liability and an equity component.
- Such components shall be classified separately as financial liabilities, financial assets or equity instrument in accordance with
  - the substance of the contractual arrangement and
  - the definitions of a financial liability, financial asset and an equity instrument.
- An entity recognises separately the components of a financial instrument that
  - a) creates a financial liability of the entity, and
  - b) grants an option to the holder of the instrument to convert it into an equity instrument of the entity.

© 2006-08 Nelson

59

# IAS 32 – Presentation

Example

Presentation from the perspective of the issuer on

Compound financial instruments



- For example, a convertible bond allows the bondholder to convert it into a fixed no. of ordinary shares of the entity
  - is a compound financial instrument.
- From the perspective of the entity, such an instrument comprises two components:
  - 1) a financial liability – a contractual arrangement to deliver cash or another financial asset), and
  - 2) an equity instrument – a call option granting the holder the right, for a specified period of time, to convert it into a fixed no. of ordinary shares of the entity.
- The economic effect of issuing such an instrument is substantially the same as issuing a debt instrument with detachable share purchase warrants.
- In all cases, the entity presents the liability and equity components separately on its balance sheet.

© 2006-08 Nelson

60



## IAS 32 – Presentation

Presentation from the perspective of the issuer on

Interests, dividends,  
losses and gains

- Interest, dividends, losses and gains relating to a financial instrument or a component that is a financial liability
  - shall be recognised as income or expense in profit or loss.
- Distributions to holders of an equity instrument
  - shall be debited by the entity directly to equity, net of any related income tax benefit.
- Transaction costs of an equity transaction, other than costs of issuing an equity instrument that are directly attributable to the acquisition of a business,
  - shall be accounted for as a deduction from equity, net of any related income tax benefit.

## IAS 32 – Presentation

### Case



Annual report of 2005 sets out that:

- Preference shares, which
  - carry a mandatory coupon,
  - or are redeemable on a specific date
  - or at the option of the shareholder,are classified as financial liabilities and are presented in other borrowed funds.
- The dividends on these preference shares
  - are recognised in the income statement as interest expense on an amortised cost basis using the effective interest method.



# IAS 32 – Presentation

## Presentation from the perspective of the issuer on

### Offsetting

- Financial asset and a financial liability are offset and the net amount presented in the balance sheet when, and only when, an entity:
  1. currently has a legally enforceable right to set off the recognised amounts; and
  2. intends either
    - to settle on a net basis, or
    - to realise the asset and settle the liability simultaneously.
- In accounting for a transfer of a financial asset that does not qualify for derecognition,
  - the entity is not allowed to offset the transferred asset and the associated liability

## Today's Agenda



### Disclosure (IFRS 7)

- Disclosure of the significance and nature of risks arising from financial instruments

# IFRS 7 – Introduction

- The objective of IFRS 7 is to require entities to provide disclosures in their financial statements that enable users to evaluate:

1) the significance of financial instruments for the entity's

- financial position and
- financial performance; and

2) the nature and extent of risks arising from financial instruments to which the entity is exposed

- during the period and
  - at the reporting date, and
- how the entity manages those risks.

## Significance

- Balance sheet
- Income statement
- Other disclosures

## Nature and Extent

- Qualitative disclosures
- Quantitative disclosures

## 1. Significance of Financial Instruments

- 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.

## Significance

Balance Sheet

Income Statement and Equity

Other Disclosures



# 1. Significance of Financial Instruments

## Balance Sheet

The carrying amounts of each of the following categories, as defined in IAS 39, shall be disclosed either on the face of the balance sheet or in the notes:

- a) financial assets at fair value through P/L, showing separately
  - i) those designated as such upon initial recognition and
  - ii) those classified as held for trading in accordance with IAS 39;
- b) held-to-maturity investments;
- c) loans and receivables;
- d) available-for-sale financial assets;
- e) financial liabilities at fair value through P/L, showing separately
  - i) those designated as such upon initial recognition and
  - ii) those classified as held for trading in accordance with IAS 39; and
- f) financial liabilities measured at amortized cost.

# 1. Significance of Financial Instruments

## Case



	Financial assets at fair value through profit or loss held for trading RMB'000	Loans and receivables RMB'000	Available-for-sale financial assets RMB'000	Total RMB'000
Financial assets included in other assets (note 18)	-	80,000	-	80,000
Interests in associates (notes 22)	-	10,000	-	10,000
Interests in jointly-controlled entities (note 23)	-	19,128	-	19,128
Available-for-sale investments	-	-	462,178	462,178
Financial assets included in prepayments, deposits and other receivables	-	321,664	-	321,664
Trade receivables	-	293,870	-	293,870
Bills receivables	-	52,346	-	52,346
Equity investments at fair value through profit or loss	102,439	-	-	102,439
Derivative financial instruments	4,440	-	-	4,440
Pledged deposits	-	52,088	-	52,088
Cash and cash equivalents	-	2,184,510	-	2,184,510
	106,879	3,013,606	462,178	3,582,663

## 2. Nature and Extent of Risks



Significance

Nature and Extent

## 2. Nature and Extent of Risks

- 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 reporting date.
- The disclosures required focus on the risks that arise from financial instruments and how they have been managed.
- These risks typically include, but are not limited to

Market Risk

Credit Risk

Liquidity Risk



Nature and Extent

Qualitative Disclosures

Quantitative Disclosures

## 2. Nature and Extent of Risks

- The disclosures required 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.
- It implies that the disclosures requirements are required
  - not only on credit risk, liquidity risk and market risk
  - but also on other risks that may be identified by the entity for its financial instruments.

Qualitative Disclosures

Quantitative Disclosures

## 2. Nature and Extent of Risks

- The disclosures in respect of the nature and extent of risks arising from financial instruments can be either
  1. given in the financial statements or
  2. incorporated by cross-reference from the financial statements to some other statement, that is available to users of the financial statements
    - on the same terms as the financial statements and
    - at the same time.

e.g. risk report, or management commentary

Without the information incorporated by cross-reference, the financial statements are incomplete. (IFRS 7.BC46)

Qualitative Disclosures

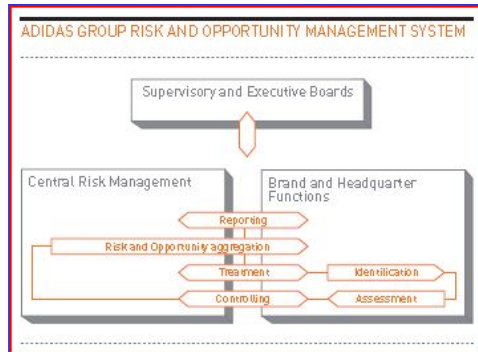
Quantitative Disclosures

## 2. Nature and Extent of Risks

### Example

- Adidas's 13-page
  - “Risk and Opportunity Report”
- HSBC's 97-page
  - “The Management of Risk” incorporated in the Report of Directors

e.g. risk report, or management commentary



Qualitative Disclosures

Quantitative Disclosures

© 2006-08 Nelson

75

## 2. Nature and Extent of Risks

### Qualitative Disclosures

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



© 2006-08 Nelson

76

## 2. Nature and Extent of Risks

### Quantitative Disclosures

- 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 reporting date.
    - The level of detail of such disclosure is based on the information provided internally to key management personnel of the entity (as defined in IAS 24 *Related Party Disclosures*), for example the entity's board of directors or chief executive officer.
  - b. the disclosures required in quantitative disclosures, to the extent not provided in (a), unless the risk is not material (see IAS 1.29-31).
  - c. concentrations of risk if not apparent from (a) and (b)



© 2006-08 Nelson

77

## 2. Nature and Extent of Risks

### Example

- Can an entity avoid disclosure of nature and extent of risk by
  - Unwinding a position of large exposure in a particular currency, or
  - Disposal of its large portfolio in equity instruments ?
- If the quantitative data disclosed as at the reporting date are unrepresentative of an entity's exposure to risk during the period, an entity is still required to provide further information that is representative.
- When an entity typically has a large exposure to a particular currency or an equity investments, 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 during the period. (IFRS 7.IG20)

© 2006-08 Nelson

78

## 2. Nature and Extent – Credit Risk

### Quantitative Disclosures

#### Credit risk

- An entity shall disclose by class of financial instrument:
  - a) the amount that best represents its maximum exposure to credit risk at the reporting date without taking account of any collateral held or other credit enhancements (e.g. netting agreements that do not qualify for offset in accordance with IAS 32);
  - 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.



## 2. Nature and Extent – Past Due

### Quantitative Disclosures

#### Financial assets that are either past due or impaired

- 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 reporting date but not impaired;
  - b) an analysis of financial assets that are individually determined to be impaired as at the reporting date, including the factors the entity considered in determining that they are impaired; and
  - c) for the amounts disclosed in (a) and (b), a description of collateral held by the entity as security and other credit enhancements and, unless impracticable, an estimate of their fair value.





## 2. Nature and Extent – Past Due

### Case

Early adopted HKFRS 7 in 2005 and its annual report 2006 states that (extract only):



(iv) Financial assets that were past due but not impaired

As at 31 December, the age analysis of the trade receivables of the Group that were past due but not determined to be impaired according to the period past due was as follows:

	Group	
	2006 \$'000	2005 \$'000
Up to 6 months	186,359	141,277
Over 6 months to 1 year	–	–
Over 1 year to 3 years *	–	8,521
Over 3 years *	8,651	142
<b>Total</b>	<b>195,010</b>	<b>149,940</b>

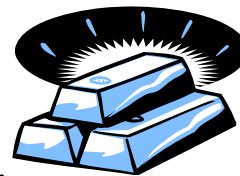
\* No provision for impairment losses has been made against trade receivables amounting to \$8,510,000 (2005: \$8,521,000) as the balances can be recovered from the Clearing House Funds.

## 2. Nature and Extent – Collateral

### Quantitative Disclosures

#### Collateral and other credit enhancements obtained

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



## 2. Nature and Extent – Liquidity Risk

### Quantitative Disclosures

#### Liquidity risk

- Before IFRS 7, contractual maturity analysis together with effective interest rate analysis was required by IAS 32 for interest rate risk disclosure.
- IFRS 7 now requires, for liquidity risk disclosure, an entity to disclose:
  - a) a maturity analysis for financial liabilities that shows the remaining contractual maturities; and
  - b) a description of how it manages the liquidity risk inherent in (a).



© 2006-08 Nelson

83

## 2. Nature and Extent – Liquidity Risk

### Case

Early adopted HKFRS 7 in 2005 and its annual report 2006 states that (extract only):



- The financial liabilities of the Group and HKEx as at 31 Dec. 2006 are analysed into relevant maturity buckets based on their contractual maturity dates in the table below:

	Group					Total
	2006					
	Up to 1 month \$'000	>1 month to 3 months \$'000	>3 months to 1 year \$'000	>1 year to 5 years \$'000	Not determinable \$'000	
Current liabilities						
Margin deposits from Clearing Participants on derivatives contracts	21,666,474	-	-	-	-	21,666,474
Accounts payable, accruals and other liabilities	11,042,527	45,937	234	363	18,139	11,107,200
Participants' admission fees received	700	50	600	-	350	1,700
	32,709,701	45,987	834	363	18,489	32,775,374

© 2006-08 Nelson

84

## 2. Nature and Extent – Market Risk

### Quantitative Disclosures

#### Market risk

- IFRS 7 requires the disclosures of sensitivity analysis.
- The disclosures of sensitivity analysis can be achieved by 2 approaches:
  - 1. Simple sensitivity analysis:**
    - sensitivity analysis for each type of market risk
  - 2. Interdependency sensitivity analysis:**
    - Sensitivity analysis that reflects interdependencies between risks variables



## 2. Nature and Extent – Market Risk

### Quantitative Disclosures

#### Market risk

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



## 2. Nature and Extent – Sensitivity

### Quantitative Disclosures

#### Market risk – Simple sensitivity analysis

- An entity shall disclose:
  - a) a sensitivity analysis for each type of market risk to which the entity is exposed at the reporting date, showing:
    - how profit or loss and equity would have been affected by changes in the relevant risk variable that were reasonably possible at that date;
  - b) the methods and assumptions used in preparing the sensitivity analysis; and
  - c) changes from the previous period in the methods and assumptions used, and the reasons for such changes.

Assuming that a **reasonably possible change** in the relevant risk variable had occurred at the balance sheet date and had been applied to the risk exposures in existence at that date.



## 2. Nature and Extent – Sensitivity

In order to disclose the simple sensitivity analysis, an entity should:

1. Decide how much detail it provides, how much emphasis it places and how it aggregates information to display
2. Identify each type of market risk to which the entity is exposed and the relevant risk variable at the reporting date
3. Judge the reasonably possible changes in the relevant risk variables at the reporting date
4. Calculate and show how profit or loss and equity would be affected at the reporting date

## 2. Nature and Extent – Sensitivity

In order to disclose the simple sensitivity analysis, an entity should:

1. Decide how much detail it provides, how much emphasis it places and how it aggregates information to display

## 2. Nature and Extent – Sensitivity

### Quantitative Disclosures

#### Market risk – Simple sensitivity analysis

- For each type of market risk, 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, an entity that trades financial instruments might disclose
  - Sensitivity analysis for each type of market risk separately for
    - financial instruments held for trading and
    - those not held for trading.
- If an entity has exposure to only one type of market risk in only one economic environment,
  - it would not show disaggregated information.

## 2. Nature and Extent – Sensitivity

In order to disclose the simple sensitivity analysis, an entity should:

1. Decide how much detail it provides, how much emphasis it places and how it aggregates information to display



2. Identify each type of market risk to which the entity is exposed and the relevant risk variable at the reporting date

## 2. Nature and Extent – Sensitivity

Market Risk

Interest Rate Risk

• Interest rate risk arises

- on interest-bearing financial instruments recognised in the balance sheet (e.g. loans and receivables and debt instruments issued) and
- on some financial instruments not recognised in the balance sheet (e.g. some loan commitments).

## 2. Nature and Extent – Sensitivity

Market Risk

Currency Risk

- **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 IFRS 7, currency risk does not arise from financial instruments that are non-monetary items or from financial instruments denominated in the functional currency.
  - A sensitivity analysis is disclosed for each currency to which an entity has significant exposure.

## 2. Nature and Extent – Sensitivity

Market Risk

Other Price Risk

- **Other price risk** arises on financial instruments because of changes in, for example:
  - commodity prices or
  - equity prices.
- To comply with IFRS 7, an entity might disclose the effect of a decrease in a specified variable, including:
  - 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.

## 2. Nature and Extent – Sensitivity

### Example

Market Risk

Other Price Risk

- 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.

## 2. Nature and Extent – Sensitivity

### Example

Market Risk

Interest Rate Risk

Currency Risk

Other Price Risk

Equity Price Risk

Commodity Price Risk

Prepayment Risk

Residual Value Risk

### Risk variables that are relevant to disclosing market risk

Yield curve of market interest rates

Foreign exchange rates

Prices of equity instruments

Market prices of commodities



## 2. Nature and Extent – Sensitivity

In order to disclose the simple sensitivity analysis, an entity should:

1. Decide how much detail it provides, how much emphasis it places and how it aggregates information to display

2. Identify each type of market risk to which the entity is exposed and the relevant risk variable at the reporting date

3. Judge the reasonably possible changes in the relevant risk variables at the reporting date

## 2. Nature and Extent – Sensitivity

### Quantitative Disclosures

#### Market risk – Simple sensitivity analysis

- 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.
  - b. the time frame over which it is making the assessment.

- 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.
- 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.

## 2. Nature and Extent – Sensitivity

### Case

How can it be reasonably possible change?

Observed assessments by certain companies:

<u>Entity name</u>	<u>Currency</u>	<u>Interest rate</u>	<u>Other price</u>
BASF	10% (drop only)	1%	10%
BP plc	VaR	VaR	10%
CLP Holdings Ltd.	1%	0.5%	15% (2006: 5%)
DBS Group	10%	0.25%	10%
Deutsche Telecom	10%	1%	N/M
France Telecom	10%	1%	N/M
Jardine Matheson Ltd.	10%	1%	25% (AFS)
Recruit	7 – 12%	N/M	N/M
Zijin Mining	10%	1%	N/M

## 2. Nature and Extent – Sensitivity

In order to disclose the simple sensitivity analysis, an entity should:

1. Decide how much detail it provides, how much emphasis it places and how it aggregates information to display
2. Identify each type of market risk to which the entity is exposed and the relevant risk variable at the reporting date
3. Judge the reasonably possible changes in the relevant risk variables at the reporting date
4. Calculate and show how profit or loss and equity would be affected at the reporting date

## 2. Nature and Extent – Sensitivity

- IFRS 7 requires the sensitivity analysis to show the effect on profit or loss and equity of reasonably possible changes in the relevant risk variable. For this purpose:
  1. Entities are not required to determine what the profit or loss for the period would have been if relevant risk variables had been different.
    - Instead, entities disclose the effect on profit or loss and equity at the balance sheet date assuming that a reasonably possible change in the relevant risk variable had occurred at the balance sheet date and had been applied to the risk exposures in existence at that date.
  2. Entities are not required to disclose the effect on profit or loss and equity for each change within a range of reasonably possible changes of the relevant risk variable.
    - Disclosure of the effects of the changes at the limits (i.e. the upper and lower limits) of the reasonably possible range would be sufficient.

## 2. Nature and Extent – Sensitivity

### Example

#### Market Risk

- IFRS 7 requires separate disclosure on
  - the sensitivity of profit or loss (that arises, for example, from instruments classified as at fair value through profit or loss and impairments of available-for-sale financial assets) is disclosed separately from
  - the sensitivity of equity (that arises, for example, from instruments classified as available for sale).
- Financial instruments that an entity classifies as equity instruments are not remeasured.
  - Neither profit or loss nor equity will be affected by the equity price risk of those instruments.
  - Accordingly, no sensitivity analysis is required.

## 2. Nature and Extent – Sensitivity

### Example

#### Example of financial assets and liabilities

- Investment in bonds, bank deposits, interest-bearing borrowings, bank loans

#### Risk variables that are relevant to disclosing market risk

Yield curve of market interest rates

- For interest rate risk, the sensitivity analysis might show separately the effect of a change in market interest rates on:
  - a) interest income and expense;
  - b) other line items of profit or loss (such as trading gains and losses); and
  - c) when applicable, equity.
- An entity might disclose a sensitivity analysis for interest rate risk for each currency in which the entity has material exposures to interest rate risk.

## 2. Nature and Extent – Sensitivity

### Quantitative Disclosures

#### Market risk – **Interdependency Sensitivity Analysis**

- An entity can alternatively prepare and disclose a sensitivity analysis, such as Value-at-Risk (VaR), that reflects interdependencies between risk variables (e.g. interest rates and exchange rates) so long as it uses such sensitivity analysis to manage financial risks.
- 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.

## 2. Nature and Extent – Sensitivity

### Quantitative Disclosures

#### Market risk – Interdependency Sensitivity Analysis

- An entity might comply the VaR methodology by disclosing
  - the type of VaR model used (eg whether the model relies on Monte Carlo simulations),
  - an explanation about how the model works and
  - the main assumptions (eg the holding period and confidence level).
- Entities might also disclose
  - the historical observation period and weightings applied to observations within that period,
  - an explanation of how options are dealt with in the calculations, and
  - which volatilities and correlations (or, alternatively, Monte Carlo probability distribution simulations) are used.

## 2. Nature and Extent – Sensitivity

### Case



#### Royal Dutch Shell plc for 2007

- Shell uses risk management systems for recording and valuing instruments.
- There is regular review of mandated trading limits by senior management, daily monitoring of market risk exposure using value-at-risk (VAR) techniques (see below), daily monitoring of trading positions against limits and marking-to-market of trading exposures with a department independent of traders reviewing the market values applied to trading exposures.
- Shell's exposure to substantial trading losses is therefore considered limited.
- Shell utilises VAR techniques based on variance/covariance or Monte Carlo simulation models and make a statistical assessment of the market risk arising from possible future changes in market values over a 24-hour period and within a 95% confidence level.
- The calculation of the range of potential changes in fair value takes into account positions, the history of price movements and the correlation of these price movements.
- Each of the models is regularly back tested against actual fair value movements to ensure model integrity is maintained.

## 2. Nature and Extent – Sensitivity

### Case



Royal Dutch Shell plc for 2007

VALUE-AT-RISK (pre-tax) \$ million	2007			2006				
	High	Low	Average	Year end	High	Low	Average	Year end
Oil Products and Chemicals	23	5	13	19	21	6	13	11
Gas & Power	20	6	11	7	16	4	9	9

## 2. Nature and Extent – Sensitivity

### Case

Reference to the time horizon and confidence level of some entities used in VaR analysis for 2007.....

Entity name	Time horizon	Confidence	Method	Coverage
BASF	1 day	95%	VC	Commodity
BMW	3 months	99%	HS	Interest
BP plc	24 hours	95%	VC or HS	Market risk
CLP	4 weeks	95%	VC	Energy price
DBS Group	1 day	99%	HS	Trading market risk
HKEx	10 day	95%	HS	Market risk
HSBC	1 day	99%	HS	Market risk
Nokia	1 month	95%	VC or MC	Market risk
Shell	24 hours	95%	VC or MC	Price risk
Standard Chartered	1 day	97.5%	HS	Trading book

*Variance-Covariance (VS), Historical simulation (HS) and Monte Carlo simulation (MC)*

# HKAS 32, HKAS 39 and HKFRS 7

(Part 2)

10 October 2008



Full set of slides in PDF can be found in  
[www.NelsonCPA.com.hk](http://www.NelsonCPA.com.hk)

**Nelson Lam 林智遠**

[nelson@nelsoncpa.com.hk](mailto:nelson@nelsoncpa.com.hk)  
[www.nelsoncpa.com.hk](http://www.nelsoncpa.com.hk)

© 2006-08 Nelson

109

# HKAS 32, HKAS 39 and HKFRS 7

(Part 2)

10 October 2008

Full set of slides in PDF can be found in  
[www.NelsonCPA.com.hk](http://www.NelsonCPA.com.hk)



**Nelson Lam 林智遠**

[nelson@nelsoncpa.com.hk](mailto:nelson@nelsoncpa.com.hk)  
[www.nelsoncpa.com.hk](http://www.nelsoncpa.com.hk)

© 2006-08 Nelson

110