GOVERNMENT OF MALAYSIA

Federal Government Accrual Accounting Manual

FINANCIAL INSTRUMENTS

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Version No.	Effective Date	Approval	Details of Changes	
			Section Reference	Description of Changes

19.0 FINANCIAL INSTRUMENTS

Introduction

19.1 This chapter covers the following matters:

- Different types of financial instruments (Financial assets and liabilities)
- Initial recognition and measurement
- Measurement subsequent to initial recognition
- Derecognition
- Impairment of financial assets
- Financial instruments denominated in foreign currency
- Concessionary loans
- Securitization of loans and accounts receivable
- Disclosure requirements

19.2 A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability of another entity.

19.3 Financial assets are classified as either of the following:

(a) Loans and receivables
(b) Financial assets 'at fair value through surplus or deficit'
(c) Held to maturity investments
(d) Available for sale assets

19.4 Financial liabilities are classified as either of the following:

(a) Financial liabilities 'at fair value through surplus or deficit'
(b) Other financial liabilities (at amortised cost)
(c) Financial guarantee contacts

Types of financial assets

<u>Loans and Receivables</u>

19.5 Loans and receivables are financial assets with a fixed or determinable payment which are not quoted in an active market. It arises when an entity provides money, goods or services directly to a debtor with no intention of trading the receivable.

19.6 Examples include account receivables, loans (computer, housing, car, educational or staff loans given) and deposits with licensed banks.

19.7 Accounts receivables are classified as short-term receivables that are normally, but not necessarily, expected to be collected within a year. Accounts receivables may include trade and non-trade receivables. The former represents amounts owed by customers for goods sold and services rendered as part of normal operations. The latter arises from a variety of transactions including return on investments (dividends), interest income, and refund of overpayments and recoveries.

19.8 Accrued receivables should be set up for estimated amounts for goods or services rendered but not recorded at the end of each month, for any material amounts. These should be subsequently reversed when definitive amounts are known, at which time an accounts receivable is set up.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Financial assets 'at fair value through surplus or deficit'

19.9 A financial asset at fair value through surplus or deficit is a financial asset that meets either of the following conditions:

(a) It is classified as held for trading. A financial asset is classified as held for trading if it is:
   (i) Acquired or incurred principally for the purpose of selling or repurchasing it in the near term;
   (ii) On initial recognition part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking; or
   (iii) A derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument).

(b) Upon initial recognition it is designated by the entity as at fair value through surpluses or deficit.

19.10 Financial assets at fair value through surplus or deficit include for example investments in shares and foreign government securities, assuming the above conditions are met.

Held to maturity investments

19.11 Held-to-maturity assets are non-derivative financial assets with fixed or determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity other than:

(a) Those that the entity upon initial recognition designates as at fair value through surplus or deficit;
(b) Those that the entity designates as available-for-sale; and
(c) Those that meet the definition of loans and receivables.

19.12 Held-to-maturity financial assets include investments in quoted bonds and foreign government securities, assuming that the conditions above are met.

19.13 Under the 'tainting rule', an entity shall not classify any financial assets as held-to-maturity if the entity has, during the current financial year or during the two preceding financial years, sold or reclassified more than significant amount of held-to-maturity before maturity.

19.14 It shall be reclassified as AFS and re-measured at fair value and the difference between its carrying amount and fair value shall be accounted for directly in net assets/equity through statement of changes in net assets/equity.

Available for sale assets

19.15 Available for sale assets are non-derivative financial assets that are designated as available-for-sale or are not classified as:

(a) Loans and receivables,
(b) Held-to-maturity investments or
(c) Financial assets at fair value through surpluses or deficit.

19.16 Available for sale financial assets consist of, for example, quoted and unquoted equity and debt securities.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Types of financial liabilities

Financial liabilities at fair values through surplus and deficit

19.17 A financial liability at fair value through surplus or deficit is a financial liability that meets either of the following conditions:

(a) It is classified as held for trading. A financial liability is classified as held for trading if it is:
  (i) Acquired or incurred principally for the purpose of selling or repurchasing it in the near term;
  (ii) On initial recognition, part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking; or
  (iii) A derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument).

(b) Upon initial recognition, designated by the entity as at fair value through surplus or deficit.

19.18 Financial liabilities at fair value from surplus or deficit include, for example, derivatives held in an unfavourable position.

Other financial liabilities

19.19 At government level, government could engage in a 'government to government loan' type, also known as bilateral loans. The bilateral loans can be syndicated (more than 1 lender) or single lender loan. . It is quite common for a group of lenders to fund a loan jointly. This is usually accomplished by a loan syndication under which each syndicate members lends a specific amount to the borrower and has the right to repayment from the borrower.

19.20 For other development works, a government can obtain a multilateral term loan from banks. These loans are for example, obtained from Islamic Development Bank or Asian Development Bank.

19.21 Accounts payable are balances owed to trade creditors, sundry creditors and others for goods, services, loans, transfer payments etc. Payables arise because of the time lag between the requirement to record the obligation and the requirement to satisfy the obligation at a later date.

19.22 Deposits consisting of general and investment deposits are monies received for specific purposes (under law or agreement) and need to be reimbursed once purpose is achieved. General deposits include deposit for unclaimed monies arising from sale proceeds from unclaimed security.

Financial guarantee contracts

19.23 A financial guarantee is a promise to pay all or a part of the principal and/or interest on a debt obligation in the event of default by the borrower. A financial guarantee contract requires the issuer to make specified payments to reimburse the holder for a loss it incurs if a specified entity (debtor) fails to make payment when due under a financial instrument's original or modified terms.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

19.24 A contract that compensates the holder more than the loss incurred does not meet the definition of a financial guarantee contract. For the definition of a financial guarantee to be met, the amount of reimbursement must be either less than the amount of loss incurred or equal to the amount incurred in order to reimburse some or all of the loss the holder suffered because the debtor defaulted.

19.25 Governments may issue financial guarantees for a variety of reasons. They are often issued to further a government's policy objectives, for example, to support infrastructure projects and stabilize the financial market in times of distress. Governments and public sector entities may be granted the power to issue financial guarantees by legislation or other authority. In assessing whether a guarantee is contractual or non-contractual, an entity distinguishes the right to issue the guarantee and the actual issue of the guarantee. The right to issue the guarantee in terms of legislation or other authority is non-contractual, while the actual issue of the guarantee should be assessed using the substance over form principle to determine whether the guarantee is contractual.

19.26 There are loans taken by statutory bodies and government linked companies, such as FELDA and Khazanah Nasional Berhad which are guaranteed by the FGOM under the provision of Loans Guarantee (Bodies Corporate) Act 1965 (Act 96). Fee consideration is charged in exchange for financial guarantees by FGOM.

Initial recognition and measurement

19.27 When a financial asset or financial liability is recognised initially, an entity shall measure it at its fair value plus, in the case of a financial asset or financial liability not at fair value through surplus or deficit, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Subsequent measurement

<u>Financial assets</u>

19.28 Loans and receivables are measured at amortized cost using the effective interest method less impairment losses.

19.29 Financial assets at fair value through surplus or deficit are subsequently measured at fair value with changes in fair value recognized in surplus or deficit.

19.30 Available for sale assets are subsequently measured at fair value through surplus or deficit except in rare circumstances where it is measured at cost less impairment (only for investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured).

19.31 Available for sale gain or loss are recognized directly to net assets/ equity through statement of changes in net assets/equity.

19.32 Dividends or similar distributions on an available-for-sale equity instrument are recognized in surpluses or deficit when the entity's right to receive payment is established.

19.33 Held-to-maturity assets are subsequently measured at amortized cost using the effective interest method cost less impairment losses.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Financial liabilities

19.34 Financial liabilities at fair value through surplus or deficit are subsequently measured at fair value with changes in fair value recognised in surplus or deficit. Financial liabilities are measured at amortized cost using the effective interest method.

19.35 Subsequent measurement for financial guarantee contracts is at the higher of the amount determined in accordance with MPSAS 19 - Provisions, Contingent Liabilities and Contingent Assets and the amount initially recognized less, where appropriate, cumulative amortization in accordance with MPSAS 9 - Revenue from Exchange Transactions (financial guarantee fees).

19.36 Where there are no examples of similar financial guarantee contracts, a government can conclude it cannot use a valuation technique as the use of a valuation technique does not provide a reliable fair value. A government can therefore determine to measure financial guarantee contract in accordance with MPSAS 19 – Provisions, Contingent Liabilities and Contingent Assets.

Effective Interest Method

19.37 The amortised cost of a financial asset or financial liabilities is defined as the amount at which the financial asset or liabilities is measured at initial recognition minus principal repayments plus or minus the cumulative amortization using the effective interest method of any differences between initial amount and the amount payable at maturity minus any reduction (through the use of an allowance account) for impairment or uncollectability. The calculation of effective interest rate is illustrated under Scenario E.2

19.38 The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest revenue or interest expense over the relevant period.

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

19.40 When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of the financial instrument (e.g. prepayments) but shall not consider future credit losses.

19.41 The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Derecognition

Financial assets

19.42 Derecognition of a financial asset is when the contractual rights to the cash flow is extinguished or waived or when all risk, reward and control have been transferred.

Financial liabilities

19.43 Derecognition of a financial liability is when the obligation is waived, cancelled, discharged or expired.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Impairment of financial assets

19.44 An entity shall assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired. If any such evidence exists, the entity shall determine the amount of any impairment loss.

19.45 A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. For FGOM, an immediate impairment is mandatorily triggered when an instalment due is three (3) months in arrears. So, when an instalment is not paid 3 months after its due date, this receivable will hit mandatory trigger and impairment assessment will be made to collate evidence for any impairment losses.

19.46 It may not be possible to identify a single, discrete event that caused the impairment. Rather the combined effect of several events may have caused the impairment. Losses expected as a result of future events, no matter how likely, are not recognized. Objective evidence that a financial asset or group of assets is impaired includes other observable data that comes to the attention of the holder of the asset about the following loss events:

(a) Significant financial difficulty of the issuer or obligor;
(b) A breach of contract, such as a default or delinquency in interest or principal payments;
(c) The lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
(d) It becoming probable that the borrower will enter bankruptcy or other financial reorganization;
(e) The disappearance of an active market for that financial asset because of financial difficulties; or
(f) Observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:
    (i) Adverse changes in the payment status of borrowers in the group(e.g., an increased number of delayed payments); or
    (ii) National or local economic conditions that correlate with defaults on the assets in the group (e.g., an increase in the unemployment rate in the geographical area of the borrowers, a decrease in oil prices for loan assets to oil producers, or adverse changes in industry conditions that affect the borrowers in the group).

19.47 In addition to the above, objective evidence impairment for an investment in an equity instrument includes information about significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the issuer operates and indicates that the cost of investment in the equity instrument may not be recovered.

19.48 A significant or prolonged decline in the fair value of an investment in equity improvement below its cost is also objective evidence of impairment.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Financial instrument denominated in foreign currency

19.49 These are financial instruments denominated in a currency other than the functional currency of FGOM which is Ringgit Malaysia (RM), that results in the contractual right to collect, or contractual obligation to deliver cash in foreign currencies. For example, when government borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency.

19.50 A translation is therefore required to convert financial data denominated in a foreign currency in terms of the functional currency.

19.51 A financial instrument denominated in a foreign currency shall be initially recognized in the functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction.

19.52 At each subsequent reporting date, these financial instruments shall be translated using the closing rate.

19.53 Exchange differences arising on the settlement of monetary items, or on translating monetary items at rates different from those at which they were translated on initial recognition, shall be recognized in surplus or deficit.

Concessionary loans

19.54 Concessionary loans are granted to or received at below market terms.

19.55 As concessionary loans are granted or received at below market terms, the transaction price on initial recognition of the loan may not be its fair value.

19.56 An entity also assesses whether the substance of the concessionary loan is in fact a loan, a grant or a contribution from owners.

19.57 Any difference between the fair value of the loan and the transaction price (the loan proceeds) is treated as follows:

(a) Where the loan is received by an entity, the difference is accounted for as a non-exchange revenue.

(b) Where the loan is granted by an entity, the difference is treated as an expense in surplus or deficit at initial recognition, except where the loan is a transaction with owners, in their capacity as owners. Where the loan is a transaction with owners in their capacity as owners, for example, where a controlling entity provides a concessionary loan to a controlled entity (ie. statutory bodies), the difference may represent a capital contribution, i.e., any investment in an entity, rather than an expense.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Securitization of loans and accounts receivable

19.58 It is fairly common for entities to raise finance by selling financial assets such as portfolios of loans and receivables.

19.59 Securitisation is a method of raising finance, first used by originators of mortgage loans through a sale of a block or poll of loans to another entity.

19.60 The receiving entity/ transferee could finance the purchase by issuing loan notes or other marketable debt instruments. This process is known as securitisation and referred to as an asset backed finance.

19.61 There are key pass through conditions to confirm whether transferee has transferred sufficient risk and rewards associated with the asset to achieve derecognition as per below:

(a) the transferor is not obliged to transfer funds to the transferee that it has not collected, that is, it is not required to fund payments to the eventual recipients. This means the transferee must bear the late payment risk;

(b) the transferors ability to sell or pledge the financial assets highlights that the transferor does not control access to the future economic benefits associated with the transferred cash flows and therefore may not have an asset; and

(c) the transferor is prohibited from re-investing the cash flows received in the short settlement period between collection of remittance. The transferor is not allowed to invest fund in other high yielding medium term investments for the benefits of the transferee or utilize funds in generating further assets for securitization.

19.62 Where a transferor selling financial assets for cash (or other assets) with no continuing involvement with the asset sold or with transferee and passes through conditions for derecognition, then the sale of financial asset will come with a corresponding derecognition of asset.

19.63 Where a transferor selling financial assets for cash still retains risk and reward to that financial obligation (or still retains recourse to that asset) and does not pass through conditions for derecognition, then the cash received transaction is treated as a financing transaction. The risk and reward of the ownership of asset have not been transferred.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Derivatives and hedging

19.64 Derivatives is a financial instrument or other contract within scope with all three of the following characteristics:

(a) its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying');

(b) 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

(c) it is settled at a future date.

19.65 Examples are foreign currency forward contract, options, interest swaps and futures.

19.66 'Hedging' is the process of using a financial instrument (usually a derivative) to mitigate all or some of the risk of a hedged item.

19.67 'Hedging accounting' changes the timing of recognition of gains and losses on either the hedged item or the hedging instrument so that both are recognised in surplus or deficit in the same accounting period.

19.68 To qualify for hedge accounting, an entity (a) at the inception of the hedge, formally designates and documents a hedge relationship between a qualifying hedging instrument and a qualifying hedged item; and (b) both at inception and on an ongoing basis, demonstrates that the hedge is highly effective.

19.69 There are three types of hedge relationship:

- Fair value hedge – a hedge of the exposure to changes in the fair value of a recognised asset or liability, or a firm commitment.
- Cash flow hedge – a hedge of the exposure to variability in cash flows of a recognised asset or liability, a firm commitment or a highly probable forecast transaction
- Net investment hedge – a hedge of the foreign currency risk on a net investment in a foreign operation.

19.70 For a fair value hedge, the hedged item is adjusted for the gain or loss attributable to the hedged risk. That element is included in the surplus or deficit where it will offset the gain or loss on the hedging instrument.

19.71 For a cash flow hedge, gains and losses on the hedging instrument, to the extent it is an effective hedge, are initially included in equity. They are reclassified to profit or loss when the hedged item affects the surplus or deficit. If the hedged item is the forecast acquisition of a non-financial asset or liability, the entity may choose an accounting policy of adjusting the carrying amount of the non-financial asset or liability for the hedging gain or loss at acquisition.

19.72 Hedges of a net investment in a foreign operation are accounted for similar to cash flow hedges.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Disclosures requirement

19.73 The disclosure requirements for financial statements are extensive. Details of the disclosures are in MPSAS 30 – Financial instruments; disclosure.

References

- MPSAS 4 – The Effect of Changes in Foreign Exchange Rates
- MPSAS 19 – Provisions, Contingent Liabilities and Contingent Assets
- MPSAS 28 – Financial Instruments, Presentation
- MPSAS 29 – Financial Instruments, Recognition and Measurement
- MPSAS 30 – Financial Instruments, Disclosures
- Accounting Policy and Interpretation

19.0 *FINANCIAL INSTRUMENTS (CONTINUED)*

Scenario A - Loans and receivable

Scenario A.1 - Recognition of accounts receivable

The entity provides services to an external party for RM500 for the provision of an air time slot.

Journal entries

1) Upon service rendered to the external party. Payment has not been received

Upon invoicing the outside party, revenue and a corresponding accounts receivables is recognized.

	Amount (RM)	Accounting Code
DR Accounts receivable	500	A0372300
CR Revenue	500	H0272302

2) Upon full settlement of the invoice

At this point the outside party has paid the entity thereby reversing the accounts receivable and increasing the entity's cash holdings.

	Amount (RM)	Accounting Code
DR Cash	500	A0113000
CR Accounts receivable	500	A0372300

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario A.2 - Recognition of provision for impairment loss, partial reversal of provision for impairment loss and its subsequent write-off

An entity decides to recognize provision for impairment loss on a long overdue accounts receivable upon approval from authorities. Based on collectability assessment, the entity sets up a provision for impairment loss account for RM10,000.

Following various discussions, the debtor committed to payment of RM2,000 resulting in a partial reversal of the provision. This amount was paid.

Subsequent to that, the vendor was declared bankrupt. The remaining provision for impairment loss written off.

Journal entries

1) To record accumulated impairment loss

When an accumulated impairment loss is recorded, an impairment loss expense is recorded. The accumulated impairment loss is a valuation account (i.e. contra asset) and is subtracted from the gross amount of the accounts receivables on the statement of financial position.

	Amount (RM)	Accounting Code
DR Impairment loss expense	10,000	B5150000
CR Accumulated impairment loss	10,000	A5150000

2) To record partial reversal of accumulated impairment loss

As the debtor had committed to payment of an amount of RM2,000, partial reversal of provision was triggered.

	Amount (RM)	Accounting Code
DR Accumulated impairment loss	2,000	A5150000
CR Impairment loss expense (reversal)	2,000	B5150000

3) To record the write-off of the accumulated impairment loss

When the debt is assessed to be irrecoverable, they will be written off upon approval from authorities.

To write-off the balance, the accumulated impairment loss (a contra account) is reversed and the accounts receivable account is credited.

	Amount (RM)	Accounting Code
DR Accumulated impairment loss	8,000	A5150000
CR Accounts receivable	8,000	A0370000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario A.3 - Recognition of provision for impairment loss, partial reversal of provision for impairment loss and its subsequent write-off of a FGOM loan receivable

Entity A was given a loan from a Development Fund for RM100,000. The repayment terms was as set at RM20,000 per year together with interest charged at 4% on reducing balance over 5 years period.

After 1 year, Entity A had not done any repayments. An impairment indicator was triggered on Entity A's loan receivable in FGOM's books. Entity A's loan was unguaranteed, there was no collateral provided against the loan and a review of Entity A's financial statements revealed that Entity A was going through financial difficulties.

FGOM decided to fully impair the loan receivable at the end of Year 1. The journal entries below assumes accounts receivable and interest income journal entries have been performed and focuses purely on the impairment entries.

Journal entries

1) To record accumulated impairment loss

100% of the loan receivable and interest income accumulated over the past 1 year was wholly impaired and an impairment loss expense was recorded amounting to RM104,000. An annual repayment of RM20,000 on principal and 4% interest should have been repaid. The below table shows the increasing interest calculated at the end of the first year.

Year	Principal (RM)	Annual interest	Annual repayment	Balance (RM)
1	100,000	4,000		104,000
2	104,000	4,160		108,160
3	108,160	4,326		112,486
4	112,486	4,499		116,986
5	116,986	4,679		121,665

	Amount (RM)	Accounting Code
DR Impairment loss expense - FGOM loan	104,000*	B5111000
CR Accumulated impairment loss - FGOM loan	104,000	A5111000

* Total receivable is charged as a loss arising for impairment. This includes interest income as impairment loss arising does not create any reversal of interest income recognised earlier.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Journal entries

2) To record reversal of accumulated impairment loss

Entity A committed and paid the annual repayment and interest due for Year 1. The repayment totalled RM24,000. The impairment was partially reversed.

	Amount (RM)	Accounting Code
DR Accumulated impairment loss - FGOM loan	24,000	A5111000
CR Impairment loss expense - FGOM loan	24,000	B5111000

3) To record the write off of the accumulated impairment loss

Entity A started defaulting repayment again in Year 2, 6 months after repayment under journal entry 2 above was done. FGOM agreed to write off this loan receivable after an appeal was made by Entity A.

Year	Principal (RM)	Annual interest	Annual repayment	Balance (RM)
1	100,000	4,000	(24,000)	80,000
2	80,000	3,200		83,200
3	83,200	3,328		86,528
4	86,528	3,461		89,989
5	89,989	3,600		93,589

(a) The remaining accumulated impairment loss amount was reversed.

	Amount (RM)	Accounting Code
DR Accumulated impairment loss - FGOM loan	83,200	A5111000
CR Impairment loss expense - FGOM loan	83,200	B5111000

(b) Entity A's outstanding principal and interest income recognised to date amounting of RM83,200 was written off against loan receivable account.

	Amount (RM)	Accounting Code
DR Bad debt written off - FGOM loan	83,200	B0551209
CR FGOM loan receivable	83,200	A0411000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario A.4 - Write off of an accounts receivable not previously provided for

An accounts receivable for RM300 is deemed as uncollectible and is written off upon approval from authorities. Before that, there was no allowance for impairment loss made.

Journal entries

1) To record the write-off

An account receivable should be written off if it is known with certainty that it is uncollectible. Where there was is no allowance of impairment of loss for that accounts receivable, the balance is removed from the books by debiting 'Bad debt written-off' and crediting 'Accounts receivable'.

	Amount (RM)	Accounting Code
DR Bad debt write off	300	B0551202
CR Accounts receivable	300	A0370000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario A.5 - Recognition of loan receivable

An entity provides a loan of RM500,000 to a state government to finance the construction of an exhibition building. The effective interest rate on loan is 6% per annum, and is repayable in monthly instalment at the end of every month over a 5-year period. There are no concessionary terms related to this scenario.

Journal entries

1) To record loan of RM500,000 given

The loan is recorded on the books at its fair value.

	Amount (RM)	Accounting Code
DR Loans receivable	500,000	A0411100
CR Cash	500,000	A0112000

2) To record accrual of interest receivable and recognize interest revenue

As interest is earned on the loan, the amount is recognized periodically as revenue for the period. In this case, interest revenue and interest receivable is recorded monthly. The amount of interest calculated in the first month is as follows: RM2,500 =RM500,000 x (6%/12months). The calculation here is assumed to approximate the effective interest rate method.

	Amount (RM)	Accounting Code
DR Loans receivable	2,500	A0411100
CR Interest revenue	2,500	H0275501

3) Record periodic repayments of the loan

As loan repayments are made, the cash holdings of the entity are increased. This is reflected by a debit to 'Cash'. The outstanding amount of the loan receivable is also reduced. When the interest is paid, the accrued interest receivable is reversed. The amount of loan repayment is: RM9,500 = RM7,000 (principal portion) + RM2,500 (interest portion). These amounts are derived using a loan calculation program.

	Amount (RM)	Accounting Code
DR Cash	9,500	A0113000
CR Loans receivable	7,000	A0411100
CR Interest on loan receivable	2,500	A0411100

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario B - Financial assets at fair value through surplus or deficits

Scenario B.1 - Purchase of financial assets at fair value through surplus or deficit and recognition of changes in fair value

An entity purchases Singapore Government Securities (SGS), a financial asset held for trading or financial asset at fair value through surplus or deficit. The fair value of the SGS amounts to RM15,000 and the entity incurs a transaction cost of RM1,000.

At the end of the financial year, the fair value of the Singapore Government Securities (SGS) increased to RM18,000.

Journal entries

1) To record the recognition of financial asset at fair value through surplus or deficit.

(a) At the point the financial assets at fair value through surplus or deficit is acquired, the financial asset is recognized at its fair value,.

	Amount (RM)	Accounting Code
DR Financial assets at fair value through surplus or deficit	15,000	A1342210
CR Cash	15,000	A0112000

(b) The transaction cost relating to the financial asset is expensed off.

	Amount (RM)	Accounting Code
DR Transaction cost expense	1,000	B0552999
CR Cash	1,000	A0112000

2) To record the recognition of changes in fair value

Where the fair value of changes, the gain/loss on the re-measurement of financial assets at fair value through surplus or deficit is recognized in the current year surplus or deficit.

	Amount (RM)	Accounting Code
DR Financial assets at fair value through surplus or deficit	3,000	A1342210
CR Gain on re-measurement of financial assets at fair value through surplus or deficit	3,000	H0187302

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario B.2 - Sale of financial assets at fair value through surplus or deficit

Following on from scenario B.1, the entity sells the financial asset at fair value through surplus or deficit at a selling price of RM12,000. The carrying amount of the financial asset at fair value through surplus or deficit is RM15,000.

Journal entries

1) To record the sale of financial assets at fair value through surplus or deficit

At the point the financial assets at fair value through surplus or deficit is disposed, the financial asset at fair value through surplus or deficit is credited and the cash account is debited. The difference between the book value of the financial asset at fair value through surplus or deficit and the selling price is recognized as either a gain or loss on sale of financial asset at fair value through surplus or deficit

	Amount (RM)	Accounting Code
DR Cash	12,000	A0113000
DR Loss on sale of financial assets at fair value through surplus or deficit	3,000	B0554201
CR Financial assets at fair value through surplus or deficit	15,000	A1342210

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario C - Available for sale assets

Scenario C.1 - Purchase and re-measurement of available-for-sale financial assets with known market price

An entity purchases a publicly listed equity security which amounts to RM15,000. The entity incurs a transaction cost of RM2,000. At the financial year end of 20X3, the security fair value increased to RM20,000.

The security is classified as available for sale financial assets.

Journal entries

1) To record the purchase of available-for-sale financial asset

(a) Both quoted and unquoted securities acquired which are not intended to be sold within near period (and also not to be hold to maturity) are classified as available-for-sale financial asset.

At the point of acquisition of the quoted equity, available-for-sale financial asset will be recognized at RM17,000.

	Amount (RM)	Accounting Code
DR Available-for-sale financial asset	17,000	A1322110
CR Cash	17,000	A0112000

2) To record the gain on the re-measurement of available-for-sale financial asset

At the financial year end of 20X3, the gain on available-for-sale financial asset is not recognized in the current year surplus/ deficits. Instead, it is credited into an account known as gains / (loss) on re-measurement of available-for-sale financial asset, which is a separate component in the net assets/ equity. The same applies for the loss on available-for-sale financial asset.

	Amount (RM)	Accounting Code
DR Available-for-sale financial asset	3,000	A1322110
CR Gains on re-measurement of available-for-sale financial asset (directly in net assets/equity)	3,000	E0111000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario D - Held-to-maturity assets

Scenario D.1 - Purchase and re-measurement of held-to-maturity financial assets with known market price

An entity purchases a quoted bonds which amounts to RM15,000. The entity incurs a transaction cost of RM2,000. At the financial year end of 20X3, the bonds were re-measured at amortized cost (using effective interest method) less impairment losses. The bonds were valued at RM10,000.

The security is classified as held-to-maturity financial assets.

Journal entries

1) To record the purchase of held-to-maturity financial asset

(a) Both quoted and unquoted securities acquired which has a fixed or determinable payment and fixed maturity are classified as held-to-maturity financial assets.

At the point of acquisition of the quoted equity, held-to-maturity financial asset will be recognized at RM17,000.

	Amount (RM)	Accounting Code
DR Held-to-maturity financial asset	17,000	A1312115
CR Cash	17,000	A0112000

2) To record the impairment loss held-to-maturity financial asset

At the financial year end of 20X3, the financial asset was impaired by RM7,000 based on amortised cost and the impairment loss is recognised in current year surplus or deficit.

	Amount (RM)	Accounting Code
DR Impairment loss expense	7,000	B5012115
CR Accumulated impairment loss	7,000	A5012115

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario E - Other financial liabilities

Scenario E.1 - Entity incurs repair expenses

An entity incurs RM6,500 in repairs for an air conditioning system for an office building. The repair expense is accrued and paid at the next financial period.

Journal entries

1) To record the repairs expense incurred

Once the operating expenses have been incurred regardless of when it is paid for or whether the invoice has been received, the entity must record by accruing the expense as a liability under accounts payable and debiting operating expenses account

	Amount (RM)	Accounting Code
DR Repair expense of office building	6,500	B0228102
CR Accrual/Accounts payable	6,500	L0128100

2) Subsequently, the entity settles this liability

Once the operating expense is paid, the entity must reduce the liability recorded in the accounts payable and the cash account is reduced accordingly.

	Amount (RM)	Accounting Code
DR Accounts payable	6,500	L0128100
CR Cash	6,500	A0112000

Scenario E.2 - Amortization of premium amounts received on local borrowing

FGOM raised funds via government investment issues totalling RM2,000,000,000 based on an annual interest rate of 4% on a nominal value of RM2,000,000,000 at premium of 0.7% for a period of 5 years.

Journal entries

1) To record the funds received amounting to RM2,000,000,000 plus the additional nominal value at 0.7% against the principal sum amounting to RM14,000,000. Total receipt was RM2,014,000,000

When borrowing is received from the bank in the form of cash payment, the cash account is debited and a liability must be accrued for as borrowing, together with the nominal amount received.

	Amount (RM)	Accounting Code
DR Cash	2,014,000,000	A0113000
CR Premium Government Investment Issues*	14,000,000	L0611211
CR Government Investment Issues*	2,000,000,000	L0611210

* On financial statement, this is disclosed on net basis.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Journal entries

2) To record Year 1 interest and amortisation of premium over borrowing

When yearly interest is paid at 4%, the amount to be amortized from borrowing premium account will be based on the difference of RM80,000,000 and the interest calculated on the IRR rate. Year 1 effective interest rate is based on RM77,407,120.93 interest payment over initial cash received 2,014,000,000 amounting to 3.843%. The same effective rate is applied for subsequent years.

Year	Cashflow (RM)	Interest	Amortize Premium (RM)	Carrying Value (RM)
0	2,014,000,000.00			2,014,000,000.00
1	(80,000,000.00)	(77,407,120.93)	(2,592,879.07)	2,011,407,120.93
2	(80,000,000.00)	(77,307,464.87)	(2,692,535.13)	2,008,714,585.80
3	(80,000,000.00)	(77,203,978.58)	(2,796,021.42)	2,005,918,564.38
4	(80,000,000.00)	(77,096,514.84)	(2,903,485.16)	2,003,015,079.22
5	(2,080,000,000.00)	(76,984,920.78)	(3,015,079.22)	-
IRR	3.843% (based on cash flows)		14,000,000.00	-

Upon payment of interest of RM80,000,000 the liability account is reduced by the cash payment.

	Amount (RM)	Accounting Code
DR Government Investment Issues	77,407,120.93	L0611210
DR Premium Government Investment Issues	2,592,879.07	L0611211
CR Cash	80,000,000.00	A0112000

At the same time, the interest accrual relating to that year's interest is expensed to surplus or deficit for that period.

	Amount (RM)	Accounting Code
DR Interest expense	77,407,120.93	B0445103
CR Government Investment Issues	77,407,120.93	L0611210

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario E.3 - Amortization of discount amounts received on local borrowing

FGOM raised funds via government investment issues totalling RM3,000,000,000 at a discounted rate of 6% for 5 years based on an annual interest rate of 8%.

Journal entries

1) To record the funds received amounting to RM2,820,000,000 at a 6% discounted rate over principal sum of RM3,000,000,000. Total discount amounted to RM180,000,000

When borrowing is received from the bank in the form of cash payment, the cash account is debited and a liability must be accrued for as borrowing together with the nominal discount received.

	Amount (RM)	Accounting Code
DR Cash	2,820,000,000	A0113000
DR Discount Government Investment Issues*	180,000,000	L0611211
CR Government Investment Issues *	3,000,000,000	L0611210

* On financial statements, this is disclosed on net basis.

2) To record Year 1 interest payment for the 1st half of the year at 4% interest rate on RM3,000,000,000 amount together with the amortization of the discount on government investment issues

When the half yearly interest is paid at 4%, the amount to be amortized from borrowing discount account will be based on the difference of RM120,000,000 and the interest calculated on the IRR rate(being the effective interest of 4.768%). The half yearly interest rate is calculated based on RM134,466,309.51 half yearly interest over initial cash received of RM2,820,000,000.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Journal entries

Upon payment of the half yearly interest of RM120,000,000 the liability account is reduced by the cash payment.

	Amount (RM)	Accounting Code
DR Government Investment Issues	134,466,309.51	L0611210
CR Discount Government Investment Issues	14,466,309.51	L0611211
CR Cash	120,000,000.00	A0112000XXX

At the same time interest accrual relating to the half yearly interest is expensed to surplus or deficit for that period

	Amount (RM)	Accounting Code
DR Interest expense	134,466,309.51	B0445103
CR Government Investment Issues	134,466,309.51	L0611210

Year	Month	Cashflow (RM)	Interest (RM)	Amortize Discount (RM)	Carrying Value (RM)
0		2,820,000,000.00			2,820,000,000.00
1	June	(120,000,000.00)	(134,466,309.51)	14,466,309.51	2,834,466,309.51
	December	(120,000,000.00)	(135,156,107.83)	15,156,107.83	2,849,622,417.34
2	June	(120,000,000.00)	(135,878,797.86)	15,878,797.86	2,865,501,215.19
	December	(120,000,000.00)	(136,635,947.98)	16,635,947.98	2,882,137,163.17
3	June	(120,000,000.00)	(137,429,201.36)	17,429,201.36	2,899,566,364.53
	December	(120,000,000.00)	(138,260,279.51)	18,260,279.51	2,917,826,644.04
4	June	(120,000,000.00)	(139,130,986.03)	19,130,986.03	2,936,957,630.07
	December	(120,000,000.00)	(140,043,210.53)	20,043,210.53	2,957,000,840.61
5	June	(120,000,000.00)	(140,998,932.71)	20,998,932.71	2,977,999,773.32
	December	(3,120,000,000.00)	(142,000,226.68)	22,000,226.68	-
IRR		4.768% (based on cash flows)		180,000,000.00	-

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario F - Financial instrument denominated in foreign currency

Scenario F.1 - Foreign Currency Transactions (Loss)

An entity purchases consumables from a U.S firm for $50,000 USD. The exchange rate is quoted at RM3.45 when the goods are received. The entity makes payment for the purchase a week later. The exchange rate on payment date is RM3.47.

Journal entries

1) To record purchase of goods at time of receipt

When the purchase is made, the entity must record the expenses in Malaysian Ringgit at the exchange rate in effect at the time the goods are received. The amount will be recorded at RM172,500 ($50,000 USD x 3.45). A payable must be set up to record the amount owing for the corresponding amount.

	Amount (RM)	Accounting Code
DR Consumables expense	172,500	B0227100
CR Account payable	172,500	L0127100

2) Entity pays for the consumables

When the payment is made, the accounts payable is reversed. The cash account would reflect the payment made at the foreign currency rate of payment date, RM173,500 ($50,000 USD x 3.47). The difference will result in a loss of RM1,000 (RM173,500 - RM172,500).

	Amount (RM)	Accounting Code
DR Loss on foreign exchange	1,000	B0557301
DR Account payable	172,500	L0127100
CR Cash	173,500	A0112000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario F.2 - Foreign Currency Transactions (Gain)

Assume all dealings in the previous scenario apply here, except that the rate in effect at payment date is $3.43USD.

Journal entries

1) Please refer to journal entry 1 under Scenario F.1 above

2) Entity pays for the consumables

Since the payment is made, the accounts payable is reversed at the original amount at which it was established. The cash account would reflect the payment made at the foreign currency rate of payment date, RM171,500 (50,000 x 3.43). The difference results in a gain of RM1,000 (RM172,500 - RM171,500).

	Amount (RM)	Accounting Code
DR Account payable	172,500	L0127100
CR Gain on foreign exchange	1,000	H0283101
CR Cash	171,500	A0112000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario F.3 - Foreign exchange translation at month end (for financial reporting)

Entity purchases consumables from a U.S firm for $50,000 USD. The exchange rate used to record the payable on the books is RM3.45 (the goods-receipt date). The account payable is recorded at RM172,500($50,000 x RM3.45). The amount was not fully settled by month end.

The same entity also sells goods to a U.S firm for $100,000 USD. The exchange rate used to record the receivable on the books was RM3.48 (the transaction date). The receivable is recorded at RM348,000 (100,000 x RM3.48). The amount was not fully settled by month end.

As at month end, the exchange rate in place is RM3.50.

Journal entries

1) To record part payment and translation of financial liabilities

(a) Part payment of liability during the month amounting to $30,000

The part payment amounted to RM104,100 based on an exchange rate of RM3.47. This amount reduces the account payable. No realised foreign exchange gain or loss is recognised at this stage.

	Amount (RM)	Accounting Code
DR Account payable	104,100	L01227100
CR Cash	104,100	A0112000

(b) Translation of foreign currency financial liabilities at month end

The total payable was originally recorded in the books at an exchange rate of RM3.45 amounting to RM172,500 ($50,000 x RM3.45).
The balance of $20,000 ($50,000 - $30,000, journal 1a above) must be translated to reflect the exchange rate in effect at the statement of financial position date and amounts to RM70,000 ($20,000 x RM3.50) .
Based on Journal 1a, the part payment settled amounting to RM104,000 leaves a balance of RM68,400 (RM172,500 – RM104,100). The fluctuation in foreign exchange rates results in a loss of RM1,600 (RM70,000-RM68,400).

	Amount (RM)	Accounting Code
DR Loss – foreign exchange	1,600	B0557301
CR Account Payable	1,600	L01227100

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Journal entries

2) To record part receipt and translation of financial assets

(a) Part receipt of receivable during the month amounting to $60,000

The part receipt amounted to RM209,400 based on an exchange rate of RM3.49. This amount reduces the account receivable. No realised foreign exchange gain or loss is recognised at this stage.

	Amount (RM)	Accounting Code
DR Cash	209,400	A0113000
CR Account receivable	209,400	A0373900

(b) Translation of foreign currency financials assets at month end

The total receivable was originally recorded on the books at RM3.48 amounting to RM348,000 ($100,000 x RM3.48).
The balance of $40,000 ($100,000 - $60,000, journal 2a above) must be translated to reflect the exchange rate in effect at the statement of financial position date and amounts to RM140,000 ($40,000 x RM3.50).
Based on Journal 2a, the part receipt received amounting to RM209,400 leaves a balance of RM138,600 (RM348,000 – RM209,400). The fluctuation in foreign exchange rates results in a total gain of RM1,400 (RM140,000 – RM138,600).

	Amount (RM)	Accounting Code
DR Account receivable	1,400	A0373900
CR Revaluation gain – foreign exchange	1,400	E0121000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario G - Concessionary loan

Scenario G.1- Recognition of concessionary loan

The entity advanced RM250 million to various students at the beginning of financial year, with the following terms and conditions:

(a) Principal is repaid as follows:
Year 1 to 3 : no principal be repaid
Year 4 : 30% principal to be repaid
Year 5 : 30% principal to be repaid
Year 6 : 40% principal to be repaid

(b) Interest is calculated at 6% interest on the outstanding loan balance and is paid annually in arrears. Assume the market rate of interest for a similar loan is 11.5%.

Journal entries

1) To record the issuance of loan amounting to RM250 million

As the concessionary loan is granted at an interest rate of 6%, below the market interest rate of 11.5%, the loan receivable is not able to be recognised at the transacted amount of RM250,000,000. (Note: the fair valuation of the loan can be done collectively).

	Amount (RM'000)	Accounting Code
DR Loan receivable	199,345	A0411800
DR Expense*	50,655	B0556108
CR Bank	250,000	A0112000

Instead, the future cash receipts of the loan is discounted using a market interest rate of 11.5% to arrive at a present value of RM199,345,480. Difference between the transaction price of RM250,000,000 and fair value of the loan of RM199,345,480 amounts to RM50,654,520 (RM250,000,000 – RM199,345,480). The difference is recognised as an expense in surplus or deficits. Please refer to the table below for the detailed calculation:

	Year 1 (RM'000)	Year 2 (RM'000)	Year 3 (RM'000)	Year 4 (RM'000)	Year 5 (RM'000)	Year 6 (RM'000)
Capital balance	250,000	250,000	250,000	175,000	100,000	-
Interest payable (6%)	15,000	15,000	15,000	15,000	10,500	6,000
Total payments (capital and interest)	15,000	15,000	15,000	90,000	85,500	106,000
Present value of payments	13,453	12,066	10,820	58,229	49,613	55,164
Total present value of payments						199,345
Proceeds paid						250,000
Off-market portion of loan to be recognised as expense						50,655

* Where concessionary loan is given to a controlled entity, the difference may represent a capital contribution i.e. an increase in investment in controlled entity rather than an expense.

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Journal entries

2) To record the accrual of interest using the effective interest method

During year 1 to year 6, interest is accrued for each year at different amount based on the effective interest rate. Please refer to the table below for the detailed calculation:

	Year 1 (RM'000)	Year 2 (RM'000)	Year 3 (RM'000)	Year 4 (RM'000)	Year 5 (RM'000)	Year 6 (RM'000)
Capital	199,345	207,270	216,106	225,958	161,944	95,067
Interest accrual (+)	22,925	23,836	24,852	25,985	18,624	10,933
Interest and capital payments(-)	15,000	15,000	15,000	90,000	85,500	106,000
Balance	**207,270**	**216,106**	**225,958**	**161,943**	**95,068**	**-**

	Amount (RM'000)	Accounting Code
DR Loan receivable(+)	22,925	A0411800
CR Interest revenue(-)	22,925	H0275508

Note: The above journal entry will be similar for accrual of interest for each subsequent year with the amount accrued as interest differing in accordance to the table above.

3) To record the payment of interest and principal as per the contractual rate of 6%

	Year 1 (RM'000)	Year 2 (RM'000)	Year 3 (RM'000)	Year 4 (RM'000)	Year 5 (RM'000)	Year 6 (RM'000)
Capital	250,000	250,000	250,000	250,000	250,000	250,000
Interest(+)	-	15,000	15,000	15,000	10,500	6,000
Payments(-)	-	15,000	15,000	90,000	85,500	106,000
Balance	**250,000**	**250,000**	**250,000**	**175,000**	**175,000**	**150,000**

During Year 1 to Year 3, there is no principal repayment. Only interest payment of RM15,000 is recorded as interest revenue.

	Amount (RM'000)	Accounting Code
DR Cash	15,000	A0113000
CR Loan receivable	15,000	A0411800

During Year 4 to Year 6, in addition to interest payment, principal amount is being repaid too. The journal entry below illustrates interest and principal payment for Year 4.

	Amount (RM'000)	Accounting Code
DR Cash	90,000	A0113000
CR Loan receivable	90,000	A0411800

Note: The above journal entry will be similar for Year 5 and Year 6 with the payment amount differing in accordance to the table above.

19.0 *FINANCIAL INSTRUMENTS (CONTINUED)*

Scenario H - Financial guarantees

Scenario H.1 - Entity provides financial guarantee contract and loan written-off – No fee

Entity A has provided a financial guarantee to entity B (the holder) to reimburse entity B against any financial effect of a default by entity C (the debtor) for a 10 year loan of RM1,000,000 that the entity has taken an for the purpose of a specific state development. The 10 year loan was taken on 1 January 20X0. The loan is repayable in 2 equal instalments of RM500,000 in 20X4 and 20X9. Entity C provided no fee consideration to entity A.

In 20X9, there was an economic downturn. Entity C sought bankruptcy protection and defaulted in the 2nd repayment of principal although it met its obligations for interest payment. Entity A confirms entity C is unlikely to recover.

Journal entries

1) Year 20x0 – Year 20x4 – Entity A provides loan guarantee to Entity B – No indication of potential default

As the probability of default is low/remote, the fair value of the final guarantee is assumed to be nil.

2) Year 20X9 – Indication arises on potential default

In view of the economic downturn and the initiation of bankruptcy protection, there arises indication of potential default by entity C. As a result, the fair value of the financial guarantee is assumed to be the maximum exposure of RM500,000. This provision is enacted upon approval from authorising.

A financial liability is created to include the RM500,000.

	Amount (RM)	Accounting Code
DR Financial guarantee expense	500,000	B0552301
CR Financial guarantee contract provision	500,000	L0491000

3) Year 20X9 - Borrower defaults and entity pays out loan guarantee to lender.

When the borrower (entity C) defaults on the loan, entity A is required to make the payment to entity B and a reduction to provision will be made.

	Amount (RM)	Accounting Code
DR Financial guarantee contract provision	500,000	L0491000
CR Cash	500,000	A0112000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario H.2 - Entity provides financial guarantee contract and loan written off – With fee

Same scenario as scenario H.1 applies with a nominal fee consideration of RM10,000 given to the issuer of the financial guarantee contract. The guarantee fee is unconditional and irrevocable.

Journal entries

1) Year 20X0 – Entity A provides loan guarantee to Entity B of the request of entity C for a consideration of RM10,000

Guarantee fee of RM10,000 received from entity C is credited to loan guarantee provision account upon approval from authorities.

	Amount (RM)	Accounting Code
DR Cash	10,000	A0113000
CR Financial guarantee contract provision	10,000	L0491000

2) Year 20X0 to 20X4 – no indication of potential default.

As there was no indication of potential default between Years 20X0 to 20X4, the fair value of the financial guarantee provision was assumed to be RM5,000. The remaining RM5,000 is recognised as revenue from the guarantee fee received (RM10,000/10 years) x 5 years.

	Amount (RM)	Accounting Code
DR Financial guarantee contract provision	5,000	L0491000
CR Miscellaneous revenue	5,000	H0182599

3) Year 20X9 – indication arises on potential default

As indication arises on potential default in view of the economic downturn and the initiation of bankruptcy protection, there arises potential default by entity C. As a result, the fair value of the financial guarantee provision is valued to be the maximum exposure of RM500,000.

As the balance in loan guarantee provision account was RM5,000 (RM10,000 - RM5,000 for entries 1 and 2 above), the additional provision to be made upon approval from authorities was RM495,000 (RM500,000 – RM5,000).

	Amount (RM)	Accounting Code
DR Financial guarantee expense	495,000	B0552301
CR Financial guarantee contract provision	495,000	L0491000

4) Year 20X9– Borrower defaults and entity pays out loan guarantee to lender, entity C

Same journal entry under no. 3 of Scenario H.1 applies.

19.0 *FINANCIAL INSTRUMENTS (CONTINUED)*

Scenario I.- Securitisation of loans and receivables

Scenario I.1 - Sale of loan with no transfer of risk to transferee

An entity decides to sell part of its housing loan portfolio to a mortgage bank A (transferee) amounting to RM500 million in cash.

Entity still retains all recourse to the original housing loans. The risk and rewards of the financial asset remains with the entity.

Journal entries

1) No change in entity portfolio of loans and account receivables

As there was no transfer of risk and rewards to transferee, the loan and accounts remains as a receivable.

2) To record the financing transaction

As the entity received amounts for the sale of loan portfolio, the entity must recognise an owing to Bank A.

	Amount (RM)	Accounting Code
DR Cash	500,000,000	A0113000
CR Amount due to Bank A	500,000,000	L0612210

3) To record repayment to Bank A

a) Repayment upon advise of collection by Bank A assuming all debt was collected.

Assume that in Year 1, RM50,000,000 loan was repaid.

	Amount (RM)	Accounting Code
DR Amount due to Bank A	50,000,000	L0612210
CR Loan receivable	50,000,000	A0421000

b) To record impairment provision upon advice on bankruptcy of a borrower and assuming debt was uncollected.

Entity needs to compensate Bank A via payment directly to Bank A as borrower is unable to make payments. The loan was valued at RM1 million.

	Amount (RM)	Accounting Code
DR Amount due to Bank A	1,000,000	L0612210
CR Cash	1,000,000	A0112000

At the same time, an impairment loss over the loan receivable was recognized.

	Amount (RM)	Accounting Code
DR Impairment loss expense	1,000,000	B5121000
CR Accumulated impairment	1,000,000	A5121000

19.0 FINANCIAL INSTRUMENTS (CONTINUED)

Scenario I.2 - Sale of loan with transfer of risk to transferee

An entity sells part of its housing loan portfolio to a mortgage Bank A (transferee), amounting to RM500 million in cash. The total portfolio sold off amounts to RM550 million.

Entity novated its loans to Bank A and as a result transferred all risk and rewards to Bank A. The novation has the main effect of changing the lender's identity to Bank A.

Journal entries

1) To record derecognition of financial assets

As there was an effective transfer of risk and rewards to transferee and transferor has no recourse to the loans, that part of the loan receivable will be derecognised.

	Amount (RM)	Accounting Code
DR Cash	500,000,000	A0113000
DR Loss on disposal	50,000,000	B0554201
CR Loans and accounts receivable	550,000,000	A042000

Where loan notes were issued in exchange of the block of loans purchased, the loan notes will be recognised as a financial asset value at book value of the asset exchanged.

On derecognition of a financial assets in its entity, the difference between the carrying amount and sum of:

- The consideration received;
- Any cumulative gain or loss recognised in other comprehensive income; and
- Is recognized in surplus or deficit.

APPENDICES

Appendix A.1 List of MPSAS to Be Adopted (with effective date on or after 01 January 2017)

MPSAS	
MPSAS 1	Presentation of Financial Statement
MPSAS 2	Cash Flow Statements
MPSAS 3	Accounting Policies, Changes in Accounting Estimates and Errors
MPSAS 4	The Effect of Changes in Foreign Exchange Rate
MPSAS 5	Borrowing Costs
MPSAS 9	Revenue From Exchange Transactions
MPSAS 11	Construction Contracts
MPSAS 12	Inventories
MPSAS 13	Leases
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List Of Acronyms

Acronym	Description
AGD	Accountant General's Department
AUC	Asset under construction
BSN	Bank Simpanan Nasional
CR	Credit
CDS	Central Depository Securities
CGU	Cash Generating Unit
DR	Debit
EIR	Effective Interest Rate
FELDA	The Federal Land Development Authority
FIFO	First In First Out
EFT	Electronic Fund Transfer
FGOM	Federal Government of Malaysia
FPA	Financial Procedure Act
F.V.	Fair Value
GGS	General Government Sector
IFRS	International Financial Reporting Standard
IPSAS	International Public Sector Accounting Standards
JANM	Jabatan Akauntan Negara Malaysia
MGS	Malaysian Government Securities
MoF	Ministry of Finance Malaysia
MPSAS	Malaysian Public Sector Accounting Standards
PFC	Public Financial Corporations sector
PFI	Private Finance Initiative
PNFC	Public Non-Financial Corporations sector
PPE	Property, plant and equipment
PPP	Public Private Partnership
RM	Ringgit Malaysia
U.S.	The United States of America
USD	American Dollar

Glossary

Accounting basis is the accrual, modified accrual, modified cash or cash basis of accounting.

Accounting policies are the specific principles, bases, conventions, rules and practices applied by the entity in preparing and presenting financial statements.

Accrual basis is the accounting basis under which transactions and other events are recognised when they occur (and not only when cash or its equivalent is received or paid). Therefore, transactions and events are recorded in the accounting records and recognised in the financial statements of the periods to which they relate. The elements recognised under accrual accounting are assets, liabilities, net assets/equity, revenue and expenses.

Active market is a market in which: a) the items traded are homogeneous; b) willing buyers and sellers can normally be found at any time; and c) prices are available to the public.

Actual amounts (for budgetary purposes) are presented as part of the comparison schedule as well as a basis of a reconciliation schedule, resulting from the execution of the budget. For the purposes of MPSAS 24 – Presentation of budget information in financial statements, they include actual expenses and obligations that are comparable to the final budget presented.

Actuarial gains and losses comprise: a) experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred); and b) the effects of changes in actuarial assumptions.

Amortization is the systematic allocation of the amortizable amount of an intangible asset over its estimated useful life.

Appropriation is an authorization granted by a legislative body to allocate funds for purposes specified by the legislature or similar authority.

Assets are resources controlled by the entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity. Assets used to deliver goods and services in accordance with the Entity's objectives, but which do not directly generate net cash inflows, are often described as having a service potential.

Associate is an entity in which an investor has significant influence and that is neither a controlled entity nor a joint venture of the investor.

Betterment: The cost incurred to enhance the service potential of asset is a betterment. Service potential may be enhanced when there is an increase in the previously assessed service capacity, associated operating costs are lowered, the useful life is extended or the quality of output is improved. The cost incurred in the maintenance of the service potential of an asset is a repair, not a betterment.

Borrowing costs are interest and other expenses incurred by an entity in connection with borrowings.

Carrying amount of a liability is the amount at which a liability is recognised in the statement of financial position.

Carrying amount of an asset is the amount at which an asset is recognised in the statement of financial position after deducting any accumulated depreciation and accumulated impairment losses thereon.

Cash consists of cash on hand and demand deposits.

Glossary (continued)

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to an insignificant risk of changes in value.

Cash flows are inflows and outflows of cash and cash equivalents.

Cash-generating assets are assets held to generate a commercial return.

Cash-generating unit is the smallest identifiable group of assets held with the primary objective of generating a commercial return that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets.

Change in accounting estimate is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not a correction of errors.

Change in accounting policy is a change from one basis of accounting to another basis of accounting. A change in the accounting treatment, recognition or measurement of a transaction, event or condition within a basis of accounting is also regarded as a change in accounting policy.

Closing rate is the spot exchange rate at the reporting date – i.e. the exchange rate used to translate foreign currency monetary balances at the end of a reporting period.

Commitments are obligations to outside organisation or individuals that will become liabilities if and when the terms of contracts, agreements or legislation are met.

Consolidated financial statements are the financial statements of an economic entity presented as those of a single entity.

Construction contract is a contract or a similar binding arrangement specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function, or their ultimate purpose or use.

Constructive obligation is an obligation that derives from the Entity's actions where: a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

Contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

Contingent liability is: a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or b) a present obligation that arises from past events but which is not recognized because it is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation or because the amount of the obligation cannot be measured with sufficient reliability.

Contract: An agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable .

Contractual commitment: Represents a legal obligation to outside organization or individual as a result of contract.

Glossary (continued)

Control is the power to govern the financial and operating policies of another entity so as to benefit from its activities.

Controlled entity is an entity under the control of another entity (known as the controlling entity).

Controlling entity is an entity that has one or more controlled entities.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction.

Cost method is a method of accounting for an investment whereby it is recognized at cost. Revenue from the investment is recognized only to the extent that the investor is entitled to receive distributions from accumulated surpluses arising after the date of acquisition.

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

Current replacement cost is the cost the entity would incur to acquire the asset on the reporting date.

Deferred revenue: Amounts received before the transactions or events that give rise to revenue occurs.

Defined benefit plans are post-employment benefit plans other than defined contribution plans.

Defined contribution plans are post-employment benefit plans under which the entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior financial periods.

Depreciated replacement cost is an approach where an asset's present value is determined based on cost to replace the asset's gross service potential after taking into account its accumulated depreciation over consumed service potential asset life.

Depreciation is the systematic allocation of the depreciable amount of a tangible asset over its estimated useful life.

Effective interest rate is the interest rate on a loan/financial product restated from the nominal interest rate as an interest rate with annual compound interest payable in arrears.

Employee benefits are all forms of consideration given by the entity in exchange for service rendered by employees. Employee benefits mean all entitlements, salaries, allowances, benefits and incentives.

Entities include federal ministries, federal departments and federal commission from FGOM.

Equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

Events after the reporting date are those events, both favorable and unfavorable, that occur between the reporting date and the date when the financial statements are authorized for issue. Two types of event can be identified -adjusting and non-adjusting events.

Exchange difference is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at different exchange rates.

Glossary (continued)

Exchange rate is the ratio for exchange of two currencies.

Exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

Expenses are decreases in economic benefits or service potential during the reporting period in the form of outflows or consumption of assets or incurrence of liabilities that result in decreases in net assets/equity, other than those relating to distributions to owners.

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

Finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset to the lessee. Title may or may not eventually be transferred.

Financial asset is any asset that is: a) cash; b) a contractual right to receive cash or another equivalent asset from another entity; c) a contractual right to exchange financial instruments with another entity under conditions that are potentially favourable; or d) an equity instrument of another entity.

Financial instrument is any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial liability is any liability that is a contractual obligation: a) to deliver cash or another financial asset to another entity; or b) to exchange financial instruments with another entity under conditions that are potentially unfavorable.

Financing activities are activities that result in changes in the size and composition of the contributed capital and borrowings of the entity.

Foreign currency is a currency other than the functional currency of the entity.

Foreign operation is an entity that is a controlled entity, associate, joint venture or branch of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity.

Functional currency is the currency of the primary economic environment in which the entity operates. For the entity this is considered to be the RM.

Impairment is a loss in the future economic benefits or service potential of an asset, over and above the systematic recognition of the loss of the asset's future economic benefits or service potential through depreciation.

Inception of the lease is the earlier of the date on which a lessor and lessee enter into a lease agreement and the date on which the parties commit to the principal provisions of the lease. As at this date a) a lease is classified as either an operating or a finance lease; and b) in the case of a finance lease, the amounts to be recognised at the commencement of the lease term are determined.

Intangible assets are identifiable non-monetary assets without physical substance.

Interest cost is the increase during a financial period in the present value of a defined benefit obligation which arises because the benefits are one period closer to settlement.

Glossary (continued)

Inventories are assets: a) in the form of materials or supplies to be consumed in the production process; b) in the form of materials or supplies to be consumed or distributed in the rendering of services; c) held for sale or distribution in the ordinary course of operations; or d) in the process of production for sale or distribution.

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Investment property is property (land or a building – or part thereof) held to earn rentals or for capital appreciation or both, rather than for: a) use in the production or supply of goods or services or for administrative purposes; or b) sale in the ordinary course of operations.

Joint control is the agreed sharing of control over an activity by a binding arrangement.

Joint venture is a binding arrangement whereby two or more parties are committed to undertake an activity that is subject to joint control.

Key management personnel are defined under MPSAS as those officials who are responsible for the planning, directing and controlling activities of the reporting entity.

Lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.

Lease term is the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

Legal obligation is an obligation that derives from: a) a contract (through its explicit or implicit terms); or b) legislation; or c) other operation of law.

Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.

Liquidity risk is 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 guarantees are a type of contingent liability.

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. Market risk comprises three types of risk: currency risk, interest rate risk, and other price risk.

Market value is the amount obtainable from the sale or payable on the acquisition, of a financial instrument in an active market.

Material omissions or misstatements are omissions or misstatements of items which could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. Materiality depends on the nature and size 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.

Glossary (continued)

Modified cash basis is the accounting basis under which revenue and expenses are usually reported when cash is received or a payment is made, but with some exceptions. Notably, expenditures can be reported prior to the payment of cash on the basis that the cash will need to be paid out soon after the end of the financial year. Under this basis, investments in physical assets and intangibles are expensed immediately, and employee benefit liabilities are not required to be reported in the financial statements.

Monetary items are units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency.

Net assets/equity is the residual interest in the assets of the entity after deducting all its liabilities. This is the residual measure in the statement of financial position.

Net realizable value is the estimated selling price in the ordinary course of operations less the estimated costs of completion and the estimated costs necessary to make the sale, exchange or distribution.

Non-cash-generating assets are assets other than cash-generating assets.

Non-exchange transactions are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

Non-monetary items are items that are not monetary items.

Notes are disclosures which contain information in addition to that presented in the statement of financial position, statement of financial performance, statement of changes in net assets/equity and cash flow statement. Notes provide narrative descriptions or disaggregation of items disclosed in those statements and information about items that do not qualify for recognition in those statements.

Obligating event is an event that creates a legal or constructive obligation that results in the entity having no realistic alternative to settling that obligation.

Operating activities are the activities of the entity that are not investing or financing activities.

Operating lease is a lease other than a finance lease.

Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) that do not fall due wholly within 12 months after the end of the financial period in which the employees render the related service.

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

Past service cost is the increase in the present value of the defined benefit obligation for employee service in prior financial periods, resulting in the current financial period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service cost may be either positive (where benefits are introduced or improved) or negative (where benefits are reduced).

Glossary (continued)

Percentage of completion method is an accounting method to account for asset under construction.

Plan assets comprise: a) assets held by a long-term employee benefit fund; and b) qualifying insurance policies.

Post-employment benefits are employee benefits (other than termination benefits) that are payable after the completion of employment.

Present value is the future amount of money that has been discounted to reflect its current value, as if it existed today.

Post-employment benefit plans are formal or informal arrangements under which the entity provides post-employment benefits for one or more employees.

Present value of a defined benefit obligation is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior financial periods.

Presentation currency is the currency in which the financial statements are presented. For the entity this is the RM.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior financial periods, arising from a failure to use or a misuse of reliable information that a) was available when financial statements for those financial periods were authorized for issue; and b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Projected unit credit method is used to determine the present value of a defined benefit obligation and the related current service cost and the applicable past service costs.

Property, plant and equipment, or **PPE**, are tangible items that are a) held for use in the production or supply of goods or services, for rental to others or for administrative purposes; and b) expected to be used during more than one reporting period. Property, plant and equipment should not be confused with inventories as defined above, although they may be counted and physically verified.

Provision is a liability of uncertain timing or amount.

Private finance initiatives is a form of public private partnership where the public sector is able to secure the provision of public services from the private sector.

Public private partnership is a government service or private business venture which is funded and operated through a partnership of government and one or more private sector companies.

Qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

Recoverable amount is the higher of an asset's or a cash-generating unit's fair value less costs to sell and its value in use.

Related parties are parties considered to be related if one party has the ability to control, or exercise significant influence over, the other party in making financial and operating decisions, or if the related party entity and another entity are subject to common control.

Glossary (continued)

Related party transaction is a transfer of resources or obligations between related parties, regardless of whether a price is charged. Related party transactions exclude transactions with any other entity that is a related party solely because of its economic dependence on the reporting entity or the government of which it forms part.

Remuneration of key management personnel is any consideration or benefit derived directly or indirectly by key management personnel from the reporting entity for services provided in their capacity as members of the governing body or otherwise as employees of the reporting entity.

Reporting date is the date of the last day of the reporting period to which the financial statements relate. In the case of the Entity, it is 31st December of each year.

Reporting period is the basic accounting period that applies to all financial recording and reporting of the Entity. The financial period begins 1st January, lasts for 12 months and ends on 31st December.

Residual value is the estimated amount that the entity would currently obtain from disposal of an asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

Retrospective application is the application of a new accounting policy to transactions, other events and conditions as if that policy had always been applied.

Retrospective restatement is a revision, correcting the recognition, measurement and disclosure of amounts of elements of financial statements as if a prior period error had never occurred.

Revenue is the gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.

Segment is a distinguishable activity or group of activities of the entity for which it is appropriate to separately report financial information for the purpose of evaluating the entity's past performance in achieving its objectives and for making decisions on the future allocation of resources.

Segment assets are those operating assets that are employed by a segment in its operating activities and that are either directly attributable to the segment or that can be allocated to the segment on a reasonable basis.

Segment expense is an expense resulting from the operating activities of a segment that is directly attributable to the segment and the relevant portion of an expense that can be allocated on a reasonable basis to the segment. These include expenses relating to the provision of goods and services to external parties, and expenses relating to transactions with other segments of the same entity.

Segment liabilities are those operating liabilities that result from the operating activities of a segment and that are either directly attributable to the segment or can be allocated to the segment on a reasonable basis.

Segment revenue is revenue reported in the entity's statement of financial performance that is directly attributable to a segment and the relevant portion of entity revenue that can be allocated on a reasonable basis to a segment, whether from budget appropriations or similar, grants, transfers, fines, fees or sales to external customers or from transactions with other segments of the same entity.

Glossary (continued)

Separate financial statements are those presented by a controlling entity, an investor in an associate or a venturer in a jointly controlled entity, in which the investments are accounted for on the basis of the direct net assets/equity interest rather than on the basis of the reported results and net assets of the investees.

Service potential is the anticipated future benefits to be obtained from an asset. Assets that are used to deliver goods and services in accordance with the Entity's objectives but which do not directly generate net cash inflows are often described as embodying service potential.

Short-term employee benefits are employee benefits (other than termination benefits) that fall due wholly within 12 months after the end of the financial period in which the employees render the related service.

Significant influence is the power to participate in the financial and operating policy decisions of an activity but is not control or joint control over those policies.

Statement of financial performance is a financial statement that measures an entity's financial performance over a specific accounting period.

Statement of financial position is a financial statement that summarizes an entity's asset and liabilities at a specific point in time.

Spot exchange rate is the exchange rate for immediate delivery.

Termination benefits are employee benefits payable as a result of either: a) the Entity's decision to terminate an employee's employment before the normal retirement date; or b) an employee's decision to accept voluntary redundancy in exchange for these benefits.

Transfers are inflows of future economic benefits or service potential from non-exchange transactions, other than taxes.

Useful life is either: a) the period over which an asset is expected to be available for use by the Entity; or b) the number of production or similar units expected to be obtained from the asset by the Entity.

Value in use of a cash-generating asset is the present value of the estimated future cash flows expected to be derived from the continuing use of an asset and from its disposal at the end of its useful life.

Venturer is a party to a joint venture and has joint control over that joint venture.