



IFRS “vs” FRS 102 for Investment Funds

Introduction

The purpose of this paper is to highlight the significant differences between International Financial Reporting Standards as adopted by the European Union (“IFRS”) and the recently developed FRS 102 (the “New Irish GAAP”) as they apply to investment funds. All Irish domiciled investment funds (provided they are not listed, or those listed but do not prepare consolidated accounts*) will have the option to choose between these reporting standards even if they have already adopted IFRS for their investment funds. This paper will focus on the main differences between the two GAAPs as they relate to valuation of investments, key disclosures, consolidation and revenue recognition for investment funds.

FRS 102 was developed by the Financial Reporting Council (“FRC”) along with FRS 100 and 101, to simplify and standardise financial reporting. It aims to make financial reports more understandable for the user by modernising the way financial reports are completed and in addition to that the FRC have replaced the “long toothed” Irish GAAP with the FRS 102 which stands at just a few hundred pages. The standard is effective for accounting periods beginning on or after the 1 January 2015.

**Parent companies preparing group accounts with securities (equity or debt) admitted to trading on a regulated market in an EU member state are required to apply IFRS*

Relevant Accounting Standards

IFRS	FRS 102
IAS 32 - Financial Instruments: Presentation	Policy choice of
IAS 39 - Financial Instruments: Recognition and Measurement	a) Section 11 - Basic Financial Instruments, Section 12 - Other Financial Instrument Issues, Section 22 - Liabilities and Equity, and Section 34 - Specialised Activities as it applies to financial institutions;
IFRS 9 - Financial Instruments	or;
IFRS 7 - Financial Instruments: Disclosures	

IFRS	FRS 102
IFRS 13 - Fair Value Measurement	b) Recognition and Measurement provisions of IAS 39 (IFRS 9) and the disclosure requirements of Sections 11, 12 and 34 as it relates to financial institutions.
IFRS 7/ IFRS 12 Amendment for offsetting	Not applicable under FRS 102
IFRS 10 Investments Entities consolidation exemption	Section 9 – Held for subsequent resale

Significant Financial Reporting Areas of Focus

Classification of Financial Assets	Financial assets are classified under four categories under IFRS [Appendix A (1)] and they are classified under two categories under FRS 102 [Appendix B (1)].	Consideration Points: <ul style="list-style-type: none"> • For money market funds the investments may be “non-complex” under section 11 of FRS 102 and may be held at amortised cost.
Initial Measurement	Under FRS 102, there is no substantial differences in the initial measurement between IFRS [Appendix A (2)] and FRS 102 [Appendix B (2)] unless the arrangement constitutes a financing transaction.	Consideration Points: <ul style="list-style-type: none"> • None

<p>Subsequent Measurement</p>	<p>Under IFRS, the classification of the assets drives the subsequent measurement with assets classified at Fair Value through Profit or Loss (“FVTPL”) and Available for sale” (“AFS”) are measured at fair value and those classified as Held to Maturity (“HTM”) or Loans and Receivables (“L&R”) are measured at cost.</p> <p>Under FRS 102 Section 11, financial instruments that meet certain conditions shall be measured at amortised cost and under Section 12, an entity shall measure all financial instruments at fair value and recognise changes in fair value in profit or loss.</p> <p>For more detail on the exceptions under IFRS and FRS 102 to the above treatments refer to Appendix A (3) and Appendix B (3) respectively.</p>	<p>Consideration Points:</p> <ul style="list-style-type: none"> • For investment funds financial instruments will usually be held at fair value so there will be little difference between the two GAAPs.
<p>Definition of Fair Value</p>	<p>Fair value under IFRS 13 is an “exit price” which may be different from fair value under FRS 102. The definition of Fair Value under IFRS is set out in Appendix A (4) while the definition and relevant hierarchy under FRS 102 are set out at Appendix B (4) and B (7) respectively. In determining fair value for financial assets that are quoted in an active market, FRS 102 requires BID pricing while IFRS 13 is more flexible, allowing use of mid-market or other pricing conventions.</p> <p>FRS 102 gives an accounting policy choice of applying either:</p> <ol style="list-style-type: none"> a) Sections 11 and 12 in full; or b) Recognition and measurement principles of IAS 39 (IFRS 9) 	<p>Consideration Points:</p> <ul style="list-style-type: none"> • The option to apply the recognition and measurement principals of IAS 39 (IFRS 9) will enable Irish GAAP accounts to be identical to IFRS accounts in the measurement of financial assets and liabilities at fair value through profit and loss.

Definition of Amortised Cost	No difference in the definition of amortised cost between IFRS [Appendix A (5)] and FRS 102 [Appendix B (5)].	Consideration Points: <ul style="list-style-type: none"> • None
Classification of Redeemable Participating Shares	<p>There is no difference in the classification of redeemable participating shares under IFRS and FRS 102. Under both standards puttable instrument that give the right to sell the instrument back to the issuer are treated as equity only when the class of instrument is subordinate to all other classes of instruments (among other conditions), so where there are more than one share class with differing characteristics they will be treated as debt under both standards.</p> <p>For more detail under IFRS and FRS 102 refer to Appendix A (8) and Appendix B (8) respectively.</p>	Consideration Points: <ul style="list-style-type: none"> • None
Disclosures	<p>Generally, there are fewer disclosures in FRS 102 Sections 11, 12 and 34. However, an investment fund will generally meet the definition of a "financial institution" under FRS 102 then the disclosures would be similar to those required under IFRS 7.</p> <p>Under IFRS there are additional disclosures for level 3 financial assets and liabilities.</p> <p>For more detail on the disclosures under IFRS and FRS 102 refer to Appendix A (6) and Appendix B (6) respectively.</p>	Consideration Points: <ul style="list-style-type: none"> • While the disclosures requirements are similar between the two GAAPs it would be expected that under FRS 102 there would be an opportunity to reduce the level of disclosure in the risk notes. Refer to Appendix A (6) and Appendix B (6) for the disclosure requirements.

Fair Value Hierarchy	<p>The criteria for the fair value hierarchy levels are different and there are additional disclosures for level 3 under IFRS 13. Refer Appendix B (6 & 7).</p>	<p>Consideration Points:</p> <ul style="list-style-type: none"> The fair value hierarchy differs between the two GAAPs as further explained in the Appendices. This will be the most significant difference for users of the financial statements as a fund that primarily held level 2 investments including fixed income securities and Over the Counter (“OTC”) derivatives, including non-complex derivatives, may now find its investments classified in Category C under FRS 102. Readers of financial statements may automatically infer that Category C under FRS 102 and Level 3 under IFRS 13 are comparable when in reality there are significant differences in the classifications.
Offsetting	<p>The IASB amended IFRS 7 Financial Instruments: Disclosures to include offsetting requirements for financial assets and liabilities. The IASB also made amendments to IAS 32 to clarify the criteria for offsetting for entities, and also to address inconsistencies in their application. Entities are required to provide both net and gross information for certain assets and liabilities as well as a table in the notes to the financial statements that sets out the Gross and Net positions of all financial instruments that can be offset through a netting arrangement, including the impact of any collateral arrangements.</p> <p>There is currently no such tabular and quantitative disclosure requirements under FRS 102.</p>	<p>Consideration Points:</p> <ul style="list-style-type: none"> The offsetting disclosures under IFRS can be complex, particularly for funds trading securities with multiple brokers. FRS 102 does not require similar tabular and quantitative disclosures, albeit a comparable disclosure requirement may be introduced under FRS 102 in the future.

Consolidation Exemption	<p>Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27), issued in October 2012, introduced an exception to the principal that all subsidiaries shall be consolidated. The amendments define an investment entity and require a parent that is an investment entity to measure its investments in particular subsidiaries at fair value through profit or loss in accordance with IFRS 9 (IAS39) instead of consolidating those subsidiaries. In addition, the amendments introduce new disclosures requirements related to investment entities in IFRS 12 and IAS 27.</p> <p>Under FRS 102 subsidiaries are required to be consolidated unless they are being “held for subsequent resale”.</p>	<p>Consideration Points:</p> <ul style="list-style-type: none"> • The Irish GAAP standard is not as explicit as when an entity can avoid consolidation as the IFRS, requiring greater management judgement.
Revenue Recognition	<p>No significant differences in the recognition of revenue between IFRS and FRS 102 for investment funds.</p>	<p>Consideration Points:</p> <ul style="list-style-type: none"> • None
Statement of Cash Flows	<p>The Statement of Cash Flows is a Primary Statement required in all IFRS accounts. Under FRS 102 there is an exemption from preparing a Statement of Cash Flows where the entity provides a statement of changes in net assets and substantially all of the entity’s investments are considered “Highly Liquid” and carried at market value (no change from the existing Irish GAAP).</p>	<p>Consideration Points:</p> <ul style="list-style-type: none"> • The exemption under FRS 102 can help reduce an administrative burden relating to the production of the statement of cash flows, however it is important to consider whether the fund’s investments meet the “Highly Liquid” definition.



Other Considerations:

The detail set out above focuses on the differences between IFRS and the New Irish GAAP from an accounting treatment perspective, however there are other factors that practitioners and management may wish to consider. IFRS is an internationally recognised GAAP that may be more comparable to US GAAP than the New Irish GAAP. However IFRS is subject to frequent revisions and updates, while the FRC has agreed to only update FRS 102 every 3 years. Furthermore there may be other factors such as transitional arrangements, accounting software, client preference etc. that should be considered when choosing your GAAP.

It is also should be noted that Irish domiciled investment fund companies have the choice to adopt alternative GAAPs, specifically those that apply in the United States of America, Canada or Japan.

Appendix A – IFRS

(1) Classification of Financial Assets

Every financial asset that falls within the scope of IAS 39 should be classified into one of the following four primary categories:

- at fair value through profit or loss (FVTPL);
- available-for-sale (AFS);
- loans and receivables (L&R); or
- held-to-maturity (HTM);

(2) Initial Measurement – IAS 39:43

IAS 39:43 requires that all financial instruments are initially recognised at fair value plus or minus, in the case of a financial asset or liability that is not classified as at FVTPL, transaction costs that are directly attributable to the acquisition or issue of the asset or liability.

(3) Subsequent Measurement

The classification of financial assets and liabilities is important because it drives the subsequent measurement of the asset or liability (i.e. either at fair value or amortised cost). Financial assets and liabilities classified at FVTPL and AFS are measured at fair value, while those classified as HTM or L&R are measured at amortised cost. The only exception to this rule arises in respect of equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured (and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments), which are instead held at cost. It should be noted that the circumstances under which equity instruments can be measured at cost is extremely rare.

(4) Definition of Fair Value – IFRS 13: Appendix A

Fair value is defined as “[t]he price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date”. [IFRS 13: Appendix A] .

This basis for measuring fair value is commonly referred to as an *exit price* approach because it reflects the price at which a market participant that holds the asset or owes the liability could *exit* that asset or liability by selling the asset or transferring the liability to a third party.

(5) Definition of Amortised Cost – IAS 39:9

Amortised cost is defined as the amount at which the financial asset or financial liability is measured at:

- (a) initial recognition
- (b) minus principal repayments,
- (c) plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and
- (d) minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

(6) Disclosures – IFRS 7:6

IFRS requires certain disclosures to be presented by category of instrument based on the IAS 39 measurement categories. Certain other disclosures are required by class of financial instrument. For those disclosures an entity must group its financial instruments into classes of similar instruments as appropriate to the nature of the information presented.

The two main categories of disclosures required by IFRS 7 are:

1. information about the significance of financial instruments.
2. information about the nature and extent of risks arising from financial instruments

Specific disclosures required

To meet the IFRS 13 disclosure objective, the following minimum disclosures are required for each class of assets and liabilities measured at fair value (including measurements based on fair value within the scope of this IFRS) in the statement of financial position after initial recognition (note these are requirements have been summarised and additional disclosure is required where necessary): [IFRS 13:93]

- the fair value measurement at the end of the reporting period*
- for non-recurring fair value measurements, the reasons for the measurement*
- the level of the [fair value hierarchy](#) within which the fair value measurements are categorised in their entirety (Level 1, 2 or 3)*
- for assets and liabilities held at the reporting date that are measured at fair value on a recurring basis, the amounts of any transfers between Level 1 and [Level 2](#) of the fair value hierarchy, the reasons for those transfers and the entity's policy for determining when transfers between levels are deemed to have occurred, separately disclosing and discussing transfers into and out of each level
- for fair value measurements categorised within [Level 2](#) and [Level 3](#) of the fair value hierarchy, a description of the valuation technique(s) and the inputs used in the fair value measurement, any change in the valuation techniques and the reason(s) for making such change (with some exceptions)*
- for fair value measurements categorised within [Level 3](#) of the fair value hierarchy, quantitative information about the significant unobservable inputs used in the fair value measurement (with some exceptions)
- for recurring fair value measurements categorised within [Level 3](#) of the fair value hierarchy, a reconciliation from the opening balances to the closing balances, disclosing separately changes during the period attributable to the following:
 - total gains or losses for the period recognised in profit or loss, and the line item(s) in profit or loss in which those gains or losses are recognised – separately disclosing the amount included in profit or loss that is attributable to the change in unrealised gains or losses relating to those assets and liabilities held at the end of the reporting period, and the line item(s) in profit or loss in which those unrealised gains or losses are recognised
 - total gains or losses for the period recognised in other comprehensive income, and the line item(s) in other comprehensive income in which those gains or losses are recognised
 - purchases, sales, issues and settlements (each of those types of changes disclosed separately)
 - the amounts of any transfers into or out of [Level 3](#) of the fair value hierarchy, the reasons for those transfers and the entity's policy for determining when transfers between levels are deemed to have occurred. Transfers into [Level 3](#) shall be disclosed and discussed separately from transfers out of [Level 3](#)
- for fair value measurements categorised within [Level 3](#) of the fair value hierarchy, a description of the valuation processes used by the entity
- for recurring fair value measurements categorised within [Level 3](#) of the fair value hierarchy:

- a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement. If there are interrelationships between those inputs and other unobservable inputs used in the fair value measurement, the entity also provides a description of those interrelationships and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement
- for financial assets and financial liabilities, if changing one or more of the unobservable inputs to reflect reasonably possible alternative assumptions would change fair value significantly, an entity shall state that fact and disclose the effect of those changes. The entity shall disclose how the effect of a change to reflect a reasonably possible alternative assumption was calculated
- if the highest and best use of a non-financial asset differs from its current use, an entity shall disclose that fact and why the non-financial asset is being used in a manner that differs from its highest and best use*.

** in the list above indicates that the disclosure is also applicable to a class of assets or liabilities which is not measured at fair value in the statement of financial position but for which the fair value is disclosed. [IFRS 13:97]*

Quantitative disclosures are required to be presented in a tabular format unless another format is more appropriate. [IFRS 13:99]

(7) Fair Value Hierarchy – IFRS 13

The fair value hierarchy is based on three types of inputs based on the lowest level of input significant to the overall fair value:

- Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date. [IFRS 13:76]
- Level 2 – Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly [IFRS 13:81]
- Level 3 inputs are unobservable inputs for the asset or liability [IFRS 13:81]

(8) Classification of an instrument as liability or equity - IAS 32

A puttable instrument is classified as equity if it meets all of the following criteria: [IAS 32:16A]

- a) The holder is entitled to a pro rata share of the entity's net assets in the event of the entity's liquidation;

- b) The instrument is in the class of instruments that is subordinate to all other classes of instruments;
- c) All financial instruments in the class of instruments that is subordinate of all other classes of instruments have identical features. For example, they must all be puttable, and the formula or other method used to calculate the repurchase or redemption price is the same for all instruments in that class;
- d) Apart from the contractual obligation for the issuer to repurchase or redeem the instrument for cash or another financial asset, the instrument does not include any contractual obligation to deliver cash or another financial asset to another entity, or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity, and it is not a contract that will or may be settled in the entity's own equity instruments as set out in subparagraph (b) of the definition of a financial liability; and
- e) The total expected cash flows attributable to the instrument over the life of the instrument are based substantially on the profit or loss, the change in the recognised and unrecognised net assets of the entity over the life of the instruments (excluding any effects of the instrument).

Profit or loss and the change in the recognised net assets should be measured in accordance with the relevant IFRSs. [IAS 32:AG14E]

For a puttable instrument to be classified as equity, in addition to meeting the above criteria in IAS 32:16A, the issuer must have no other financial instrument or contract that has: [IAS 32:16B]

- a) Total cash flows based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity (excluding any effects of such instrument or contract); and
- b) The effect of substantially restricting or fixing the residual return to the puttable instrument holders.

When applying IAS 32:16B (a) and (b), the issuer is not required to consider non-financial contracts with a holder of an instrument described in IAS 32:16A that have contractual terms and conditions that are similar to the contractual terms and conditions of an equivalent contract that might occur between a non-instrument holder and the issuing entity.

Appendix B – FRS 102

(1) Classification of Financial Assets - FRS 102 11:8 & FRS 102 12:3

Under FRS 102, financial instruments are classified as either basic instruments or complex instruments and the accounting treatment is determined by Section 11 and Section 12 respectively.

An entity shall account for the following financial instruments as basic financial instruments in accordance with Section 11:

- (a) cash;
- (b) a debt instrument (such as an account, note, or loan receivable or payable) that meets the conditions in paragraph 11.9;
- (c) commitments to receive or make a loan to another entity that:
 - i. cannot be settled net in cash; and
 - ii. when the commitment is executed, are expected to meet the conditions in paragraph 11.9; and
- (d) an investment in non-convertible preference shares and non-puttable ordinary shares or preference shares.

Section 12 applies to all financial instruments except the following:

- (a) Those covered by Section 11.
- (b) Investments in subsidiaries, associates and joint ventures.
- (c) Employers' rights and obligations under employee benefit plans.
- (d) Insurance contracts (including reinsurance contracts) that the entity issues and reinsurance contracts that the entity holds.
- (e) Financial instruments that meet the definition of an entity's own equity and the equity component of compound financial instruments issued by the reporting entity that contain both a liability and an equity component.
- (f) Leases unless the lease could, as a result of non-typical contractual terms, result in a loss to the lessor or the lessee.
- (g) Contracts for contingent consideration in a business combination. This exemption applies only to the acquirer.
- (h) Any forward contract between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination at a future acquisition date. The term of the forward contract should not exceed a reasonable period normally necessary to obtain any required approvals and to complete the transaction.

- (i) Financial instruments, contracts and obligations to which Section 26 Share-based Payment applies, except for contracts within the scope of paragraph 12.5.
- (j) Financial instruments issued by an entity with a discretionary participation feature.
- (k) Reimbursement assets.
- (l) Financial guarantee contracts

(2) Initial Measurement – FRS 102 11:13 & FRS 102 12:7

When a financial asset or financial liability is recognised initially, under Section 11 an entity shall measure it at the transaction price unless the arrangement constitutes, in effect, a financing transaction, while under Section 12 an entity shall measure it at its fair value, which is normally the transaction price.

A financing transaction may take place in connection with the sale of goods or services, for example, if payment is deferred beyond normal business terms or is financed at a rate of interest that is not a market rate. If the arrangement constitutes a financing transaction, the entity shall measure the financial asset or financial liability at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

(3) Subsequent Measurement – FRS 102 11:14 & FRS 102 12:8

For assets classified under Section 11, at the end of each reporting period, an entity shall measure financial instruments as follows, without any deduction for transaction costs the entity may incur on sale or other disposal:

Debt instruments that meet the conditions in paragraph 11.8(b) shall be measured at amortised cost using the effective interest method. Debt instruments that are payable or receivable within one year shall be measured at the undiscounted amount of the cash or other consideration expected to be paid or received unless the arrangement constitutes, in effect, a financing transaction. If the arrangement constitutes a financing transaction, the entity shall measure the debt instrument at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

- (a) Debt instruments that meet the conditions in paragraph 11.8(b) may upon their initial recognition be designated by the entity as at fair value through profit or loss provided doing so results in more relevant information, because either:

- (i) it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as ‘an accounting mismatch’) that would otherwise arise from measuring assets or debt instruments or recognising the gains and losses on them on different bases; or
 - (ii) a group of debt instruments or financial assets and debt instruments is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the entity’s key management personnel (as defined in Section 33 Related Party Disclosures, paragraph 33.6), for example members of the entity’s board of directors and its chief executive officer.
- (b) Commitments to receive a loan and to make a loan to another entity that meet the conditions in paragraph 11.8(c) shall be measured at cost (which sometimes is nil) less impairment.
- (c) Investments in non-convertible preference shares and non-puttable ordinary shares or preference shares shall be measured as follows (paragraphs 11.27 to 11.32 provide guidance on fair value):
- (i) if the shares are publicly traded or their fair value can otherwise be measured reliably, the investment shall be measured at fair value with changes in fair value recognised in profit or loss; and
 - (ii) all other such investments shall be measured at cost less impairment.

For assets classified under Section 12, at the end of each reporting period, an entity shall measure all financial instruments within the scope of Section 12 at fair value and recognise changes in fair value in profit or loss, except as follows:

- (a) investments in equity instruments that are not publicly traded and whose fair value cannot otherwise be measured reliably and contracts linked to such instruments that, if exercised, will result in delivery of such instruments, shall measure at cost less impairment; and
- (b) hedging instruments in a designated hedging relationship accounted for in accordance with paragraph 12.23.

(4) Definition of Fair Value - FRS 102 2:34

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

(5) Definition of Amortised Cost - FRS 102 11:15

The amortised cost of a financial asset or financial liability at each reporting date is the net of the following amounts:

- (a) the amount at which the financial asset or financial liability is measured at initial recognition;
- (b) minus any repayments of the principal;

- (c) plus or minus the cumulative amortisation using the effective interest method of any difference between the amount at initial recognition and the maturity amount;
- (d) minus, in the case of a financial asset, any reduction (directly or through the use of an allowance account) for impairment or collectability.

(6) Disclosures - FRS 102 34:23 & FRS 102 34:24

A financial institution shall disclose information that enables users of its financial statements to evaluate the nature and extent of credit risk, liquidity risk and market risk arising from financial instruments to which the financial institution is exposed at the end of the reporting period.

For each type of risk arising from financial instruments, a financial institution shall disclose:

- (a) the exposures to risk and how they arise;
- (b) its objectives, policies and processes for managing the risk and the methods used to measure the risk; and
- (c) any changes in (a) or (b) from the previous period.

Further disclosures for each of the main risk categories (Credit, Liquidity and Market) are required under Sections 34:25 to 34:30.

(7) Fair Value Hierarchy - FRS 102 11:27

An entity shall use the following hierarchy to estimate the fair value:

- (a) The best evidence of fair value is a quoted price for an identical asset in an active market. Quoted in an active market in this context means quoted prices are readily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted price is usually the current bid price.
- (b) When quoted prices are unavailable, the price of a recent transaction for an identical asset provides evidence of fair value as long as there has not been a significant change in economic circumstances or a significant lapse of time since the transaction took place. If the entity can demonstrate that

the last transaction price is not a good estimate of fair value (e.g. because it reflects the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distress sale), that price is adjusted.

(c) If the market for the asset is not active and recent transactions of an identical asset on their own are not a good estimate of fair value, an entity estimates the fair value by using a valuation technique. The objective of using a valuation technique is to estimate what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations.

(8) Classification of an instrument as liability or equity - FRS 102 22.4

Some financial instruments that meet the definition of a liability are classified as equity because they represent the residual interest in the net assets of the entity:

(a) A puttable instrument is a financial instrument that gives the holder the right to sell that instrument back to the issuer for cash or another financial asset or is automatically redeemed or repurchased by the issuer on the occurrence of an uncertain future event or the death or retirement of the instrument holder. A puttable instrument that has all of the following features is classified as an equity instrument:

- (i) It entitles the holder to a pro rata share of the entity's net assets in the event of the entity's liquidation. The entity's net assets are those assets that remain after deducting all other claims on its assets.
- (ii) The instrument is in the class of instruments that is subordinate to all other classes of instruments.
- (iii) All financial instruments in the class of instruments that is subordinate to all other classes of instruments have identical features.
- (iv) Apart from the contractual obligation for the issuer to repurchase or redeem the instrument for cash or another financial asset, the instrument does not include any contractual obligation to deliver cash or another financial asset to another entity, or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity, and it is not a contract that will or may be settled in the entity's own equity instruments as set out in paragraph 22.3(b) of the definition of a financial liability.



(v) The total expected cash flows attributable to the instrument over the life of the instrument are based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity over the life of the instrument (excluding any effects of the instrument).

(b) Instruments, or components of instruments, that are subordinate to all other classes of instruments are classified as equity if they impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation.