FINANCIAL INSTRUMENTS FACT SHEET #9

INVESTMENTS IN RESIDUAL INTERESTS		
Definition	A residual interest is any contract that represents an interest in the assets of one entity after deducting all of its liabilities. A residual interest includes contributions from owners, which may be evidenced by: (a) equity instruments or similar forms of unitised capital; (b) a formal designation of a transfer of resources (or a class of such transfers) by the parties to the transaction as forming part of an entity's net assets, either before the contribution occurs or at the time of the contribution; or (c) a formal agreement, in relation to the contribution, establishing or increasing an existing financial interest in the net assets of an entity. Typical examples include investments in controlled entities, and investments in listed or unlisted equity instruments.	Paragraph 2.1 and AG2.25-AG2.26
Scope	Investments in residual interests held by an entity are accounted for in terms of GRAP 104. Interests in the residual interests of controlled entities, associates or joint ventures are excluded from GRAP 104, except where the relevant Standards of GRAP require or permit application of GRAP 104, e.g. fair value required in separate financial statements or fair value permitted for significant influence in venture capital organisations.	Paragraph 1.3(a) and 1.5-1.7
Recognition	Recognise the investment when entity becomes party to the contractual provisions of the instrument. Consider whether trade date accounting is applicable for regular way purchases of investments in residual interests (typically when traded on an exchange).	Paragraph 3.1 and AG3.21-AG3.13
Classification	Investments in residual interests do not meet the solely payments of principal and interest test. They are therefore measured at fair value through surplus or deficit.	Paragraph 4.1-4.5 and AG4.1-AG4.67
	As a practical expedient, if a reliable measure of fair value cannot be determined, an entity may measure investments in residual interests at cost less impairment losses.	AG4.71-AG4.72
	Fair value cannot be reliably determined when there is no active market and (a) the variability in the range of reasonable fair value estimates is significant or (b) the probabilities of the various estimates within the range cannot be reasonably assessed.	Paragraph AG5.47-AG5.48
Initial measurement	Fair value, plus transaction costs (if at cost). Fair value is the price agreed by a willing buyer and a willing seller in an arm's length transaction. Fair value is determined based on the following: • A quoted price in an active market. • If no active market, using a valuation technique.	Paragraph 5.1 and AG5,1, AG5.34-AG5.49
	The difference between the transaction price and fair value is recognised as follows: • Surplus or deficit - If fair value is determined using level 1 inputs or a	Paragraph 5.2 and AG5.4

This Fact Sheet explains the Secretariat's views on the possible accounting treatment of public sector transactions based on the principles in GRAP 104 on Financial Instruments (revised in 2019). This Fact Sheet accompanies, and is not a replacement for, the complete text of GRAP 104 Financial Instruments. The Fact Sheet outlines the most common features and accounting considerations related to a particular transaction. The accounting may differ depending on the facts and circumstances of individual arrangements. This Fact Sheet has not been reviewed, approved or otherwise acted on by the ASB.

	valuation technique that only uses data from observable markets. • Deferred on the statement of financial position – When any other valuation basis used. The principles for the recognition of the difference on initial recognition do not apply to concessionary investments.	
	Concessionary investments are investments made in another entity where part is an investment in the residual interest of the entity and part is a non-exchange transaction.	Paragraph 5.4-5.6 and AG5.25-AG5.27
Subsequent measurement	Fair value, or as a practical expedient, cost less accumulated impairment losses.	Paragraph 5.7-5.8, 5.10-5.11 and AG5.34-AG5.49
	Subsequent gains and losses are recognised in surplus or deficit.	Paragraph 5.42
Impairment losses **(only where cost is used)**	Impairment losses are only recognised when <u>cost</u> is used. Impairment losses are recognised based on whether there is objective evidence that a loss has been incurred (incurred loss impairment model). This assessment is based on the criteria in the definition of a 'credit impaired financial asset'. A credit-impaired financial asset is a financial asset that is credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred. Evidence that a financial asset is credit-impaired includes observable data about the following events: (a) significant financial difficulty of the issuer or the borrower; (b) a breach of contract, such as a default or past due event; (c) the lender(s) of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession(s) that the lender(s) would not otherwise consider; (d) it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; (e) the disappearance of an active market for that financial asset because of financial difficulties; or (f) the purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses. It may not be possible to identify a single discrete event—instead the combined effect of several events may have caused financial assets to become credit-impaired. Impairment losses are measured as the difference between the carrying amount of the financial asset and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Any impairment losses recognised cannot be reversed.	Paragraph 2.1 (definition of credit impaired instrument) and 5.36

Derecognition	An investment in a residual interest is derecognised (in part or in its entirety) when: (a) the contractual cash flows have expired, are settled or waived; (b) the entity transfers to another party substantially all of the risks and rewards of ownership of the financial asset; or (c) the entity has retained significant risks and rewards, but transferred control to another party, and that party has the practical ability to sell the asset to an unrelated third party.	Paragraph 6.1-6.15 and AG6.1-AG6.14
	Consider if trade date accounting is applicable.	Paragraph 3.1
	Gains and losses that arise from the derecognition of a residual interest in another entity are recognised in surplus or deficit.	Paragraph 5.42 and 5.43
Presentation and disclosure	An entity considers the presentation and disclosure requirements in GRAP 104 and applies materiality when preparing the financial statements. General disclosures – paragraphs 8.1 and 8.2 Accounting policies – paragraph 8.3 Classes of financial instruments and level of disclosure – paragraph 8.4 Significance of financial instruments to financial position and performance – paragraph 8.5. Statement of financial position – paragraphs 8.6, 8.11 (if at cost), 8.21, 8.22. Statement of financial performance – paragraphs 8.30, 8.31-8.35, 8.36-8.40 Nature and extent of risks arising from financial instruments – credit risk: 8.42-8.56 (if at cost), market risk (if significant exposure to market risk): paragraphs 8.59-8.60.	Presentation: paragraphs 7.1-7.17 and AG7.1-AG7.8