

ACCOUNTING POLICIES FOR FINANCIAL INVESTMENTS AND FINANCIAL INSTRUMENTS IN UKRAINE

Accounting is often said to be the language of business. It is used in the business world to describe the transactions entered into by all kinds organizations. Accounting terms and ideas are therefore used by people associated with business, whether they are managers, owners, investor, bankers, lawyers or accountants.

The actual record-making phase of accounting is usually called book-keeping. However, accounting extends far beyond the actual making records. Accounting is concerned with the use to which these records are put, their analysis and interpretation. An accountant should be concerned with more than the record-making phase. In particular, he should be interested in the relationship between the financial results and the events which have created them. He should be studying the various alternatives open to select the best plan of action for the business. The owners and managers of a business will need some accounting knowledge in order that they may understand what the accountant is telling them.

Probably there are two main questions that the managers or owners of a business want to know:

the first, whether or not the business is operating at a profit;

the second, they will want to know whether or not the business will be able to meet its commitments as they fall due, and so not have to close down owing to lack of funds. Both of these questions should be answered by the use of accounting reports [1].

Accounting policies in Ukraine and in other countries refer to specific principles, bases, conventions, rules and practises adopted by an enterprise with regard to significant transactions (or classes of transactions) and events while preparing and presenting financial statements. Examples of accounting policies: inventory valuation first-in, first-out (FIFO), weighted average (WA); revenue recognition; provisions recognition and estimation.

The accounting policies make a difference to the figures that are then used in the financial statements. Development of IFRS-compliant accounting policies by an enterprise is the responsibility of the enterprise's accountants (to develop) and management (to approve).

By adopting IFRS-compliant accounting policies Ukrainian enterprises make sure that financial statements are prepared according to IFRS [2].

Financial statements shall present fairly the financial position, financial performance and cash flows of an

entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework. But such Framework is absent in Ukrainian practice.

In virtually all circumstances, an entity achieves a fair presentation by compliance with applicable IFRSs. A fair presentation also requires an entity:

a) to select and apply accounting policies in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. IAS 8 sets out a hierarchy of authoritative guidance that management considers in the absence of an IFRS that specifically applies to an item;

b) to present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;

c) to provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

The most big problem in using IFRS in Ukraine is accounting policies for financial investments and financial instruments. Different scientists try to give solutions, but the main reason is in undeveloped markets of stocks and bonds [3; 4].

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

A financial asset is any asset that is: cash, an equity instrument of another entity, a contractual right to receive cash or another financial asset from another entity. Examples: Trade debtors, Notes receivable, Investments in equity instrument of another entity, Debt instruments.

A financial liability is any liability that is: a 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 unfavorable to the entity. Examples: Trade creditors, Bonds, Loans, Notes Payable.

Financial investments are investments for getting profits from interests and dividends or for obtaining the significant influence and control over an entity. Accounting for investments in equity instrument of another entity is

depended from a share of the investors. There are three levels of possessing:

- 1) to 20 per cent;
- 2) from 20 to 50 per cent;
- 3) more than 50 per cent.

The first level. IAS 39 Financial Instruments: Recognition and Measurement is used sets out the requirements for recognizing and measuring financial assets and financial liabilities[5] .

Many users of financial statements and other interested parties told the Board that the requirements in IAS 39 were difficult to understand, apply and interpret. They urged the Board to develop a new standard for the financial reporting of financial instruments that was principle-based and less complex. Although the Board amended IAS 39 several times to clarify requirements, add guidance and eliminate internal inconsistencies, it had not previously undertaken a fundamental reconsideration of reporting for financial instruments.

The Board intends that IFRS 9 will ultimately replace IAS 39 in its entirety. However, in response to requests from interested parties that the accounting for financial instruments should be improved quickly, the Board divided its project to replace IAS 39 into three main phases. As the Board completes each phase, it will delete the relevant portions of IAS 39 and create chapters in IFRS 9 that replace the requirements in IAS 39. The three main phases of the Board's project to replace IAS 39 are:

a) Phase 1: Classification and measurement of financial assets and financial liabilities. In November 2009 the Board issued the chapters of IFRS 9 relating to the classification and measurement of financial assets. Those chapters require all financial assets to be classified on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset. Assets are initially measured at fair value plus, in the case of a financial asset not at fair value through profit or loss, particular transaction costs. Assets are subsequently measured at amortized cost or fair value;

b) Phase 2: Impairment methodology. In June 2009 the Board published a Request for Information on the feasibility of an expected loss model for the impairment of financial assets;

c) Phase 3: Hedge accounting. The Board is considering how to improve and simplify the hedge accounting requirements of IAS 39.

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.

Following accounting transactions can be proposed for Ukrainian practice:

1) Purchasing of an equity instrument of another entity

Dr 145 „Financial investments”

Cr 31 „Cash at Bank”

2) Revaluation of an equity instrument of another entity under increasing of Fair value

Dr 145 „Financial investments”

Cr 735 „Profit of an entity”

The second level. International Accounting Standard 28 Investments in Associates is used [2]. The Standard permits an investor that continues to have significant influence over an associate to apply the equity method.

The Standard clarifies that investments in associates over which the investor has significant influence must be accounted for using the equity method whether or not the investor also has investments in subsidiaries and prepares consolidated financial statements.

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

The equity method is a method of accounting whereby the investment is initially recognized at cost and adjusted thereafter for the post-acquisition change in the investor's share of net assets of the investee. The profit or loss of the investor includes the investor's share of the profit or loss of the investee.

Accounting transactions that are used in Ukraine:

1) Purchasing of Investments in Associates

Dr 141 „Investments in Associates”

Cr 31 „Cash at Bank”

2) Revaluation of Investments with increasing of net assets of investee

Dr 141 „Investments in Associates”

Cr 721 „Profit from Investments in Associates”

3) Getting of Dividends from Investee

Dr 373 „Dividends receivable”

Cr 141 „Investments in Associates”

The third level. International Accounting Standard 27 Consolidated and Separate Financial Statements is used [2].

Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. A group is a parent and all its subsidiaries. A parent is an entity that has one or more subsidiaries. Consolidated financial statements are the financial statements of a group presented as those of a single economic entity. Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to a parent.

The objective of IAS 27 is to enhance the relevance, reliability and comparability of the information that a parent entity provides in its separate financial statements and in its consolidated financial statements for a group of entities under its control.

The Standard specifies:

the circumstances in which an entity must

consolidate the financial statements of another entity (being a subsidiary);

the accounting for changes in the level of ownership interest in a subsidiary;

the accounting for the loss of control of a subsidiary;

and the information that an entity must disclose to enable users of the financial statements to evaluate the nature of the relationship between the entity and its subsidiaries.

A parent must consolidate its investments in subsidiaries. There is a limited exception available to some non-public entities. However, that exception does not relieve venture capital organizations, mutual funds, unit trusts and similar entities from consolidating their subsidiaries.

A group must use uniform accounting policies for reporting like transactions and other events in similar circumstances. The consequences of transactions, and balances, between entities within the group must be eliminated.

Non-controlling interests must be presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent. Total comprehensive income must be attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Financial assets that are excluded from fair valuation and have a fixed maturity should be measured at amortized cost.

Under IAS 39, amortized cost is calculated using the effective interest method. The effective instrument rate is the rate that exactly discounts the estimated cash flows associated with the financial instrument through the expected life of the instrument.

The following example illustrates how amortized cost is calculated using the effective interest method. For example: entity A purchases a debt instrument with three years remaining to maturity. The instrument has a principal amount of \$230,000 and carries fixed interest of 9 per cent that is paid annually ($\$230,000 * 9\% =$

$\$20,700$ per year). The market-based rate for similar instruments is 10 per cent.

The market price of debt instrument:

1) $PV = 230,000 * PV(3; 10\%) = 230,000 * 0,7513 = \$172,799$;

2) $PVA = 20,700 * PVA(3; 10\%) = 20,700 * 2,4869 = \$51,479$;

3) Total amount = $\$172,799 + \$51,479 = \$224,278$.

The discount is equal $\$230,000 - \$224,278 = \$5,722$.

This discount is amortized to profit over the term to maturity of the note using the effective interest method.

Following accounting transactions can be proposed for Ukrainian practice:

1) Purchasing of a debt instrument

Dr 146 „Held-to-maturity financial asset” 230,000

Cr 147 „Discount” 5,722

Cr 31 „Cash at bank” 224,278

2) Accounting with using of the effective interest method at the end of 20x1

Dr 373 „Interests receivable” 20,700

Dr 147 „Discount” 1,728

Cr 73 „Interests revenue” 22,428

Dr 31 „Cash at bank” 20,700

Cr 73 „Interests receivable” 20,700

3) Accounting with using of the effective interest method at the end of 20x2

Dr 373 „Interests receivable” 20,700

Dr 147 „Discount” 1,901

Cr 73 „Interest revenue” 22,601

Dr 31 „Cash at bank” 20,700

Cr 373 „Interests receivable” 20,700

4) Accounting with using of the effective interest method at the end of 20x3

Dr 373 „Interests receivable” 20,700

Dr 147 „Discount” 2,093

Cr 73 „Interests revenue” 22,793

Dr 31 „Cash at bank” 20,700

Cr „Interests receivable” 20,700

5) Accounting of fixed payment at maturity

Year	Interest income	The amount by effective interest method	Amortization of discount	Amortized cost at the end of the year
20x0	-	-	-	224,278
20x1	20,700	22,428	1,728	226,006
20x2	20,700	22,601	1,901	227,907
20x3	20,700	-	2,093	230,000
	62,100	-	5,722	-

Dr 31 „Cash at bank” 230,000

Cr 146 „Held-to-maturity financial asset” 230,000

These transactions could be used by Ukrainian enterprises for adopting of IFRS, but a lot of problems in accounting for financial investments and financial instruments are presented. One of such problems is IFRS 7 „Financial Instruments: Disclosures”. This standard requires the entity to provide disclosures about financial assets it has designated as at fair value through profit or loss [2]. At initial recognition, an entity shall measure a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

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Леонова Л. О. Облікова політика у відношенні фінансових інвестицій і фінансових інструментів

У статті розглянуто проблемні питання формування облікової політики у відношенні фінансових інвестицій і фінансових інструментів. Складність цих питань розкрито як на рівні застосування міжнародних стандартів, і в українській практиці. Багато правил і принципів не діє в Україні у зв'язку з відсутністю розвинутого ринку цінних паперів. Крім того, сама організація бухгалтерського обліку фінансових інструментів в Україні вимагає реформування і прийняття виправлень для того, щоб підприємства могли правильно формувати облікову політику. Отже, подаємо рекомендації щодо застосування нових рахунків білку фінансових активів.

Ключові слова: облікова політика, фінансовий

інструмент, фінансовий актив, фінансові інвестиції, інвестиції в асоційовані компанії, контроль, борговий інструмент.

Леонова Л. А. Учетная политика в отношении финансовых инвестиций и финансовых инструментов

В статье рассмотрены проблемные вопросы формирования учетной политики в отношении финансовых инвестиций и финансовых инструментов. Сложность этих вопросов раскрыта как на уровне применения международных стандартов, так и в украинской практике. Многие правила и принципы не соблюдаются в Украине из за отсутствия развитого рынка ценных бумаг. Кроме того, сама организация бухгалтерского учета финансовых инструментов в Украине требует реформирования и принятия поправок для того, чтобы предприятия могли правильно формировать учетную политику. В этой связи даны рекомендации по применению новых счетов для учета финансовых активов.

Ключевые слова: учетная политика, финансовый инструмент, финансовый актив, финансовые инвестиции, инвестиции в ассоциированные компании, контроль, долговой инструмент.

Leonova L. A. Accounting Policies for Financial Investments and Financial Instruments in Ukraine

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Key words: accounting policies, financial instrument, financial asset, financial investments, investments in associates, control, debt instrument.

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