

ACCOUNTING FOR INCOME AND EXPENSES RELATED TO FINANCIAL INSTRUMENTS

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Abstract

This study examines the accounting treatment of income and expenses related to financial instruments and their presentation in financial statements in accordance with International Financial Reporting Standards. The research focuses on the recognition, measurement, and classification of income and expenses arising from financial instruments under IFRS 9 Financial Instruments. Particular attention is given to interest income and expenses, fair value changes, foreign exchange differences, and amortization of discounts and premiums. The study analyzes how these components are reflected in financial performance and how accounting methods influence the accuracy and transparency of financial reporting.

Keywords

Financial instruments; IFRS 9; income and expenses; effective interest rate; fair value measurement; amortized cost; financial reporting; accounting treatment; financial performance; presentation in financial statements.

Introduction

In the context of ongoing globalization and the rapid development of financial markets, financial instruments are becoming increasingly important strategic components of economic entities' activities. Through these instruments, enterprises are able to raise capital, expand investment opportunities, efficiently allocate financial resources, and manage various financial risks. This, in turn, contributes to ensuring economic stability and improving business performance efficiency.

At the same time, the proper recognition, measurement, and reliable presentation of income and expenses related to financial instruments in the accounting system is one of the key tasks of modern accounting practice. This is

because the transparency, reliability, and compliance of financial statements with international standards are directly dependent on these processes.

In the Republic of Uzbekistan, the development of financial markets, economic modernization, and the gradual alignment of the accounting and financial reporting system with International Financial Reporting Standards (IFRS) have been identified as priority directions of state policy. A number of regulatory legal acts have been adopted in this regard, which form the legal and institutional framework for reforming the financial reporting system.

In particular, the Presidential Decree of the Republic of Uzbekistan No. PF-4947 dated February 7, 2017 defined the priority directions of national development and laid the foundation for economic liberalization and financial system reform [1]. The Presidential Decree No. PF-60 dated January 28, 2022 set the Development Strategy of New Uzbekistan, defining tasks such as financial market development, improvement of corporate governance, and implementation of international standards [2]. Furthermore, Resolution No. PP-4611 dated February 24, 2020 legally strengthened the transition of joint-stock companies to full compliance with international financial reporting standards [3].

As a result of these reforms, opportunities are expanding for aligning the recognition, measurement, and presentation of financial instruments with international requirements, improving the transparency of accounting systems, and creating a reliable financial environment for foreign investors. From this perspective, the proper accounting of income and expenses related to financial instruments remains one of the most relevant scientific and practical areas of accounting research.

Literature Review

In international financial theory, the issue of financial instruments and the accounting of related income and expenses has been extensively studied by leading economists.

Breeden and Litzenberger (2019) interpret financial instruments as a mechanism for reallocating future cash flows, emphasizing that their main function is to redistribute risk and time value through financial markets. According to them, income and expenses arising from financial instruments are directly linked to the market's risk-reflection mechanism and serve as a key source of information for investment decisions [4].

De George, Li, and Shivakumar (2020), based on empirical research, demonstrate that the primary role of financial reporting is to reduce information asymmetry for investors. They argue that fair value accounting increases the

transparency of financial information and improves the quality of decision-making in capital markets [5].

D. Linsmeier and N. G. E. Küting note that the implementation of IFRS 9 significantly simplified the recognition system for income from financial assets. According to them, the expected credit loss (ECL) model enables earlier recognition of financial losses, thereby strengthening the prudence principle and improving the reliability of financial reporting [6].

Zülch, Henner, and Halbleib (2019) analyze the informational relevance of fair value accounting for investors, concluding that this method more accurately reflects economic reality in financial statements. They emphasize that the fair value approach ensures a higher level of transparency for market participants in decision-making [7].

Badertscher, Collins, and Lys (2020) show that the recognition of credit risk changes through OCI under IFRS 9 smooths income volatility in financial statements. They argue that this mechanism enhances reporting stability and forecasting ability [8].

Lins, Karl, and Sliwka (2021) empirically demonstrate that the complexity of financial instruments increases the risk of misinterpretation of income and expenses. They emphasize that separate accounting treatment of derivatives and hybrid instruments significantly improves the reliability of financial reporting [9].

Campbell, Rohan, and Vuolteenaho (2019) highlight that the primary purpose of hedge accounting is to reduce artificial volatility in financial results and accurately reflect the company's risk management strategy. According to them, hedge accounting is an important tool for ensuring earnings stability for investors [10].

Analysis and Results

Accounting for income and expenses related to financial instruments, as well as their accurate presentation in financial statements, is one of the key areas of modern financial accounting. This process is primarily regulated by the requirements of IFRS 9 Financial Instruments.

This standard establishes the principles for recognition, measurement, and accounting of income and expenses arising from financial assets and financial liabilities. At the same time, it ensures the transparency of an entity's financial performance by properly reflecting the economic substance of financial instruments.

Recognition of Income and Expenses from Financial Instruments

In accordance with IFRS 9, income and expenses related to financial instruments are generated through the following main channels:

interest income and interest expenses (using the effective interest rate method);

- gains or losses arising from the remeasurement of financial assets;
- income and expenses resulting from changes in foreign exchange rates;
- impairment expenses under expected credit losses (ECL);
- amortization of discounts and premiums on financial liabilities.

These income and expenses are presented in the statement of financial performance either separately or aggregated within relevant line items.

Impact of Classification and Measurement of Financial Instruments

•In accordance with IAS 32 Financial Instruments: Presentation, financial instruments must be properly classified between liabilities and equity. This classification directly affects how income and expenses are recognized and reported.

- In particular:
- interest expenses on debt instruments are recognized in profit or loss;
- dividends on equity instruments are presented as distributions of profit.

Presentation in Financial Statements

According to IAS 1 Presentation of Financial Statements, all income and expenses related to financial instruments must be presented in a transparent and understandable manner in financial statements.

For each financial asset and liability, the entity is required to provide sufficient disclosures regarding:

- carrying amount;
- income generated from these instruments;
- expenses incurred in relation to these instruments.

Relationship Between Risks and Expenses

Financial instruments are not only a source of income but are also associated with various financial risks. Therefore, expected losses related to credit risk, market risk, and liquidity risk are also included in financial expenses.

- These expenses are mainly reflected through:
- impairment allowances for credit losses;
- losses arising from remeasurement;
- hedging-related expenses.

Table 1

Mechanism of accounting for income and expenses on financial instruments²

² Source: author development

N	Type of Income / Expense	Source of Generation	Accounting Method (IFRS 9)	Presentation in Financial Statements
1	Interest income	Loans, bonds	Effective Interest Rate	Profit or Loss Statement
2	Interest expense	Loans, bonds	Amortized cost	Profit or Loss Statement
3	Revaluation /gain/loss	Changes in market value	Fair Value Through Profit or Loss (FVTPL)	Profit or Loss Statement
4	Foreign exchange differences	Foreign currency assets/liabilities	Remeasurement at reporting date	Profit or Loss Statement
5	Credit losses (ECL)	Receivables, loans	Expected Credit Loss Model	Recognized expense
6	Discount/premium amortization	Bonds, borrowings	Amortization method	Profit or Loss Statement

Analysis and Results

According to the research findings, income and expenses arising from financial instruments are formed as a result of various economic sources and financial transactions. Their accounting is primarily carried out in accordance with the requirements of IFRS 9 Financial Instruments.

The table analysis shows that income and expenses related to financial instruments are classified into the following main groups:

Interest income arises from loans and investment assets, while interest expenses arise from debt obligations. They are measured using the amortized cost and effective interest rate (EIR) methods. This category is considered the most stable source of impact on financial results.

Changes in the market value of financial assets result in gains or losses. These indicators reflect the entity's sensitivity to market risks.

When financial instruments denominated in foreign currencies are remeasured, exchange rate fluctuations generate income or expenses. This factor reflects the impact of the external economic environment.

In accordance with IFRS 9 Financial Instruments, expected credit losses related to credit risk are recognized as separate expenses and are of significant importance in assessing financial stability.

For financial liabilities and debt instruments, discounts or premiums are gradually recognized as expenses and included in interest expenses.

Key findings of the analysis

Income and expenses from financial instruments are multi-component and originate from various sources;

The largest share relates to interest income and expenses;

Market and foreign exchange risks increase the volatility of income and expenses;

The ECL model allows for the forward-looking estimation of credit-related expenses;

IFRS 9 plays a key role in ensuring transparent and economically faithful financial reporting.

Conclusion of the Study

The study shows that accounting for income and expenses related to financial instruments, as well as their proper presentation in financial statements, is one of the key areas of modern accounting. This process is mainly based on the recognition of interest income and expenses, their accurate measurement, and compliance with international standards.

It was found that the formation of income and expenses from financial instruments is primarily associated with the correct accounting treatment of interest income and interest expenses.

In this regard, the main regulatory framework is provided by IFRS 9 Financial Instruments. This standard establishes a unified methodological basis for the recognition, measurement, and classification of income and expenses related to financial instruments.

Recognition of interest income and expenses using the effective interest rate (EIR) method ensures that financial results are presented in a manner consistent with economic substance and reliability.

In addition, proper classification and accounting of income and expenses related to financial instruments enhance the transparency and comparability of financial statements.

The research results show that there is a need to harmonize national accounting practices with international standards in the area of accounting for income and expenses from financial instruments.

In conclusion, the proper presentation of income and expenses from financial instruments contributes to the reliability and transparency of financial performance, as well as increasing the informational value for external users.

Recommendations

1. Develop a separate standard or methodological guideline within the national accounting system for the accounting of income and expenses related to financial instruments.

2. Broaden the implementation of practices for recognition, measurement, and accounting of income and expenses in accordance with IFRS 9 Financial Instruments.

3. Improve the system of transparent disclosure of income and expenses from financial instruments as separate line items in financial statements.
4. Strengthen the system of retraining and professional development of accounting and financial specialists based on international standards.
5. Improve mechanisms for assessing risks related to financial instruments and analyzing their impact on income and expenses within enterprises.

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