HMRC - CFM23045 - FRS 102: Measurement Of Basic Financial Instruments: Amortised Cost

The amortised cost of a financial asset or financial liability is

the amount at which the asset or liability is measured at initial recognition (usually ‘cost’)

minus any repayments of principal,

minus any reduction for impairment or uncollectibility, and

plus or minus the cumulative amortisation of the difference between that initial amount and the maturity amount.

You work out the amortisation using the effective interest method.

Assets accounted for at amortised cost are subject to review for impairment. This is covered in more detail at CFM23030.

Effective interest method

This is a method of calculating the amortised cost of a financial asset or financial liability, and of allocating the interest income or interest expense over the relevant period. The effective interest rate in a financial instrument is the rate that exactly discounts the cash flows associated with the instrument (either through to maturity or to the next re-pricing date) to the net carrying amount at initial recognition, i.e. a constant rate on the carrying amount. The effective interest rate is sometimes termed the level yield to maturity (or the next re-pricing date), and is the internal rate of return of the financial asset or liability for that period.

There is more about computing the effective interest rate, with an example, at CFM21180.

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