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***“ACCOUNTING FOR THE EFFECT OF CHANGES IN PRICE  
LEVELS”***

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# Presentation content

1. Introduction
2. Alternative solutions
3. Reasons for the use of an index rate for the accumulated inflation for the last three years lower than the one contemplated by IAS 29 (100%)
4. Proposed Restatement Mechanism

# Introduction

## Why a research paper?

Main effects of inflation on not restated financial statements are the following:

- Understatement of assets measured at historical cost and of the impairments recognized when cost is higher than their recoverable value
- Understatement of owners' contributions or the capital contributions to the entity
- Distortion of the presentation of income and expenses due to the inadequate comparison of items stated in currency of different purchasing power
- Unrecognized gains or losses due to the exposure of monetary items to inflation
- .....>

# Introduction

## Why a research paper?

Main effects of inflation on not restated financial statements are the following:

- .....>
- Significant distortion in the measurement of income/loss originated in financial assets and liabilities that are stated in nominal terms despite being stated in real terms.
- It is impossible to determine the amount corresponding to capital maintenance; consequently, without knowing the growth in equity in real terms, there is no sound basis for the distribution of earnings or dividends to shareholders

# ALTERNATIVE SOLUTIONS

## Current value measurement:

- ❑ It is a basic accounting principle that all measurements must be made by using the same measurement unit.
- ❑ To be useful this unit must have a relatively constant value over time.
- ❑ fair valuing assets and liabilities (or to use current cost measurements) is not a proper solution for the unit of measurement distortion.
- ❑ the components of equity will be substantially distorted and will not properly present the causes for the changes in equity.

# ALTERNATIVE SOLUTIONS

## Disclosure of the restated information:

- ❑ Countries having medium and high levels of inflation briefly used this proposal, but the experience was unsatisfactory.
- ❑ Most users found it confusing to have two different measurements of profit, total assets, equity, etc. and very difficult to understand the differences between them.
- ❑ To only disclose the restated information was discontinued and prohibited by the standard setters because of the misleading and confusing information provided to users.
- ❑ Accordingly, restated information was the only required in the basic financial statements, including the separate presentation of the result produced by the inflation effects on the net monetary position.

# ALTERNATIVE SOLUTIONS

## Constant currency accounting:

- ❑ The goal here is to measure all the figures of the financial statements in currency with the same purchasing power (the one corresponding to the closing date of the last period presented).
- ❑ Because of cost-benefit reasons, the method can be used only when the distortions for not using the method are relevant for financial information analysis.
- ❑ Distortions, especially in the statement of profit or loss and other comprehensive income, are crystal clear when the inflation rate for the period is high, thereby justifying the cost of the restatement.
- ❑ Countries with medium and high inflation, but not hyperinflation, have been using this method of restatement with very satisfactory results

## Reasons for the use of an index rate lower than the one contemplated by IAS 29 (100%)

- ❑ Empirical demonstrations show that the distortion is significantly higher where the inflation rates are higher than in stable economies.
- ❑ Necessary to establish a reference point that justifies the costs and efforts necessary for preparers to produce the corresponding changes to the nominal financial information.
- ❑ All parameters are arbitrary and cannot be demonstrated, our opinion is based in our experience from having lived and worked during very prolonged periods in which we had environments of high, medium and low inflation rates, and having prepared and analyzed financial information, both with and without restatement of the financial information.



# Reasons for the use of an index rate lower than the one contemplated by IAS 29 (100%)

- ❑ Based on our experience, we suggest replacing the 100% with a reference number of 26% (high inflation), meaning about 8% annual.
- ❑ Also, based on our previous experience, we can say that an inflation rate 8% is not sustainable during a prolonged time.
- ❑ The empirical evidence shows that environments evolve into a reduction of the rate to certain limits, which can be sustained during prolonged periods (less to 3% annual) or to a substantial increase in the inflation rate.

# Reasons for the use of an index rate lower than the one contemplated by IAS 29 (100%)

2012 Relationships	Non monetary Fixed Assets	Equity	Equity/Fix ed Assets	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	Average distortion	Maximum distortion
<b>Alstom (France)</b>	<b>10.256</b>	<b>4.434</b>	<b>43%</b>												
Results Restated/Published Difference				9,21%	10,20%	2,47%	-2,97%	11,04%	8,38%	27,31%	-11,59%	-5,96%	-4,20%	4,39%	27,31%
Equity Restated/Published Difference				22,44%	20,04%	16,75%	20,93%	28,26%	20,88%	21,96%	20,35%	8,58%	9,91%	19,01%	28,26%
Period Inflation				1,98%	2,08%	1,54%	0,88%	2,82%	1,49%	1,67%	1,75%	2,14%	2,14%	1,85%	
Three years accumulated inflation				4,57%	5,32%	5,27%	6,09%	4,99%	5,66%	6,16%					
Total Period accumulated inflation				20,09%	17,76%	15,36%	13,61%	12,62%	9,54%	7,93%	6,16%	4,33%	2,14%		
<b>Carrefour (France)</b>	<b>20.918</b>	<b>8.361</b>	<b>40%</b>												
Results Restated/Published Difference				3,78%	37,32%	15,42%	-41,09%	20,52%	5,54%	7,52%	11,09%	15,59%	18,79%	9,45%	-41,09%
Equity Restated/Published Difference				40,48%	41,01%	25,89%	22,53%	23,70%	16,37%	15,40%	13,51%	11,33%	6,27%	21,65%	41,01%
Period Inflation				1,98%	2,08%	1,54%	0,88%	2,82%	1,49%	1,67%	1,75%	2,14%	2,14%	1,85%	
Three years accumulated inflation				4,57%	5,32%	5,27%	6,09%	4,99%	5,66%	6,16%					
Total Period accumulated inflation				20,09%	17,76%	15,36%	13,61%	12,62%	9,54%	7,93%	6,16%	4,33%	2,14%		
<b>Telefonica (Spain)</b>	<b>85.060</b>	<b>27.661</b>	<b>33%</b>												
Results Restated/Published Difference				5,59%	14,78%	3,87%	-13,88%	14,47%	9,94%	23,45%	12,89%	10,63%	13,08%	9,48%	23,45%
Equity Restated/Published Difference				40,73%	37,08%	25,82%	29,55%	42,51%	27,30%	23,59%	17,90%	14,66%	4,54%	26,37%	42,51%
Period Inflation				2,44%	3,05%	2,04%	-0,24%	4,13%	2,84%	3,56%	3,38%	3,05%	3,10%	2,74%	
Three years accumulated inflation				4,91%	6,00%	6,84%	10,91%	10,11%	10,33%	9,84%					
Total Period accumulated inflation				30,92%	27,80%	24,02%	21,53%	21,82%	16,99%	13,76%	9,84%	6,25%	3,10%		
<b>EDET (Argentina)</b>	<b>116.507</b>	<b>55.952</b>	<b>48%</b>												
Results Restated/Published Difference				1,50%	-9,03%	24,36%	54,28%	101,59%	129,39%	115,54%	203,65%	-67,84%	532,03%	108,55%	532,03%
Equity Restated/Published Difference				92,19%	86,14%	102,89%	97,34%	83,16%	53,88%	38,57%	26,57%	11,51%	12,38%	60,46%	102,89%
Period Inflation				13,13%	12,67%	14,56%	10,27%	8,98%	14,56%	7,17%	10,64%	8,35%	1,50%	10,18%	
Three years accumulated inflation				42,33%	37,66%	37,66%	33,80%	35,84%	28,48%	21,68%					
Total Period accumulated inflation				162,13%	131,72%	105,65%	79,52%	62,80%	49,39%	30,40%	21,68%	9,98%	1,50%		

## Reasons for the use of an index rate lower than the one contemplated by IAS 29 (100%)

N <sup>a</sup>	Country	Ac. 2005/2007	2007	2006	2005
1	Zimbabwe:	526386,8%	12563,0%	1033,5%	266,8%
2	Turkmenistan:	1327,1%	11,3%	11,5%	1050,0%
3	Iraq:	113,3%	4,7%	53,2%	33,0%
4	Guinea:	100,5%	23,4%	30,0%	25,0%
5	Burma:	94,7%	35,0%	20,0%	20,2%
6	São Tomé and Príncipe:	67,3%	18,0%	23,1%	15,2%
7	Venezuela:	56,6%	18,7%	13,7%	16,0%
8	Angola:	56,4%	12,2%	13,3%	23,0%
9	Eritrea:	54,7%	17,0%	15,0%	15,0%
10	Iran:	48,7%	17,0%	12,0%	13,5%
11	Yemen:	48,6%	10,0%	20,8%	11,8%
12	Ethiopia:	48,5%	17,2%	13,5%	11,6%
13	Sri Lanka:	46,9%	15,8%	13,7%	11,6%
14	United Arab Emirates:	43,0%	14,0%	13,5%	10,5%
15	Ukraine:	42,9%	12,8%	11,6%	13,5%
16	Zambia:	42,6%	10,6%	9,0%	18,3%
17	Haiti:	42,0%	8,5%	13,1%	15,7%
18	Malawi:	41,8%	7,9%	13,9%	15,4%
19	Moldova:	41,6%	12,3%	12,7%	11,9%
20	Ghana:	41,3%	10,7%	10,9%	15,1%
21	Madagascar:	40,5%	10,3%	10,8%	15,0%

# Reasons for the use of an index rate lower than the one contemplated by IAS 29 (100%)

N <sup>a</sup>	Country	Ac. 2005/2007	2007	2006	2005
22	Costa Rica:	38,8%	9,4%	11,5%	13,8%
23	Kenya:	38,5%	9,7%	14,5%	10,3%
24	Azerbaijan:	38,5%	16,7%	8,3%	9,6%
25	Qatar:	38,3%	13,7%	11,8%	8,8%
26	Jamaica:	37,1%	9,5%	8,6%	15,3%
27	Tajikistan:	35,5%	13,1%	11,9%	7,1%
28	Russia:	34,8%	9,0%	9,7%	12,7%
29	Indonesia:	32,8%	6,3%	13,1%	10,5%
30	Nicaragua:	32,8%	11,1%	9,1%	9,6%
31	Argentina:	31,2%	8,8%	10,0%	9,6%
32	Mozambique:	30,4%	8,2%	13,2%	6,5%
33	Turkey:	30,0%	8,7%	10,5%	8,2%
34	Botswana:	29,7%	7,1%	11,5%	8,6%
35	Syria:	29,6%	12,2%	10,0%	5,0%
36	Kazakhstan:	29,5%	10,8%	8,6%	7,6%
37	Nigeria:	29,4%	5,4%	8,2%	13,5%
38	Burundi:	29,1%	8,3%	2,8%	16,0%
39	Georgia:	29,1%	9,3%	9,2%	8,2%
40	Guyana:	28,7%	12,3%	7,2%	6,9%
41	Rwanda:	28,2%	9,1%	8,8%	8,0%
42	Belarus:	27,9%	8,4%	7,0%	10,3%
43	Pakistan:	26,7%	7,6%	7,9%	9,1%
44	Paraguay:	26,5%	8,1%	9,6%	6,8%
45	Sudan:	26,2%	8,0%	7,2%	9,0%
46	Vietnam:	26,1%	8,3%	7,5%	8,3%

# Proposed Restatement Mechanism

## Economic Environment:

- i. **Inflationary** : when inflation levels cause the local currency to depreciate significantly with regard to its purchasing power, it can no longer be considered a point of reference for settling financial transactions
- ii. **Non-Inflationary**: when inflation is negligible and, is considered to be controlled in the country; the foregoing means that such inflation has no impact on the country's main economic indicators

# Proposed Restatement Mechanism

## Restatement of Financial Statements:

- i. Integral restatement:** Restate the amounts of all the figures to be included in the financial statements as a previous procedure, to homogenize all the measurements using a currency unit with the same purchasing power during all the periods included in the financial statements.
- ii. Measurement of assets, liabilities and equity:**
  - i. Historical cost:** The same calculation with restated amounts
  - ii. Fair value or other current values:** Doesn't change the amount in the SFP but the results differ because the comparison is with restated amounts
  - iii. Financial assets & liabilities at amortized cost:** Doesn't change the amount in the SFP but the results differ because the comparison is with restated amounts

# Proposed Restatement Mechanism

## Restatement of Financial Statements:

### iii. Presentation of inflation effects on financial statements information:

- Disclosure of the nominal change in the values of financial assets and liabilities separated from the effect of inflation on the mentioned items produce relevant information.
- Presentation of the results for maintenance of financial items (monetary items) without compensation of interest or other form of adjustment in inflationary environments is very important for the understanding of the financial information in high inflation environments.

**Thank you very much !!**