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Project	IAS 21 *The Effects of Changes in Foreign Exchange Rates*		
Paper topic	Revenue transaction denominated in foreign currency		
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This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination. Decisions made by the IFRS Interpretations Committee are reported in IFRIC *Update*. The approval of a final Interpretation by the Board is reported in IASB *Update*.

Introduction

1. The IFRS Interpretations Committee (the 'Interpretations Committee') received a submission asking how to determine which exchange rate to use when reporting revenue transactions denominated in a foreign currency in accordance with IAS 21 *The Effects of Changes in Foreign Exchange Rates*. In particular, the submission described a circumstance in which the customer paid for the goods or services in advance.

2. The issue was initially discussed by the Interpretations Committee at its meeting in November 2014.[1] As noted in the IFRIC *Update* of that meeting (reproduced in Appendix B), the Interpretations Committee tentatively decided to develop guidance on identifying the date of the transaction for revenue transactions denominated in a foreign currency, as an interpretation of paragraph 22 of IAS 21.

3. Paragraphs 21–22 of IAS 21 require that a foreign currency transaction should be recorded, on initial recognition in the functional currency, by applying the spot exchange rate at the date of the transaction. The date of the transaction is the date on which the transaction first qualifies for recognition in accordance with IFRS.

[1] See Agenda Paper 14 for the Interpretation Committee's meeting in November 2014.

4. The majority of the Interpretations Committee members supported recognising revenue using the exchange rate at the date of the non-refundable advance payment or at the date that the advance payment is due, if earlier (ie the date that the contract liability (or deferred revenue) is initially recognised) ('View B').[2] This View is based on the following principles:

   (a) the obligation to transfer goods or services (which gives rise to deferred revenue on recognition of an advance cash receipt) and the performance of that transfer (which gives rise to revenue) is a single transaction; and

   (b) the transaction first qualifies for recognition when the transaction is first recorded with a value in the financial statements, which is generally only when one of the parties to the contract first performs.

5. This purpose of this paper is to consider:

   (a) the interaction of View B with other Standards and whether the scope of any guidance should include other foreign currency transactions (paragraphs 8-50);

   (b) how View B applies to more complex scenarios (paragraphs 51-69); and

   (c) the effective date and transition arrangements of any guidance (paragraphs 70-78).

6. The key points arising in the paper are that the staff recommend that:

   (a) the Interpretations Committee should publish a draft interpretation for public consultation based on View B, revised as discussed in this paper.

   (b) the proposed interpretation should not be restricted to revenue transactions, but should also apply to other foreign currency transactions (purchase and sales transactions) that are similarly affected by the issue.

   (c) the proposed interpretation should only deal with circumstances in which the advance receipt or payment is cash that is denominated in a foreign

[2] This approach was described as 'View B' in Agenda Paper 14 for the Interpretation Committee's meeting in November 2014. A summary of the different views considered at the November 2014 meeting is given in Appendix A of this paper.

currency and gives rise to a non-monetary deferred income liability or prepayment asset.

(d) the proposed interpretation should clarify that the date of the transaction is determined as the transaction is initially recognised, so if the transaction is initially recognised in stages, so is the date of the transaction.

(e) the date of initial recognition of the amount of consideration paid or received in advance is the date of the transaction used to translate the portion of the income, expense or asset, on initial recognition, to which each advance consideration payment or receipt relates. This should reflect the pattern used to derecognise the non-monetary deferred income liability or prepayment asset.

(f) the effective date should not be before the effective date of IFRS 15 *Revenue from Contracts with Customers.*

(g) on transition to the proposed requirements, entities may either apply the proposed interpretation:

   (i) retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; or

   (ii) retrospectively with the cumulative effect of initially applying the proposed interpretation at the start of the reporting period in which an entity first applies the proposed interpretation, or at the start of a prior reporting period presented, but only to transactions that are not completed transactions at that date.

7. Appendix A contains a background on the issue and a summary of the tentative conclusions that the Interpretations Committee made at its meeting in November 2014.

Interaction with other Standards and other types of transactions denominated in a foreign currency

Interaction with other Standards

8. Our analysis to date has considered the issue within the context of revenue contracts from the seller's perspective. But similar considerations arise when there are advanced payments or receipts in a foreign currency in respect of other (non-financial) transactions. For example:

    (a) purchases and sales of property, plant and equipment (PPE) (IAS 16 *Property, Plant and Equipment*);

    (b) purchases of intangible assets (IAS 38 *Intangible Assets*);

    (c) purchases and sales of investment property (IAS 40 *Investment Property*);

    (d) purchases of inventory (IAS 2 *Inventories*); and

    (e) purchases of services.

9. None of the above Standards specify the accounting treatment for any foreign currency implications. Nor is foreign currency translation addressed in the *Conceptual Framework for Financial Reporting* (current or proposed).

10. We note that paragraph 24 of IAS 21 states:

    > The carrying amount of an item is determined in conjunction with other relevant Standards. For example, property, plant and equipment may be measured in terms of fair value or historical cost in accordance with IAS 16 *Property, Plant and Equipment*. Whether the carrying amount is determined on the basis of historical cost or on the basis of fair value, *if the amount is determined in a foreign currency it is then translated into the functional currency in accordance with this Standard*. [emphasis added]

11. Paragraph 24 of IAS 21 appears to be written primarily within the context of translating non-monetary items at subsequent reporting period-ends, using either the exchange rate at the date of the transaction (for items measured at historical cost) or the exchange rate at the date the fair value was measured (for items measured at fair

value). However the principle quoted in paragraph 10 in italics implies that the measurement requirements of other Standards are applied to the foreign currency amounts and, separately, that those amounts are translated into the entity's functional currency in accordance with IAS 21. We note that, consistently with this, IFRS 13 *Fair Value Measurement* does not contain any guidance in respect of the foreign exchange implications of the fair value measurement of items denominated in a foreign currency. Similarly, other Standards (eg IFRS 15, IAS 16) do not give guidance on the foreign exchange aspects of transactions.

12. That is not to say that IAS 21 disregards other Standards—indeed, to determine the date of the transaction, paragraph 22 of IAS 21 specifically requires us to look to the recognition requirements of other Standards. Similarly, the exchange rate to use on subsequent measurement of a non-monetary item depends upon the measurement basis (historical cost or fair value) of the carrying amount, as required by other Standards. However, having determined the date of initial recognition and the measurement basis in accordance with other Standards, IAS 21 is applied to determine which exchange rate should be used to translate those foreign currency items into an entity's functional currency.

13. This provides a basis for interpreting paragraphs 21 and 22 of IAS 21, without needing to interpret the recognition or measurement requirements of other Standards.

14. Despite this, in interpreting IAS 21, we will look at the initial measurement requirements of other Standards to see whether they may offer a guide as to the most appropriate interpretation of 'date of transaction' and to ensure that any interpretation is not inconsistent with the requirements in other Standards. In this respect, Agenda Paper 14 for the November 2014 Interpretations Committee meeting considered some of the measurement aspects of IFRS 15. In addition, further consideration of the variable consideration and non-cash consideration requirements in IFRS 15 is given in Appendix C. As noted in Appendix C, we think that the variable consideration requirements in IFRS 15 do not apply to variability in value that is only due to movements in foreign exchange rates. In addition, the non-cash consideration requirements do not apply to cash denominated in a foreign currency. We note that even if applied by analogy, those requirements would not appear to apply to a change in the value of consideration that is solely due to the form of the consideration.

Furthermore, we think that these requirements in IFRS 15 do not help to clarify what the date of transaction might be when an entity receives cash in a foreign currency under a contract with a customer.

Scope of the proposed interpretation

15. The scope of the proposed interpretation could be either:

    (a) restricted to revenue contracts; or

    (b) widened to include other foreign currency transactions that are similarly affected by the issue.

16. The first option has the benefit of restricting the scope of the proposed interpretation, which may prevent unintended consequences if the scope is widened. However, IAS 21 applies to all foreign currency transactions. Because we are interpreting IAS 21, and not other Standards, we think that the same interpretation of IAS 21 should apply to the translation of other foreign currency transactions in which there are advance payments or receipts of foreign currency. In addition:

    (a) widening the scope of the proposed guidance to other foreign exchange transactions will reduce diversity where more than one interpretation of IAS 21 is compatible with other Standards; and

    (b) limiting the scope of the issue only to revenue transactions could lead to confusion over whether the principles in the interpretation should be applied by analogy to other similar circumstances (such as prepayments for purchases of services).

17. The issue considered to date arises when, under a contract with a customer, there is an advance cash receipt in a foreign currency before the recognition of the revenue derived from the sale of those goods or services. This advance cash receipt gives rise to a non-monetary contract asset (ie deferred revenue/contract liability). Below we consider which other foreign currency transactions could be similarly affected and whether View B is compatible with other relevant Standards, as follows:

    (a) sales of other assets, including

        (i) PPE, investment property and intangible assets;

(ii) subsidiaries, associates and joint ventures;

(b) purchases of assets, goods and services, including

(i) inventory, investment property and intangible assets;

(ii) business combinations;

(c) financial instruments;

(d) insurance contracts;

(e) leases;

(f) government grants;

(g) taxes, levies and fees (including income taxes).

Sales of other assets

18. Similar circumstances arise when there is an advance cash receipt in a foreign currency for the sale of assets (eg PPE) other than through contracts with customers. We think that, in principle, the same interpretation of the 'date of transaction' should apply when considering which exchange rate should be used to translate the amount of consideration included in the gain or loss on disposal of other assets in the income statement.

Sales of PPE, investment property and intangible assets

19. In accordance with IAS 16, IAS 40 and IAS 38, the derecognition date and the amount of consideration included in the gain or loss arising from the disposal of PPE, investment property and intangible assets is determined consistently with the requirements in IFRS 15.[3] Consequently, the same issues and considerations apply to the sale of such assets as for revenue transactions, which we have already considered. Therefore, we think that the proposed guidance should also apply to such transactions.

Sales of subsidiaries, associates and joint ventures

20. IAS 27 *Separate financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* do not provide any further guidance regarding the measurement of the

[3] These requirements were made as consequential amendments following the issue of IFRS 15.

consideration that should be recognised in the income statement as part of the gain or loss on disposal of the subsidiary (in separate financial statements), associate or joint venture. Consequently, we think that View B is compatible with IAS 27 and IAS 28.

21. The requirements for disposals of subsidiaries in consolidated financial statements are given in IFRS 10 *Consolidated Financial Statements*. IFRS 10 states that if a parent loses control of a subsidiary it shall recognise the 'fair value of consideration received', which is included in the gain or loss recognised in the income statement. There is no further guidance regarding the date at which the fair value of the consideration is determined if it is received in advance of the date that the parent derecognises the subsidiary. Hence we think that recognising foreign currency cash using the exchange rate that the consideration is received is compatible with IFRS 10.

Summary

22. We therefore recommend that the proposed interpretation of the date of transaction in IAS 21 should be applied to the sale or disposal of goods, services and other assets in circumstances in which the entity receives foreign currency cash in advance of the recognition of the related revenue, or gain or loss on disposal.

Purchases of assets, goods and services

23. The issue can also arise when an entity pays foreign currency cash in advance for goods or services in a foreign currency before it recognises those goods or services in the financial statements as assets or expenses. We think that the same considerations apply for purchases as they do for sales. Applying the same interpretation of the 'date of transaction' for purchased assets or expenses initially recognised at cost (ie translating the purchased assets or expenses using the exchange rate at the date of recognition of advance cash payment):

    (a) is consistent with the treatment of foreign exchange differences for sales of goods, assets and services;

    (b) avoids recognising a foreign exchange gain or loss on initial recognition of an asset, because there is no remeasurement of the (non-monetary) prepayment asset; and

(c) reflects that, after payment, the entity is not exposed to any further foreign exchange risk in respect of the purchase. (Any foreign currency risk arising on foreign currency debt to fund the purchase arises on a separate transaction (ie the foreign currency financing)).

Purchases of inventory, PPE, investment property and intangible assets

24. Purchases of inventory, PPE, investment property and intangible assets are all initially measured at cost in accordance with the relevant Standards, regardless of whether such assets are subsequently revalued, impaired or written down.

25. IAS 16, IAS 38 and IAS 40 define cost as

> 'the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction or, where applicable, the amount attributed to that asset when initially recognised in accordance with the specific requirements of other IFRSs, eg IFRS 2 *Share-based Payment.*

26. IAS 2 states that the costs of purchase of inventories includes the purchase price after deducting trade discounts, rebates and other similar items. IAS 2 does not contain any further explanation about how to determine the purchase price.

27. Applying the 'single transaction' view (ie View B) to purchases means that the date of transaction[4] is the date that the advance payment is made. This view is compatible with the definition of cost in these other Standards.

Summary

28. We therefore recommend that the proposed interpretation of the date of transaction in IAS 21 should be applied to purchase of goods, services and other assets in circumstances in which the entity pays foreign currency in advance of the recognition of the related asset or expense.

[4] IAS 21 defines the date of transaction as the date on which the transaction first qualifies for recognition in accordance with IFRSs.

Business combinations

29. On the acquisition of a business, paragraphs 32, 37 and 38 of IFRS 3 *Business Combinations* require the measurement of goodwill to include the consideration transferred measured at 'acquisition-date fair value'. If the consideration transferred includes assets of the acquirer that have carrying amounts that differ from their fair values at the acquisition date (for example non-monetary assets), the acquirer remeasures the transferred assets or liabilities to their fair values as of the acquisition date and recognises the resulting gains or losses.

30. Difficulties could arise in interpreting this requirement if any consideration, such as foreign currency, has been paid in advance of the acquisition date. To avoid any unintended consequences, we recommend that the proposed interpretation need not apply to business combinations, or to any other circumstances in which the consideration for the purchase of an asset is measured at fair value for inclusion in the initial measurement of the asset.

Cash-settled share-based payments

31. Consideration for purchase transactions may be a cash-settled share-based payment. Paragraph 30 of IFRS 2 *Share-based Payments* requires that for such transactions the entity should measure the goods or services acquired and the liability incurred at the fair value of the liability. The Standard does not give any specific guidance for the measurement of any advance payments.

32. Due to the specific requirements in IFRS 2 and the potential complexities involved, we think that the proposed interpretation of IAS 21 need not apply to cash-settled share-based payments. Equity-settled share-based payments are considered in paragraphs 66-68 of this paper.

Financial instruments

33. We do not think that the same issue arises for financial instruments because, in accordance with IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 9 *Financial Instruments*, financial instruments are treated as a single transaction

from inception of the contract.[5] This is because they represent a series of cash flows without any non-financial element. We therefore think that the proposed interpretation need not apply to financial instruments or other contracts that are accounted for in accordance with IFRS 9 or IAS 39. This would include investments in subsidiaries, associates and joint ventures in separate financial statements that are accounted for in accordance with IFRS 9 or IAS 39, instead of at cost, as permitted in paragraph 10 of IAS 27.

Insurance contracts

34. Similar circumstances could arise when a customer pays in advance for an insurance contract before the income is recognised in the income statement. However the foreign exchange implications of insurance contracts has already been considered as part of the IASB's Insurance project. (The Exposure Draft *Insurance Contracts* ED/2013/7 proposes that insurance contracts should be treated as monetary items for the purposes of IAS 21). Consequently, we recommend that the proposed interpretation need not apply to insurance contracts.

Leases

35. Payments may be made under lease contracts before the initial recognition of the lease assets, liabilities, income or expense, as discussed below. Hence the same issue arises if these advance payments are in a foreign currency. We recommend that advance payments under lease contracts should therefore be included within the scope of the proposed interpretation.

36. In accordance with paragraph 4 of IAS 17 *Leases*, the commencement of the lease term is the date from which the lessee is entitled to exercise its right to use the leased asset. It is also the date of initial recognition of the lease (ie the recognition of the assets, liabilities, income or expenses resulting from the lease), which may be some time *after* the inception of the lease. Any payments made or received before the commencement of the lease would be recognised as prepayments or deferred income.

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[5] Paragraphs 14 of IAS 39 and 3.1.1 of IFRS 9 state that 'An entity shall recognise a financial asset or financial liability... when, and only when, the entity becomes a party to the contractual provisions of the instrument'.

37. For a finance lease, these prepaid amounts would be added to the lease asset on initial recognition by the lessee, or be included as part of the consideration to be included in the gain or loss on disposal of the underlying asset by the lessor. The foreign currency implications of the advance payments in this scenario are similar to the sales and purchases of PPE discussed above and should therefore be treated in the same way.

38. Payments made under operating leases are recognised as an expense (for lessees) or income (for lessors) over the lease term. The accounting for operating leases is not dissimilar to that of service contracts (albeit that the pattern of recognition of the expense or income may differ over the contract term). Consequently, we think that the proposed interpretation should equally apply to advance payments and receipts made in a foreign currency under an operating lease contract.

39. The IASB's project on leases proposes changes to the accounting treatment for lessees. (The accounting for lessors would be unchanged.) A final Standard is expected in the second half of 2015. Under the proposals, lessees would initially recognise all leases as lease assets and liabilities at the present value of future lease payments. The current proposals (as included in the Exposure Draft *Leases* ED/2013/6 published in May 2013) would require lease assets and lease liabilities to be initially recognised on commencement of the lease, which, similarly to IAS 17, may be a date after the inception of the lease. Under these proposals, at initial recognition, the cost of the right-of-use asset includes any lease payments made to the lessor at or before the commencement date, less any lease incentives received from the lessor. We understand that there are no proposals to include any specific requirements or guidance in respect of leases denominated in a foreign currency. Hence, we think that the proposed interpretation would be likely to be equally applicable to advance payments under lease contracts under the proposed new Standard on leases.

Government grants

40. The transactions discussed above are examples of exchange transactions between two parties made under contract. However, not all transactions involving foreign currency

are exchange transactions or contractual. Government grants[6] are examples of transactions that could involve advance payments in a foreign currency that are not necessarily exchange transactions.

41. However, the same issue arises when foreign currency cash is received that is a government grant that, at a later date, is recognised as a credit in the income statement, or deducted from the cost of another asset, in accordance with IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. Although not an exchange transaction as such, it would be appear to be similar to the other scenarios. One party (the government) pays an amount in advance to the entity, which, if yet to be earned, is recognised as deferred income. At a later date, the entity fulfils its obligations under the terms of the grant, which results in the recognition of the grant either in the income statement or as a deduction from the cost of another asset.

42. We therefore recommend that the proposed interpretation should also be applicable to government grants.

Taxes, levies and fees

43. An entity is obliged to pay various taxes and fees, including income tax and levies, that could be denominated in a foreign currency and may be paid in advance of their recognition in the income statement. Paragraph 12 of IAS 12 *Income Taxes* states that 'If the amount already paid in respect of current and prior periods exceeds the amount due for those periods, the excess shall be recognised as an asset'.

44. Although not contractual or an exchange transaction, the same issues arise if the advance payment in a foreign currency in respect of a tax, levy or fee denominated in a foreign currency gives rise to a non-monetary asset (which will depend upon the specific facts and circumstances) before it is recognised as an expense (or added to the cost of an asset). Although, in some cases the recognition of the tax, levy or fee may be triggered by something other than the actions of the entity, in principle we think

[6] Paragraph 3 of IAS 20 defines a government grant as assistance by the government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity.

that the proposed interpretation should apply to such items, with a possible exception for income tax as discussed below.

Income taxes

45. Prepayments of income tax generally arise in respect of current tax. However, there is an interplay with deferred tax and in particular in respect of deductible temporary differences that give rise to possible deferred tax assets. Furthermore, paragraph 78 of IAS 12 permits entities to classify foreign exchange gains or losses on deferred foreign tax liabilities or assets as deferred tax expense (income), if that presentation is considered to be the most useful to the users of financial statements.

46. We are concerned that the complexities in this area could lead to unintended consequences, with potentially little benefit. Because of this, we recommend that the proposed interpretation need not apply to income taxes.

Conclusion

47. As discussed above, we note that IAS 21 implies that the measurement requirements of other Standards are applied to the foreign currency amounts and that those amounts are translated separately into the entity's functional currency in accordance with IAS 21. This provides a basis for interpreting paragraphs 21 and 22 of IAS 21, without needing to interpret the recognition or measurement requirements of other Standards.

48. The staff recommend that the proposed interpretation should not be restricted to revenue transactions, but should apply to other foreign currency transactions that are similarly affected by the issue. That is, the proposed interpretation should apply to foreign currency transactions in circumstances in which there is consideration in a foreign currency that is paid or received in advance of the recognition of the asset, income or expense to which the payment or receipt of the foreign currency relates to; ie there is some element of prepayment or deferred income.

49. Applying View B to other foreign currency transactions means that when the advance payment or receipt gives rise to a non-monetary asset or liability that is a prepayment or deferred income, the transaction is recognised in the financial statements using the

exchange rate at the date the advance payment or receipt of cash is initially recognised in the financial statements. This is based on the following principles:

(a) the obligation to perform created by the recognition of an advance receipt of cash and the subsequent fulfilment of that obligation (which gives rise to income (or the reduction in the cost of an asset)) is a single transaction.

(b) similarly, the right to future assets, goods or services (created by an advance payment and recognised as a prepayment) and the subsequent fulfilment of those rights (which gives rise to the recognition of the assets or expense that the prepayment relates) is a single transaction.

(c) the transaction first qualifies for recognition when the transaction is first recorded with a value in the financial statements, which is generally only when one of the parties to the transaction first performs.

50. However, for the reasons given above the proposed interpretation need not apply to:

(a) business combinations or other asset purchases when the consideration for the purchase of the asset is measured at fair value for inclusion in the initial measurement of the asset;

(b) financial instruments or other contracts that are accounted for in accordance with IFRS 9 or IAS 39;

(c) cash-settled share-based payments;

(d) insurance contracts; and

(e) income taxes.

Question 1 for the Interpretations Committee
1. Does the Interpretations Committee agree that the proposed interpretation should apply to other foreign currency transactions that are similarly affected by the issue, as recommended in paragraphs 48-50 above?

Applying the principle to more complex scenarios

51. So far our focus has been on a relatively straightforward fact pattern (100 per cent advance payment, which is non-refundable, of a fixed amount of cash denominated in a foreign currency). In this section we consider the implications of View B for more complex payment arrangements, as follows:

    (a) only part of the consideration is paid or received in advance;

    (b) the advance consideration is a monetary item; and

    (c) the advance consideration is denominated in a foreign currency but in a form other than cash (eg shares denominated in a foreign currency).

Only part of the consideration is paid or received in advance

52. Often advance payments for goods or services are for only part of the total consideration, with the remainder paid on or around the delivery of the related goods or services or in arrears. We consider the implications of this in circumstances in which the goods or services are recognised:

    (a) at a single point in time; and

    (b) at multiple points in time or over time.

Multiple payments for goods/services recognised at a single point in time

53. Consider a scenario in which only part of the consideration is received or paid in advance of the subsequent recognition of the income, expense or asset to which the whole consideration relates, with the remainder of the consideration paid in arrears. The advance consideration is paid or received in cash denominated in a foreign currency and is non-refundable. The income, expense or asset to which the whole consideration relates is recognised in the financial statements completely at a single point in time. For example, an entity may purchase a machine for to use in its business. The payment for the machine is denominated in a fixed amount of foreign currency (say FC100)[7]. The machine is recognised as PPE when it is delivered to the

[7] In this paper, foreign currency amounts are denominated in 'foreign currency units' (FC).

entity. FC20 of the consideration is non-refundable and paid in advance of delivery of the machine and the balance of the consideration is paid in arrears.

54. We think that on applying View B, only part of the contract (FC20 in our example) has initially been recognised on the advance payment and therefore the 'date of the transaction' has only been determined for FC20 of the PPE prior to the date of recognition of the PPE. In this case, FC20 of the machine would be recognised as PPE using the spot rate at the date of the advance payment, and FC80 of the PPE would be recognised using the spot rate at the date of transfer of the goods. We think that this 'blended rate' reflects the economics, which is that on delivery of the goods there is no foreign exchange risk in respect of the FC20 already paid, but the entity is still exposed to foreign exchange risk on the remaining balance. Consequently, applying the spot rate at initial recognition of the PPE for the amount still outstanding represents the best estimate of the cost of that portion of the PPE.

55. Furthermore, the treatment of the part of the income, expense or asset (PPE in our example) paid in arrears is consistent with the exchange rate used to recognise the income, expense or asset (PPE) when 100 per cent of the payment is in arrears. We also note that such an approach minimises structuring opportunities to 'fix' the reported income (including revenue), expense or asset by entering into contracts with de minimis advance payments. Finally, such an approach is, we understand, consistent with US GAAP.[8]

56. Hence, we recommend that the proposed interpretation should clarify that the date of the transaction is determined as the transaction is initially recognised, so if the transaction is initially recognised in stages, so is the date of the transaction. This is consistent with the treatment when payment is in arrears and the transaction is recognised over time as the goods or services are transferred.

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[8] FASB Codification paragraph 830-20-20 *Foreign currency transactions* defines the transaction date as:

> The date at which a transaction (for example, a sale or purchase of merchandise or services) is recorded in accounting records in conformity with generally accepted accounting principles (GAAP). A long-term commitment may have more than one transaction date (for example, the due date of each progress payment under a construction contract is an anticipated transaction date).

Multiple payments for multiple goods/services over time

57. A transaction may be recognised in the financial statements at multiple points in time or continuously over time. If part of the consideration is paid or received in advance, it is necessary to determine which part of the income, expense or asset should be translated on initial recognition using the exchange rate of the advance payment(s) or receipt(s) in the foreign currency.

58. For example, in accordance with IFRS 15, a contract with a customer may have multiple distinct performance obligations that are recognised as revenue at different points in time. Each performance obligation may be recognised over time (such as in many service contracts) or at a point in time.

59. Consider a revenue transaction for which two goods are delivered to a customer; one will be delivered in March and the second in June. The total contract price is FC100, of which FC20 is receivable in January and the balance is receivable in June. Applying IFRS 15 allocates FC40 to the first good and FC60 to the second good. A question arises as to whether the FC20 deferred income relates to the first good, the second good, or both.

60. We think that the revenue that *relates* to the advance receipt should be recognised using the rate at the date of recognition of the deferred revenue (ie the contract liability), with the remainder being recognised using the rate at the date of the related transfer of goods or services. This should reflect the pattern used to release the deferred revenue (ie as the entity fulfils its obligation to transfer the goods), which may depend upon the specific terms and circumstances of each contract. That is, the exchange rate issue should follow the approach taken to amortise the deferred revenue.

61. Hence in our example above, the question becomes whether the FC20 deferred income relates to the first good, the second good, or both, for the purposes of recognising the deferred income as revenue in the income statement on delivery of the goods. We note that this is a general question and not one that is specific to contracts denominated in a foreign currency. Consequently, we do not think that it is appropriate to include, in a proposed interpretation of IAS 21, any guidance on which part of the revenue relates to the advance receipt of consideration.

62. Similarly, for other types of foreign currency transactions, the date of initial recognition of the amount of consideration paid or received in advance is the date of the transaction used to translate the portion of the income, expense or asset, on initial recognition, to which each advance consideration payment or receipt relates. This should reflect the pattern used to derecognise the non-monetary deferred income liability or prepayment asset.

Advance consideration is a monetary item

63. An advance receipt or payment of consideration typically gives rise to a non-monetary deferred income liability or prepayment asset. This is consistent with paragraph 16 of IAS 21, which states that amounts prepaid for goods or services (eg prepaid rent) is an example of a non-monetary item.

64. However, the terms of the transaction could be such that the advance consideration is a monetary item instead of a non-monetary item.[9] The determination of whether an advance payment or receipt gives rise to a monetary or non-monetary item depends upon the specific facts and circumstances, which can be a difficult judgement to make. However, this is a separate issue and we do not intend to include guidance on what is a monetary or non-monetary item as part of the proposed guidance.

65. When the advance consideration is determined to give rise to a monetary item, paragraphs 28 and 29 of IAS 21 require that an exchange difference is recognised in the income statement when there is a change in the exchange rate between the transaction date and the date of settlement of that asset or liability. Consequently, the issue about which exchange rate to use only arises when the advance consideration gives rise to the recognition of a non-monetary prepayment asset or of a deferred income liability. We therefore recommend that the proposed interpretation should only deal with circumstances in which the advance receipt or payment of cash in a foreign currency gives rise to a non-monetary item.

[9] Paragraph 8 of IAS 21 defines monetary items as units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency.

The advance consideration is denominated in a foreign currency but in a form other than cash (eg shares denominated in a foreign currency)

66. In the examples above, the advance consideration has been in the form of cash denominated in a foreign currency. However, other forms of advance consideration may also be non-monetary items denominated in a foreign currency; for example, equity shares denominated in a foreign currency may be received in advance in exchange for the provision of services. Should the proposed interpretation also provide guidance on how to determine the date of the exchange rate in such circumstances?

67. Non-cash consideration is often recognised at fair value (as noted in Appendix C and paragraphs 21 and 29 above, IFRS 15, IFRS 10 and IFRS 3 require non-cash consideration to be recognised at fair value). For purchases, non-cash consideration can also include equity-settled share-based payments. Paragraph 10 of IFRS 2 *Share-based Payment* requires that the entity measures the goods or services received at the fair value of the goods or services rendered. But if the fair value cannot be estimated reliably, the goods or services shall be measured by reference to the fair value of the equity instruments granted instead.

68. The principles in paragraph 23(c) of IAS 21 would require that when an item denominated in a foreign currency is subsequently remeasured at fair value, it is translated using the exchange rate at that measurement date. Hence, to avoid any unintended consequences, we recommend that the proposed guidance should only deal with circumstances in which the advance consideration is cash that is denominated in a foreign currency.

Summary

69. To summarise, we recommend that:

    (a) the proposed interpretation should clarify that the date of the transaction is determined as the transaction is initially recognised, so if the transaction is initially recognised in stages, so is the date of the transaction.

    (b) the date of initial recognition of the amount of consideration paid or received in advance is the date of the transaction used to translate, on initial

recognition, the portion of the income, expense or asset, to which each advance consideration payment or receipt relates. This should reflect the pattern used to derecognise the non-monetary deferred income liability or prepayment asset.

(c) the proposed interpretation only deals with circumstances in which the advance receipt or payment is cash that is denominated in a foreign currency and gives rise to a non-monetary deferred income liability or prepayment asset.

Question 2 for the Interpretations Committee
2. Does the Interpretations Committee agree with the staff recommendations summarised in paragraph 69?

Effective date and transition

Effective date

70. The effective date of any guidance will be determined when the timing of the issue of the final guidance is known. However the staff recommend that the effective date of any guidance is not earlier than the effective date of IFRS 15 (ie for accounting periods beginning on or after 1 January 2017), but with earlier application permitted. This is because our outreach indicates that in practice the issue is particularly widespread in respect of long-term construction contracts. Because of the imminent changes in this area due to the application of IFRS 15, it would be preferable for entities affected by both the proposed interpretation and IFRS 15 to be able to undertake the transition to both at the same time.

Transition requirements

71. In accordance with IAS 8, a change in accounting policy should be made retrospectively, unless there are specific transition requirements in the Standard or Interpretation.

72. Because of the interplay with the initial application of IFRS 15, we recommend that similar transition arrangements should apply, although amended slightly as indicated by the underlined sections below. That is, on initial application entities may either apply the proposed interpretation:

    (i) retrospectively in accordance with IAS 8[10]; or

    (ii) retrospectively with the cumulative effect of initially applying the interpretation at the start of the reporting period in which an entity first applies the Interpretation, or at the start of a prior reporting period presented, but only to transactions that are not completed transactions at that date.

73. As well as being consistent with the transition requirements in IFRS 15, the second option means that entities need not retrospectively restate all assets purchased before either the current reporting period or prior reporting periods presented. Full retrospective application on transition, in particular for foreign currency transactions involving purchases of assets, may be burdensome. Furthermore entities may not have sufficient information to make a reliable restatement.

First-time adopters

74. First-time adopters of IFRS are not permitted to apply the transition requirements in other Standards. Without any specific exemptions in IFRS 1, a first-time adopter is required to use the same accounting policies in its opening IFRS statement of financial position and throughout all periods presented in its first IFRS financial statements.

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[10] IFRS 15 permits the following practical expedients on initial application of the Standard:

a. for completed contracts, an entity need not restate contracts that begin and end within the same annual reporting period;

b. for completed contracts that have variable consideration, an entity may use the transaction price at the date the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods; and

c. for all reporting periods presented before the date of initial application, an entity need not disclose the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the entity expects to recognise that amount as revenue.

However these are not relevant to the initial application of the proposed interpretation and are therefore not considered for inclusion in the proposed transitional arrangements.

75. IFRS 1 does not permit first-time adopters to use the cumulative catch-up transition method in IFRS 15, because it is not consistent with the principles of IFRS 1. This is because it would eliminate comparability within a first-time adopter's first IFRS financial statements by providing relief from restating comparative years. The IASB also observed that the cumulative catch-up transition method may not reduce the burden of retrospective application, because it would potentially require two separate reconciliations—one for the transition to IFRS at the beginning of the earliest comparative period and one for the transition to IFRS 15, at the beginning of the entity's first IFRS reporting period. This would not only be challenging for preparers but might also be confusing for users of financial statements.

76. Despite this, the IASB decided to amend IFRS 1 to provide an optional exemption for first-time adopters from the requirements of IFRS 15 in accounting for contracts completed before the earliest period presented.

77. We could similarly propose an optional exemption for first-time adopters from the requirements of the proposed interpretation for transactions completed before the earliest period presented. But we think that this is unnecessary for transactions recognised in the income statement because the consequence of applying the proposed guidance to the IFRS amounts does not impact on the net profit or loss for a period. It would, however, provide relief from restating assets purchased before the earliest period presented. On the other hand, if there are significant implications of the proposed guidance for first-time adopters, first-time adopters already have the option to elect to measure an item of PPE, investment property or intangible asset at fair value as deemed cost (paragraphs D5-D7 of IFRS 1).

78. We therefore recommend that no specific requirements or exemptions should be given for first-tine adopters in respect of this issue.

Question 3 for the Interpretations Committee
3. Does the Interpretations Committee agree that:

(a) the effective date of any guidance is not earlier than the effective date of IFRS 15 (ie for accounting periods beginning on or after 1 January 2017), but with earlier application being permitted?

(b) on initial application entities may either apply the proposed interpretation:

(i) retrospectively in accordance with IAS 8; or

(ii) retrospectively with the cumulative effect of initially applying the interpretation at the start of the reporting period in which an entity first applies the Interpretation, or at the start of a prior reporting period presented, but only to transactions that are not completed transactions at that date?

(c) no specific provisions or exemptions should be given for first-time adopters?

Next steps

79. The staff recommends that the Interpretations Committee should publish a draft interpretation for public consultation based on the principles in View B, revised as discussed above.

80. If the Interpretations Committee agrees, the staff will draft a proposed interpretation, which will be circulated to members of the Interpretations Committee for review. The draft interpretation will be discussed by the Interpretations Committee at its meeting in March 2015.

Question 4 for the Interpretations Committee

4. Does the Interpretations Committee agree to draft a proposed interpretation for public consultation based on the principles in View B, revised as discussed above?

APPENDIX A

Background to issue and summary of previous tentative conclusions of the Interpretations Committee

A1. This Appendix summarises the issue, as explained in Agenda Paper 14 of the Interpretation Committee's November 2014 meeting. It also summarises the tentative conclusions reached at that meeting. It does not contain any new information or considerations.

The issue

A2. The submitter illustrates the issue with the following scenario:

An entity enters into a sales contract with a customer for delivery of goods or services that is denominated in a foreign currency. A non-refundable payment for the contract is received in advance and, at a later date, the entity transfers the goods or services to the customer.

A3. The submitter asks which exchange rate should be used to recognise the revenue under such a contract in the entity's functional currency in accordance with IAS 21.

A4. Paragraphs 21 and 22 of IAS 21 require that:

(a) A foreign currency transaction shall be recorded, on initial recognition in the functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction.

(b) The date of a transaction is the date on which the transaction first qualifies for recognition in accordance with IFRSs.

A5. The submitter has put forward three views when there is a revenue contract with payment in advance of performance:

(a) View A—revenue is recognised using the exchange rate at the date the contract is entered into, or the date the contract becomes enforceable, if later.

(b) View B—revenue is recognised using the exchange rate at the date the related deferred revenue is recognised (or, if earlier, the date that the revenue is recognised on the transfer of the goods or services).

(c) View C—revenue is recognised using the spot rate at the date of recognition of the revenue (ie on performance of the obligations under the contract by the entity).

Outreach

A6. Outreach indicated that:

(a) the issue is widespread, especially in the construction industry;

(b) there is diversity in practice between View B and View C; and

(c) this diversity expected to continue after implementation of IFRS 15.

Previous tentative conclusions

A7. At its meeting in November 2014, the majority of the Interpretations Committee agreed with the staff analysis that:

(d) IAS 21 is not entirely clear.

(e) IAS 21 does not define 'the transaction' and therefore it is possible to read it as applying separately to the receipt of cash and transfer of goods/services ('two transaction approach') or treat the two events as part of the same transaction ('one transaction approach').

(f) For contracts in which payment is in advance, IFRS 15 can be read as indicating that revenue should be measured at either the spot rate at the date of the advance payment (ie the exchange rate inherent in deferred revenue) or at the spot rate at the date of recognition of the revenue.

(g) For a transaction to 'qualify for recognition in accordance with IFRSs', the transaction must be recorded in the financial statements. Hence View A is not appropriate.

A8. Comparing Views B and C, the majority of the Interpretations Committee members supported View B (the 'one transaction' approach) as a more appropriate interpretation of IAS 21, because:

(a) it reflects that an entity is no longer exposed to foreign exchange risk in respect of the revenue transaction once it has received the cash (ie the entity can control whether or not to continue to hold the foreign currency and be exposed to foreign exchange risk);

(h) the obligation to transfer goods/services (which gives rise to deferred revenue on recognition of an advance cash receipt) and the performance of that transfer (which gives rise to revenue) is a single transaction; and

(i) it is consistent with the treatment of deferred revenue as a non-monetary item.

A9. The Interpretations Committee agreed to add the item to its agenda with the aim of developing an interpretation of IAS 21.

APPENDIX B

IFRIC Update for November 2014

IAS 21 *The Effects of Changes in Foreign Exchange Rates*—Revenue transaction denominated in a foreign currency: What is the date of the transaction for the purpose of identifying the applicable exchange rate for revenue recognition? (Agenda Paper 14)

The Interpretations Committee considered a submission that asked how to determine which exchange rate to use when reporting revenue transactions denominated in a foreign currency in accordance with IAS 21. In particular, the submission described a circumstance in which the customer paid for the goods or services by making a non refundable payment in advance.

The Interpretations Committee noted that outreach indicates that:

a. the issue affects a number of jurisdictions, particularly in the construction industry;
b. there is diversity in practice between recognising revenue using the exchange rate at the date of the receipt of the non-refundable advance payment and the exchange rate at the date of the transfer of goods or services; and
c. the diversity is expected to continue after the implementation of IFRS 15.

The Interpretations Committee noted that paragraphs 21–22 of IAS 21 require that a foreign currency transaction should be recorded, on initial recognition in the functional currency, by applying the spot exchange rate at the date on which the transaction first qualifies for recognition in accordance with IFRS.

The Interpretations Committee tentatively concluded that IAS 21 is not entirely clear on whether revenue should be recognised using the exchange rate at the date of the advance payment or at the date of recognition of the revenue. However, most members of the Interpretations Committee think that recognising revenue using the exchange rate at the date of the advance payment (or at the date that the advance payment is due, if earlier) may be a more appropriate interpretation of IAS 21, because:

a. an entity is no longer exposed to foreign exchange risk once it has received the cash;
b. the obligation to transfer goods or services (which gives rise to deferred revenue on recognition of an advance cash receipt) and the performance of that transfer (which gives rise to revenue) is a single transaction; and
c. it is consistent with the treatment of deferred revenue as a non-monetary item that is not retranslated after initial recognition in accordance with paragraph 23 of IAS 21.

The Interpretations Committee tentatively decided to develop guidance on identifying the date of the transaction for revenue transactions denominated in a foreign currency, as an interpretation of paragraph 22 of IAS 21.

The Interpretations Committee noted that the issue interacts with IFRS 15 and that to the extent that issues arise in respect of IFRS 15, the Transition Resource Group for Revenue (TRG) should be informed of those issues.

The staff will present further analysis at a future meeting of the Interpretations Committee.

APPENDIX C

Interaction with variable consideration and non-cash consideration requirements in IFRS 15

C1. In this appendix, we review the variable consideration and non-cash consideration requirements in IFRS 15, to consider whether the requirements might provide some guidance for the interpretation of paragraph 22 of IAS 21 within the context of foreign currency translation.

C2. The variable consideration requirements in paragraphs 50 and 51 of IFRS 15 state that:

> If the consideration promised in a contract includes a variable amount, an entity shall estimate the amount of consideration to which the entity will be entitled in exchange for transferring the promised goods or services to a customer.
>
> An amount of consideration can vary because of *discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties or other similar items*. The promised consideration can also vary if an entity's entitlement to the consideration is *contingent on the occurrence or non-occurrence of a future event*. For example, an amount of consideration would be variable if either a product was sold with a right of return or a fixed amount is promised as a performance bonus on achievement of a specified milestone. [emphasis added]

C3. The transaction price of a revenue contract in which the consideration is due in foreign currency will vary in value in the entity's functional currency. For example if the amount of foreign currency consideration is fixed at FC100, in terms of the entity's functional currency the consideration will vary in value with movements in the exchange rate.

C4. However, variability in the value of the transaction price in a foreign currency due to exchange rates is not 'similar' to the types of variability listed in italics in the quote in paragraph C2. This is because a variation in value due to exchange rate movements

does not alter the amount of the foreign currency consideration to which the entity is entitled under the contract.

C5. Cash denominated in a foreign currency is not 'non-cash consideration'. Accordingly, the requirements in IFRS 15 for non-cash consideration do not apply. However, foreign currency cash has some features that are similar to non-cash consideration, in that its value varies with movements in the market price of the underlying form of consideration (ie foreign exchange rates). Similarly, if the consideration is in the form of shares, then the value of the consideration varies with its market price.

C6. Paragraphs 66 and 68 of IFRS 15 state the following:

> To determine the transaction price for contracts in which a customer promises consideration in a form other than cash, an entity shall measure the non-cash consideration (or promise of non-cash consideration) at fair value.
>
> The fair value of the non-cash consideration may vary because of the form of the consideration (for example, a change in the price of a share to which an entity is entitled to receive from a customer). If the fair value of the non-cash consideration promised by a customer varies for reasons other than only the form of the consideration (for example, the fair value could vary because of the entity's performance), an entity shall apply the requirements in paragraphs 56–58.

C7. The last sentence in paragraph 68 of IFRS 15 further emphasises that the variable consideration requirements in IFRS 15 do not apply to variability that is only due to the form of consideration—such as variability due to share price movements in respect of shares or foreign exchange movements in respect of foreign currency cash consideration.

C8. Hence we do not think that the variable consideration requirements in IFRS 15 are applicable to the variability that is only due to movements in foreign exchange movements in respect of foreign cash consideration.

C9. IFRS 15 does not state at which date non-cash consideration should be measured at fair value[11]. Consequently, we think that these requirements in IFRS 15 do not provide any further guidance regarding what the appropriate date of transaction might be for the recognition of revenue with foreign currency consideration.

Conclusion

C10. To summarise, we think that the variable consideration requirements in IFRS 15 do not apply to variability in value that is only due to movements in foreign exchange rates. In addition, the non-cash consideration requirements do not apply to cash denominated in a foreign currency. We note that even if applied by analogy, those requirements would not appear to apply to a change in the value of consideration that is solely due to the form of the consideration. Furthermore, we think that these requirements in IFRS 15 do not help to clarify what the date of transaction might be when an entity receives cash in a foreign currency under a contract with a customer.

[11] This issue has already been submitted to the Transition Resource Group for Revenue (TRG) within the context of non-cash consideration and is scheduled for initial discussion at the meeting of the TRG on 26 January 2015. (See TRG submissions log submission number 20.)