STAFF PAPER

May 2016

Project	**High Inflation**		
Paper topic	Comment letter analysis—feedback received from the Agenda Consultation process		
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Purpose

1. This paper summarises the feedback received on the research project on high inflation. That feedback is derived from:

   (a) the International Accounting Standards Board's (the Board's) request for views *2015 Agenda Consultation* ('the RFV'). The RFV was published for public comment in August 2015. The comment period ended on 31 December 2015.[1]

   (b) the short online survey of investors that the Board conducted as part of its work on the RFV, to better understand their priorities with respect to financial reporting.[2]

   (c) the meeting in April 2016 of the Accounting Standards Advisory Forum (ASAF).

2. This paper provides a high-level summary of the comments received. It does not include any staff recommendations.

[1] The full analysis of the comments received on the RFV can be found in Agenda Paper 24A of March 2016.

[2] We use the term 'investor', which we broadly mean to encompass the various members of the investor community, such as asset managers, credit ratings analysts, sell-side and buy-side analysts, creditors and lenders, shareholders, etc.

Structure of this paper

3. This paper is organised as follows:

   (a) background;

   (b) comments received on the high inflation project; and

   (c) background information on countries with high inflation.

Background

4. In this research project, the IASB considered a request made by the Group of Latin American Accounting Standard Setters (GLASS) to:

   (a) eliminate or reduce the cumulative inflation rate threshold currently included in IAS 29 *Financial Reporting in Hyperinflationary Economies* to identify when hyperinflation exists; and

   (b) modify the procedures for reporting the adjustments resulting from restating the financial statements.

5. The Board completed its assessment work on this project in April 2015.[3] At the April Board meeting, the Board tentatively decided that it would not propose lowering the inflation threshold in IAS 29 and nor would it do any work on developing an alternative to IAS 29 or a Standard that addresses inflation more generally. The project was therefore designated as having a low priority but remained on the research programme to enable interested parties to comment on these decisions as part of the 2015 Agenda Consultation.

6. In the RFV, the Board stated that it:

   (a) had completed its assessment of this project and planned no further work at this stage; and

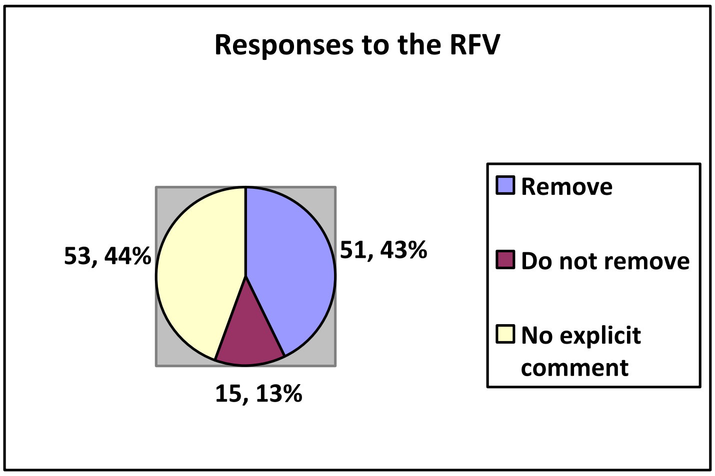
   (b) intended to remove this project from the research programme, unless it receives strong new evidence from the Agenda Consultation that it should reassess its decision.

[3] http://www.ifrs.org/Meetings/MeetingDocs/IASB/2015/April/AP14-High%20Inflation.pdf

Comments received on the high inflation project

Responses to the RFV

7. The Board received 119 comment letters in response to its RFV. 66 respondents (55%) commented on the Board's tentative decision to remove the project from the research programme. 51 (43%) explicitly supported that tentative decision, whereas 15 explicitly opposed it (13%) The other 53 (45%) respondents did not explicitly agree or disagree with the Board's tentative decision.



8. The 51 respondents that explicitly supported the Board's tentative decision to remove the high inflation project from the research programme gave the following reasons:

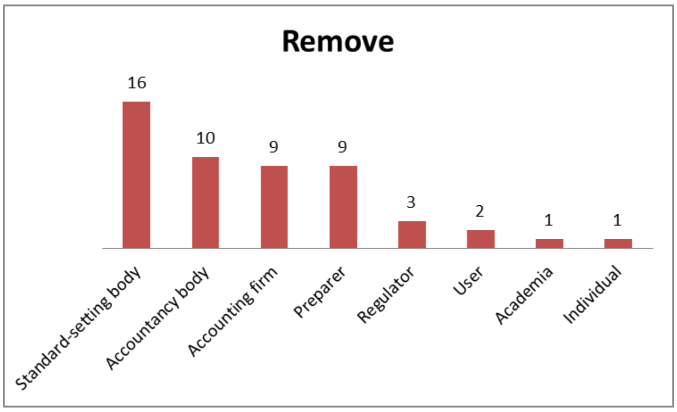
   (a) The issue is of limited interest and applicability. It affects only a few jurisdictions at the moment, and is negligible in most parts of the world.

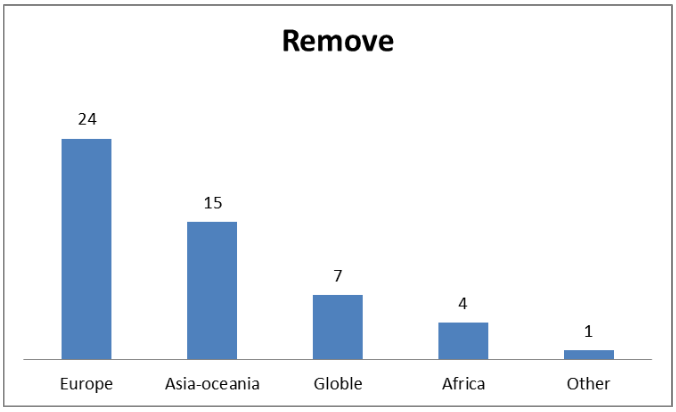
   (b) The Board's assessment of the project shows there is no need to do any more work on the project.

   (c) The project is less important than other projects on the Board's work plan.

   (d) All currently inactive projects should be removed from the research programme.

9. For those respondents supporting the Board's tentative decision to remove the project, their type and geographical location are represented in the following charts:





10. The 15 respondents that explicitly disagreed with the Board's tentative decision to remove the project from the research programme are standard setters in Latin America and the Russian Federation, an accountancy body in Korea, preparers/ preparer bodies in Europe (including Switzerland and the United Kingdom). Their reasons are:

(a) High inflation is a phenomenon that affects many countries in Latin America and other parts of the world.

(b) High inflation causes significant distortions in financial statements well before hyperinflation is reached.

(c) If inflation becomes high in more economies in the future, issues caused by inflation will become more widespread. The Board should be forward-looking in its approach, and should improve IAS 29 now before the need becomes urgent.

(d) In some circumstances, the interaction between IAS 29 and IAS 21 *The Effects of Changes in Foreign Exchange Rates* can lead to distortion of information presented in the financial statements and those distortions cannot be corrected solely by disclosure. This issue is discussed in more detail in Agenda Paper 24E Foreign Currency Translation*: Comment letter analysis—feedback received from the Agenda Consultation process*.

(e) High inflation is more prevalent in emerging economies. Stakeholders in these economics could work on this matter, with the Board keeping a watching brief.[4]

(f) It is better to maintain a list of such potential research projects as an aide-memoire in order to be able to reactivate them quickly if more resources become available, or if a change in the economic or accounting environment leads to a rise in the priority of these projects.[5]

Responses to the online survey

11. As part of its agenda consultation process, the Board conducted an online survey as described for the April 2016 meeting in Agenda Paper 24D *Online Survey: detailed responses and respondent demographics*. 60 (36%) of the 169 respondents to the online survey, including 31 users of financial statements, explicitly supported removing the project from the Board's agenda. 19 (11%) of the respondents disagreed with removing the project. 90 (53%) did not express an explicit opinion on the Board's tentative decision. Those expressing an opinion raised similar issues to those raised in the comment letter responses to the RFV (see paragraphs 8 and 10). A few of those respondents who disagreed with removing the project from the research programme noted that high inflation was less prevalent today. However, they cautioned that this may not be a permanent situation so the Board should not lose sight of the importance of the issue.

[4] This was the only reason given by one of the 13 respondents (a global accounting firm).

[5] This was the only reason given by three of the 13 respondents (representative bodies of preparers in France and Germany, and a German preparer).

Summary of views by the members of the Accounting Standards Advisory Forum (ASAF)

12. During the ASAF meeting in April 2016, the Group of Latin American Accounting Standard-Setters (GLASS) made a presentation on 'Accounting for the Effects of Inflation'.[6] GLASS encouraged the Board to add to its technical programme a project addressing the effects of inflation, considering that entities in many jurisdictions in Latin America are required to pay dividends based on retained earnings. GLASS argued that when dividends are paid on the basis of profits that are not adjusted for the effects of inflation, those dividends are paid from 'paper money' and, in effect, reduce the entity's capital.

13. The recommendation of GLASS is to reduce the level set for one of the indicators that an economy is hyperinflationary, instead of starting a complete and long-term project to review IAS 29. In IAS 29, that indicator currently states that **the cumulative inflation rate over three years is approaching, or exceeds, 100%**. Compared with other indicators in paragraph 3 of IAS 29, that indicator seems to gain more attention that the others, perhaps because it is quantitative. GLASS suggest two options:

    (a) reduce that indicator to, for example, a cumulative inflation rate of 26% over three years. This corresponds to an annual rate of around 8%. At the ASAF meeting, a representative of GLASS stated that this suggestion was based on the following factors:

        (i) by the time inflation reaches around 8%, the effects of inflation are often material;

        (ii) experience shows that countries generally struggle to keep, or bring, inflation under control once it stays above 8% for more than a short period; and

        (iii) Central Banks generally do not set target inflation levels any higher than 8%; or

    (b) require the use of IAS 29 when the effects of inflation are material to the entity.

[6] ASAF meeting Agenda Paper 4 http://www.ifrs.org/Meetings/MeetingDocs/ASAF/2016/April/1604-ASAF-04-0-Presentation-Inflation-project.pdf

14. ASAF members comments included:

(a) Since the development of IAS 29, there have been many economic changes and the levels of inflation that existed globally at the time it was developed are no longer prevalent. Consequently, members understood the call to reduce the threshold in IAS 29 but acknowledged that currently the issue affects limited jurisdictions. However it was acknowledged that the issue also arises on consolidation in other jurisdictions for entities that have some operations in jurisdictions with high inflation.

(b) The Board was encouraged to use indicators to determine whether hyperinflation (or high inflation) exists and so allow management to exercise judgement in deciding when to apply IAS 29. However, members held the view that if indicators are applied, then the inflation index needs to be specified. It was noted that if option (b) in paragraph 12 was proposed (ie require application when the effects are material), all entities would be required to consider whether to apply IAS 29.

(c) IAS 29 was developed some time ago. If it were to be applied more widely, application issues may arise and require the support of the IFRS Interpretations Committee.

(d) Rather than merely changing the scope of IAS 29, one member suggested an alternative would be to complete Chapter 8 of the *Conceptual Framework* (on capital maintenance). This would not address the problem in the short-term but would help the Board to consider a more fundamental review later.

(e) A question raised was whether it was really necessary to amend IAS 29 or whether the Board could instead provide guidance on how to apply the requirements of IAS 29. This option was not supported as many considered that the current Standard is consistently applied.

(f) Before a project could be undertaken, information would be required about the information needs of users of financial statements and about whether IAS 29 produces information that would be acceptable to those users who do not currently use financial statements in which IAS 29 is applied. It was also agreed that greater understanding of global inflation rates was required.

Background information on jurisdictions with high inflation

15. As noted previously, IAS 29 sets out indicators for the presence of hyperinflation. One of these indicators is that **the cumulative inflation rate over three years is approaching, or exceeds, 100%.** One suggestion made by GLASS was to reduce the level of that indicator, to refer to a **cumulative inflation rate over three years is approaching, or exceeds, 26%.** (That change might need to be accompanied by an acknowledgement that the scope of the Standard was being broadened from hyperinflation to high inflation).

16. To enable Board members to test the practical effect of that suggestion, the staff have summarised some data on inflation in various jurisdictions. The data was obtained from the World Bank.[7] It shows the Consumer Price Inflation (CPI) rates since 1987. (For some countries, data is not available for all years).

17. The staff examined the data for countries requiring or permitting the use of IFRS Standards. The data was available for 110 such jurisdictions. Using that data, the staff have identified three groups of countries, according to whether the highest cumulative inflation rate over any three year period since 1987 (the effective date of IAS 29) was:

    (a) above 100% (an indicator of hyperinflation);[8]

    (b) between 26% and 100% (an indicator of high inflation);[9] and

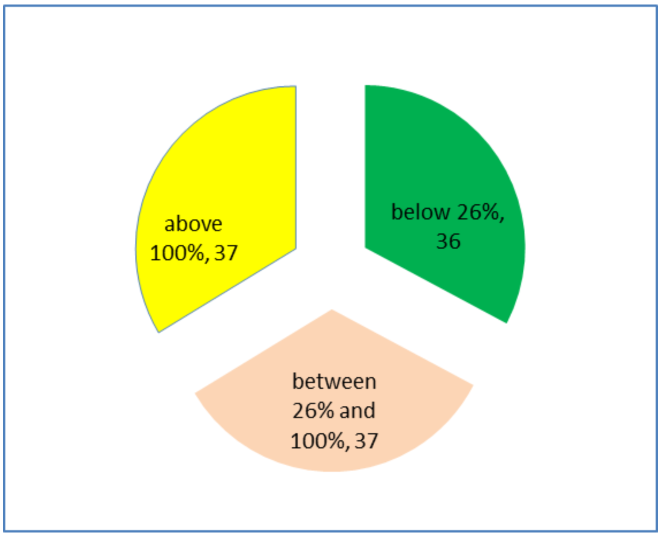
    (c) below 26%.

[7] http://data.worldbank.org/data-catalog/world-development-indicators

[8] Yellow indicates estimated periods in which IAS 29 would apply if a threshold of inflation exceeding 100 per cent over three years is used.

[9] Brown indicates estimated periods in which IAS 29 would apply if a threshold of inflation exceeding 26 per cent over three years is used.

18. The 110 jurisdictions were evenly spread between the three groups.



19. The analysis, set out in the appendices to this paper, shows that if the indicator had been 100 per cent over three years, IAS 29 would have been likely to be applied for 37 jurisdictions. However, if the indicator had been 26 per cent over three years, IAS 29 would have been likely to be applied far more frequently, and by entities in more jurisdictions (74), than is the case using the existing indicator. (As a reminder, the indicator is just one of several indicators; it is not an absolute threshold).

20. Appendix A lists the 36 jurisdictions within the data range for which cumulative inflation did not exceed 26 per cent in any three-year period.

21. Appendix B (Agenda Paper 24G) shows the jurisdictions within the data range for which cumulative inflation exceeded 26 per cent in any three-year period. Periods for which cumulative inflation exceeds 100 per cent are highlighted in yellow.[10] Periods for which cumulative inflation exceeds 26 per cent (but not 100%) are highlighted in orange.

22. The chart in Appendix B shows that the number of jurisdictions for which inflation exceeds 100 per cent has dramatically reduced since the late 1990s. It

[10] Staff suggest that Appendix B be printed in colour, landscape orientaiton and on A3-size paper.

also shows that the number of jurisdictions for which inflation exceeds 26 per cent has reduced significantly since the late 2000s.[11]

[11] Paragraph 12 of Agenda Paper 24E refers to a foreign currency translation issue relating to Venezuela, which relates to inflationary difficulties in that country (see Agenda Paper 24E). Venezuela is not included in the data range covered by the Appendices to this paper. For information, its cumulative inflation rate has been in excess of 26 per cent consistently in each three-year period since 1987. Its cumulative inflation rate exceeded 100 per cent in each three-year period up to 1999 and from 2012-2015.

Appendix A: Jurisdictions within the data range for which cumulative inflation did not exceed 26% in any three-year period.

	Country Name
1.	Antigua and Barbuda
2.	Australia
3.	Austria
4.	Bahrain
5.	Bangladesh
6.	Barbados
7.	Belgium
8.	Belize
9.	Bosnia and Herzegovina
10.	Brunei Darussalam
11.	Canada
12.	Cyprus
13.	Denmark
14.	Dominica
15.	Finland
16.	France
17.	Germany
18.	Grenada
19.	Ireland
20.	Italy
21.	Japan
22.	Kosovo
23.	Kuwait
24.	Luxembourg
25.	Malaysia
26.	Malta
27.	Netherlands
28.	Norway
29.	Oman
30.	Panama
31.	Saudi Arabia
32.	Singapore
33.	Spain
34.	Switzerland
35.	United Arab Emirates
36.	United Kingdom