IFRS Accounting

Staff paper

Agenda reference: 12B

IASB® meeting

Date	**February 2023**
Project	**Lack of Exchangeability (Proposed amendments to IAS 21)**
Topic	**Due process, effective date and other matters**
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Introduction and purpose

1. In December 2022 the International Accounting Standards Board (IASB) decided to proceed with its proposed amendments to IAS 21 with some changes to the proposals in the Exposure Draft *Lack of Exchangeability*.

2. The purpose of this paper is to:

   (a) ask the IASB whether it agrees with our recommendations with respect to potential amendments to other IFRS Accounting Standards:

      (i) IFRS 1 *First-time Adoption of International Financial Reporting Standards*; and

      (ii) IFRS 13 *Fair Value Measurement*;

   (b) ask the IASB whether it agrees with our recommendations with respect to the effective date for the amendments;

   (c) set out the steps in the IFRS Foundation *Due Process Handbook* *(Due Process Handbook)* that the IASB has taken in developing the amendments;

   (d) ask the IASB to confirm it is satisfied that it has complied with the due process requirements; and

(e) ask whether any IASB member intends to dissent from the amendments.

Structure of this paper

3. This paper includes:

    (a) summary of staff recommendations;

    (b) summary of the amendments;

    (c) potential amendments to other Accounting Standards;

    (d) effective date; and

    (e) due process steps and permission for balloting:

        (i) re-exposure;

        (ii) intention to dissent;

        (iii) confirmation of due process steps; and

        (iv) proposed timetable for balloting and publication.

4. There are two appendices to this paper:

    (a) Appendix A—Extracts from the *Due Process Handbook*; and

    (b) Appendix B—Actions taken to meet the due process requirements.

Summary of staff recommendations

5. We recommend that the IASB:

    (a) proceed with the proposed amendments to IFRS 1;

    (b) make no amendments to IFRS 13;

    (c) require an entity to apply the amendments for annual reporting periods beginning on or after 1 January 2025, with earlier application permitted; and

    (d) finalise the amendments without re-exposure.

Summary of the amendments

6. IAS 21 generally requires the use of a spot exchange rate when an entity reports foreign currency transactions or a foreign operation's results and financial position in its financial statements. A spot exchange rate is the exchange rate for immediate delivery. IAS 21 specifies the exchange rate to use in reporting foreign currency transactions when exchangeability between two currencies is temporarily lacking. However, IAS 21 does not specify what an entity is required to do when a lack of exchangeability is not temporary.

7. The IASB proposed to add requirements to IAS 21 for an entity to determine whether a currency is exchangeable into another currency and the accounting requirements to apply when it is not. More specifically, the proposed amendments to IAS 21 would:

    (a) set out factors an entity considers in assessing exchangeability and specify how those factors affect the assessment;

    (b) specify how an entity determines the spot exchange rate when a currency is not exchangeable into another currency;

    (c) require an entity to disclose information that would enable users of its financial statements to understand how a lack of exchangeability between two currencies affects, or is expected to affect, its financial performance, financial position and cash flows; and

    (d) require an entity to apply the amendments from the date of initial application and permit earlier application.

8. In December 2022 the IASB tentatively decided to proceed with its proposals. However, in response to feedback the IASB tentatively decided to make the following changes to the proposals:

    (a) *for factors to consider when assessing exchangeability*—

        (i) clarify that an entity does not consider 'unofficial markets' in assessing exchangeability but, when exchangeability is lacking, it can use exchange rates from these markets to estimate the spot exchange rate;

(ii) develop an example of the 'aggregate method' either as application guidance or an illustrative example; and

(iii) clarify that an entity is required to consider all factors when assessing exchangeability, and that the absence of one factor would indicate a lack of exchangeability.

(b) *for determining the spot exchange rate*—amend proposed paragraph 19A to state that an entity's objective in estimating the spot exchange rate is to reflect at the measurement date the rate at which an orderly exchange transaction would take place between market participants under prevailing economic conditions.

Potential amendments to other Accounting Standards

IFRS 1

9. The requirements in IFRS 1 related to severe hyperinflation refer to, but do not define, exchangeability. Consequently, the IASB proposed aligning that wording in IFRS 1 with the proposed amendments to IAS 21:

> 31C:
>
> If an entity elects to measure assets and liabilities at fair value and to use that fair value as the deemed cost in its opening IFRS statement of financial position because of severe hyperinflation (see paragraphs D26–D30), the entity's first IFRS financial statements shall disclose an explanation of how, and why, the entity had, and then ceased to have, a functional currency that is subject to severe hyperinflation. ~~has both of the following characteristics:~~
>
> ~~(a) a reliable general price index is not available to all entities with transactions and balances in the currency.~~
>
> ~~(b) exchangeability between the currency and a relatively stable foreign currency does not exist.~~

D27:

The currency of a hyperinflationary economy is subject to severe hyperinflation if it has both of the following characteristics:

(a) a reliable general price index is not available to all entities with transactions and balances in the currency.

(b) ~~exchangeability between~~ the currency is not exchangeable into ~~and~~ a relatively stable foreign currency ~~does not exist~~. Exchangeability is assessed by applying IAS 21.

10. Almost all respondents provided no feedback on this proposal. We recommend proceeding with the proposed amendments to IFRS 1.

11. One respondent suggested also amending paragraph D27 of IFRS 1 to state that the currency of a hyperinflationary economy is not considered to be subject to severe hyperinflation when entities using that currency as their functional currency are able to apply IAS 29 *Financial Reporting in Hyperinflationary Economies*. In our view, such a change is beyond the project's scope.

Question 1 – Amendments to IFRS 1
Does the IASB agree with our recommendation to proceed with the proposed amendments to IFRS 1?

IFRS 13

Respondents' comments

12. One respondent to the Exposure Draft suggested providing guidance about the effect on the fair value 'levelling' disclosures required by IFRS 13 from the use of an estimated exchange rate. The respondent said:

> We suggest adding some consideration of the levelling disclosures required under IFRS 13. While the disclosures required by paragraph A17 provide quantification of the carrying

amounts of the assets and liabilities that are affected by a lack of exchangeability, that disclosure is not linked to the fair value hierarchy. We believe that users need to be informed as to the effect on the levelling disclosure from the use of estimated exchange rates.

Consider Entity Y that consolidates its Foreign Operation X. Entity X holds only Level 1 listed securities. There is a lack of exchangeability between the functional and presentation currency of Entity Y and the functional currency of X. It is not clear how the values of Entity X's assets that are based on an estimated exchange rate should be presented in the levelling disclosure in the group financial statements.

Staff analysis and recommendation

13. IFRS 13 establishes a fair value hierarchy and requires an entity to categorise into three levels the inputs to valuation techniques used to measure fair value and to make respective disclosures. This hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1 inputs) and the lowest priority to unobservable inputs (level 3 inputs). Paragraph 73 of IFRS 13 states that a 'fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement'. Therefore, if an estimated exchange rate is an input that is significant to the fair value measurement of an asset or liability, it could affect the fair value measurement category in the fair value hierarchy.

14. The appropriate categorisation of a fair value measurement determined using estimated exchange rates will depend on the facts and circumstances. However, we think the requirements in IFRS 13 are sufficient to enable an entity to determine the appropriate categorisation and make necessary disclosures[1].

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[1] See, for example, the requirements in paragraphs 91 and 93(d) of IFRS 13.

15. Based on our analysis, we recommend making no amendments to IFRS 13.

Question 2 – Amendments to IFRS 13
Does the IASB agree with our recommendation to make no amendments to IFRS 13?

Effective date

16. Paragraph 6.35 of the *Due Process Handbook* explains that the effective date of any amendments is set so that (a) jurisdictions have sufficient time to incorporate the new requirements into their legal systems; and (b) those applying IFRS Accounting Standards have sufficient time to prepare for the new requirements.

17. The IASB generally allows at least 12–18 months between the issuance of a new IFRS Accounting Standard or amendment and its effective date. If the IASB agrees with our recommendations set out in this paper, we expect the IASB to issue the amendments in the third quarter of 2023.

18. We recommend an effective date of annual reporting periods beginning on or after 1 January 2025—that is, approximately 15–17 months after issuance of the amendments.

19. In our view, an entity would have sufficient time to prepare for the new requirements if the IASB were to set this as an effective date because:

    (a) the amendments are narrow in scope; and

    (b) an entity is required to apply the amendments from the date of initial application and not restate comparative information.

20. Further, such an effective date would allow jurisdictions sufficient time to incorporate the new requirements into their legal systems.

21. The IASB received no feedback on its proposal to permit earlier application. We therefore recommend permitting such earlier application, with a requirement to disclose the fact that the amendments have been applied early when that is the case.

Question 3 – Effective date
Does the IASB agree with our recommendation to require an entity to apply the amendments for annual reporting periods beginning on or after 1 January 2025, with earlier application permitted?

Due process steps and permission for balloting

Re-exposure

22. As noted in paragraph 8 of this paper, the IASB tentatively decided to proceed with the amendments including making some changes to the proposals.

23. In the light of these changes, we considered the requirements in paragraphs 6.25–6.29 of the *Due Process Handbook* (reproduced in Appendix A to this paper) to assess whether the IASB should re-expose the amendments.

24. In our view, the changes set out in paragraph 8 of this paper respond to feedback without fundamentally changing the proposed amendments that were included in the Exposure Draft. The changes either clarify the proposed requirements or make the proposed requirements more practical to apply. In our view, it is unlikely that re-exposure would reveal new information or feedback not already considered.

25. Accordingly, we recommend finalising the amendments without re-exposure.

Question 4 – Re-exposure
Does the IASB agree with our recommendation to finalise the amendments without re-exposure?

Intention to dissent

26. In accordance with paragraph 6.23 of the *Due Process Handbook*, we are asking whether any IASB member intends to dissent from the amendments.

Question 5 – Dissent
Does any IASB member intend to dissent from the amendments?

Confirmation of due process steps

27. In our view the IASB has undertaken all the due process steps identified as being required in the *Due Process Handbook* and, thus, is able to finalise the amendments. Appendix B to this paper summarises the due process steps taken in developing the amendments. The applicable due process steps to date for issuing the amendments have been completed.

28. We request permission to start the balloting process if the IASB is satisfied that (a) it has been provided with sufficient analysis, and (b) has undertaken appropriate consultation and due process to support issuing the amendments.

Question 6 – Permission to ballot
Is the IASB satisfied it has complied with the applicable due process requirements and that it has undertaken sufficient consultation and analysis to begin the balloting process for the amendments?

Proposed timetable for balloting and publication

29. The balloting process for the amendments will commence in the near term, with the amendments planned for issue in the third quarter of 2023.

Appendix A—Extracts from the *Due Process Handbook* (August 2020)[2]

6.25 In considering whether there is a need for re-exposure, the Board:

(a) identifies substantial issues that emerged during the comment period on the exposure draft and that it had not previously considered;

(b) assesses the evidence that it has considered;

(c) determines whether it has sufficiently understood the issues, implications and likely effects of the new requirements and actively sought the views of interested parties; and

(d) considers whether the various viewpoints were appropriately aired in the exposure draft and adequately discussed and reviewed in the basis for conclusions.

6.26 It is inevitable that the final proposals will include changes from those originally proposed. The fact that there are changes does not compel the Board to re-expose the proposals. The Board needs to consider whether the revised proposals include any fundamental changes on which respondents have not had the opportunity to comment because they were not contemplated or discussed in the basis for conclusions accompanying the exposure draft. The Board also needs to consider whether it will learn anything new by re-exposing the proposals. If the Board is satisfied that the revised proposals respond to the feedback received and that it is unlikely that re-exposure will reveal any new concerns, it should proceed to finalise the proposed requirements.

6.27 The more extensive and fundamental the changes from the exposure draft and current practice the more likely the proposals should be re-exposed. However, the Board needs to weigh the cost of delaying improvements to financial reporting against the relative urgency for the need to change and what additional steps it has taken to

[2] In this extract, 'Board' refers to the International Accounting Standards Board.

consult since the exposure draft was published. The use of consultative groups or targeted consultation can give the Board information to support a decision to finalise a proposal without the need for re-exposure.

6.28 The Board should give more weight to changes in recognition and measurement than disclosure when considering whether re-exposure is necessary.

6.29 The Board's decision on whether to publish its revised proposals for another round of comment is made in a Board meeting. If the Board decides that re-exposure is necessary, the due process to be followed is the same as for the first exposure draft. However, because it is not the first exposure of the proposed IFRS Standard, it may be appropriate to have a shortened comment period, particularly if the Board is seeking comments on only specific aspects of the revised exposure draft, while recognising that respondents may not limit their comments to these aspects. The public comment period for such documents will normally be at least 90 days.

Appendix B—Actions taken to meet the due process requirements

Step	Required/Optional	Actions
Consideration of information gathered during consultation		
The IASB posts all of the comment letters that are received in relation to the Exposure Draft on the project pages.	Required	All comment letters received by the IASB (48 comment letters) have been posted on the project website.
IASB and IFRS Interpretations Committee meetings are held in public, with papers being available for observers. All decisions are made in public sessions.	Required	At its January 2022 meeting, the IASB discussed a summary of feedback on the Exposure Draft. At its September 2022 meeting, the IFRS Interpretations Committee discussed a summary of feedback on the Exposure Draft and provided advice on the project's direction. At its December 2022 meeting, the IASB considered staff analysis and recommendations and discussed how the project should proceed. The IASB decided to finalise its proposed amendments to IAS 21 with some changes.

Step	Required/Optional	Actions
		All staff papers above are publicly available. The [project page]() has up-to-date information about all related technical papers.
Analysis of likely effects of the forthcoming Standard or major amendment, for example, costs or ongoing associated costs.	Required	The IASB considered the likely effects of the amendments at each stage of their development. The Basis for Conclusions on the amendments will include the IASB's views on these effects.
Finalisation		
Due process steps are reviewed by the IASB.	Required	This step will be met by this Agenda Paper.
Need for re-exposure of a Standard is considered.	Required	This Agenda Paper discusses re-exposure. We recommend not re-exposing the amendments.
The IASB sets an effective date for the Standard, considering the need for effective implementation.	Required	This Agenda Paper discusses the effective date. We recommend an effective date of annual reporting periods beginning on or after

Step	Required/Optional	Actions
		1 January 2025, with earlier application permitted.
Drafting		
Drafting quality assurance steps are adequate.	Required	To be completed in due course. The Translations, Taxonomy and Editorial teams will review the pre-ballot draft. We intend to send a draft of the amendments to external parties for review before finalisation. This process provides us with feedback on the clarity and understandability of the new requirements.
Publication		
News release to announce the final Standard.	Required	To be completed in due course. A news release will be published with the amendments.
A Feedback Statement is provided for a new IFRS Accounting Standard or a major amendment to a	Required	Not considered necessary because these amendments are narrow in scope.

Step	Required/Optional	Actions
Standard, which provides an executive summary of the Standard and explains how the IASB has responded to the comments received.		The Basis for Conclusions on the amendments will explain how the IASB has responded to comments received.
Standard is published.	Required	The amendments will be made available on our website when published.