IFRS Accounting

Staff paper

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Project	**Translation to a Hyperinflationary Presentation Currency**
Topic	**Proposed translation method**
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Introduction

1. As we explain in Agenda Paper 12, this paper includes our summary of the feedback, and our analysis about the proposed translation method included in the Exposure Draft *Translation to a Hyperinflationary Presentation Currency* (Exposure Draft).

Summary of staff recommendations in this paper

2. We recommend:

   (a) subject to the exception in paragraph 2(b), finalising the proposal to require the following entities to translate amounts subject to translation, including comparative amounts, using the closing rate at the date of the most recent statement of financial position[1]:

      (i) an entity whose functional currency is that of a non-hyperinflationary economy that presents its financial statements in a currency of a hyperinflationary economy; and

[1] As we note in Agenda Paper 12, we refer in these papers to this proposal as the 'proposed translation method' throughout this paper.

(ii) an entity whose presentation currency is the currency of a hyperinflationary economy that translates the results and financial position of a foreign operation, whose functional currency is the currency of a non-hyperinflationary economy.

(b) requiring an entity in paragraph (a)(ii)—whose functional currency is that of a hyperinflationary economy and applies IAS 29 *Financial Reporting in Hyperinflationary Economies*—to restate the comparative information of the foreign operation by applying the change in the general price index it applies to corresponding figures in accordance with paragraph 34 of IAS 29.

Structure of this paper

3. In this agenda paper we include:

(a) background and overview of feedback (paragraphs 5–7);

(b) a summary and our analysis of feedback relating to entities translating their own financial statements (paragraphs 8–12);

(c) a summary and our analysis of feedback relating to entities translating a foreign operation (paragraphs 13–37);

(d) staff recommendations (paragraph 38);

(e) question to the IASB (page 17); and

(f) appendix—background information.

4. For simplicity and unless otherwise stated, all references to currencies being either hyperinflationary or non-hyperinflationary refer to the economy of that particular currency.

Background and overview of feedback

Background

5. The International Accounting Standards Board (IASB) proposed requiring an affected entity[2] to apply the proposed translation method. This translation method is already applied by entities with, or for foreign operations with, a hyperinflationary functional currency (see paragraph 42 of IAS 21 *The Effects of Changes in Foreign Exchange Rates)*. The IASB expected the proposed translation method to:

   (a) improve the usefulness of information provided to users of financial statements (investors) by expressing translated amounts in a current measuring unit in a simple and cost-effective manner; and

   (b) remove existing diversity in the accounting applied by entities translating amounts of a foreign operation as described in paragraph 2(a)(ii).

6. The Appendix to this paper reproduces relevant paragraphs from the Basis for Conclusions on the Exposure Draft (Basis for Conclusions) that provide information about the background to the proposed translation method.

Overview of feedback

7. Many respondents agree with the proposed translation method with no concerns and for the reasons considered by the IASB in developing its proposals. In particular:

   (a) almost all respondents agree (or do not disagree) with requiring entities described in 2(a)(i) of this paper to apply the proposed translation method.

   (b) some respondents raise concerns about requiring entities described in paragraph 2(a)(ii) of this paper to apply the proposed translation method. Most notably they expressed concerns about the cost of applying the proposed translation method when preparing comparative information.

[2] Paragraphs 2(a)(i) and 2(a)(ii) set out the affected entities.

Summary and analysis of feedback relating to entities translating their own financial statements

Feedback

8. Almost all respondents agree (or do not disagree) with requiring an entity described in paragraph 2(a)(i)—that is, an entity whose functional currency is non-hyperinflationary that presents its financial statements in a hyperinflationary currency—to apply the proposed translation method.

9. One respondent disagrees. The respondent does not disagree with stakeholders who say applying the current requirements in IAS 21 does not provide relevant information (see for example, paragraphs BC6 and BC29(e) of the Basis for Conclusion). The respondent says:

> …However, the broader issue of relevance of information resulting from translation into a presentation currency is not unique to financial statements presented in the currency of a hyperinflationary economy. It is also the case whenever the exchange rate between the functional and presentation currency is volatile…
>
> Further, the proposed method appears to produce an outcome contrary to the expectations of the users of financial statements who indicated that they would like to be able to translate the entity's (or its foreign operation's) financial statements back into the (functional) currency of a non-hyperinflationary economy as noted in BC20. Accordingly, we believe that, if the issue of relevance of information as a result of translation into a presentation currency is to be addressed, this should be done in a holistic way, i.e. not only in the context of the presentation in the currency of a hyperinflationary economy.

Analysis

10. We acknowledge that questions about the usefulness of information (for example, the accumulation of exchange differences in other comprehensive income as discussed in paragraph BC29(e) of the Basis for Conclusions) could also arise in other situations in which an entity translates its own financial statements to a different presentation currency. This is something the IASB was aware of when developing the proposed amendments. However, as previously discussed, stakeholders said these questions are more pronounced when the presentation currency is hyperinflationary (see paragraph 17(c)(ii) of Agenda Paper 12B for the IASB's December 2023 meeting which reports stakeholders views' that when the entity's presentation currency is hyperinflationary, substantial amounts of exchange differences can accumulate in equity given the level of inflation and resulting devaluation of the local currency).

11. We also note that when an entity has applied the proposed translation method and provided the relevant proposed disclosures (discussed in Agenda Paper 12C of this meeting), investors would be able to easily translate amounts to a non-hyperinflationary currency.

Conclusion

12. Based on our analysis, we continue to think the proposed translation method is appropriate for entities described in paragraph 2(a)(i). Developing a solution for other situations in which an entity translates its own financial statements or extending the proposed translation method to those situations would require further research, outreach and analysis that would go beyond the project's scope.

Summary and analysis of feedback relating to entities translating a foreign operation

Overview

13. Many respondents agree (or do not disagree) with requiring an entity described in paragraph 2(a)(ii) of this paper—that is, an entity whose presentation currency is hyperinflationary that translates a foreign operation whose functional currency is non-hyperinflationary—to apply the proposed translation method to translate a foreign operation. Some respondents raise concerns about the proposals.

14. The most notable concern relates to the cost for an entity whose functional currency is hyperinflationary—and applies IAS 29—of preparing comparative information. In Agenda Paper 12B of this meeting we explain and analyse this concern. Based on our analysis in that paper, we recommend introducing an exception to the proposed translation method. Paragraphs 2(b) and 38(b) summarise that exception.

15. We have grouped and analysed separately other concerns about:

    (a) using the closing rate to get to a current measuring unit (paragraphs 16–24);

    (b) one-way lack of exchangeability (paragraphs 25–29);

    (c) interaction with methods of consolidation (paragraphs 30–36); and

    (d) other matters (paragraph 37).

Using the closing rate to get to a current measuring unit

Proposals

16. In developing the proposed translation method, the IASB acknowledged that at a given point in time exchange rates might not fully reflect differing price levels between the two economies to which a currency relates. Paragraph BC10 of the Basis for Conclusions states:

…Although at a given point in time exchange rates might not fully reflect differing price levels between the two economies to which the currencies relate, the IASB concluded that translating amounts using the closing rate would result in those items being expressed in terms of a current measuring unit because:

(a) paragraph 17 of IAS 29 allows entities to estimate a general price index using movements in the exchange rate between the functional currency and a relatively stable foreign currency when a general price index is not available.

(b) entities in the situation described in the submission to the Committee that apply Alternative II (described in paragraph BC3(b)) translate the assets and liabilities of its foreign operation at the closing rate at the date of the statement of financial position without further restatement. The IASB therefore understands that the closing rate is accepted as a proxy for a current measuring unit for assets and liabilities. The IASB has not identified a conceptual reason to suggest that it is necessary for the current measuring unit for income and expenses and comparative amounts to differ from the current measuring unit for assets and liabilities.

(c) in developing IAS 21, the IASB decided not to require an entity to restate comparative amounts in situations in which the entity's functional currency is the currency of a hyperinflationary economy and its presentation currency is that of a non-hyperinflationary economy (see paragraph BC22 of the Basis for Conclusions on IAS 21). One of the reasons for that decision was, if exchange rates fully reflect differing price levels between the two economies to which they relate, translating comparative amounts would result in the same amounts for the comparatives as were reported as current year amounts in the prior year financial statements. This rationale assumes a sufficient link between changes in a price index and changes in exchange rates.

Feedback

17. A few respondents disagree and say using the closing exchange rate might not result in amounts being measured in terms of a current measuring unit. This is because there might be little correlation between changes in an exchange rate and an inflation index, particularly in jurisdictions that restrict or control the exchange rate.

18. Most of these respondents suggest requiring an entity described in paragraph 2(a)(ii) to continue to apply paragraph 39 of IAS 21 to translate its foreign operation but to then require that entity to restate the results and comparative information of the foreign operation applying the change in the general price index. This approach is 'Alternative II' currently applied by some entities (see paragraphs BC3 and BC12–BC13 of the Basis for Conclusions). Some of these respondents say requiring entities currently applying Alternative II to change to the proposed translation method would result in those entities providing what they view as less useful information.

Analysis

19. As paragraph BC10 of the Basis for Conclusions (reproduced in paragraph 16) notes, the IASB was aware that at a given point in time exchange rates might not fully reflect differing price levels between the two economies to which a currency relates.

20. Respondents did not provide evidence that disputes the IASB's reasons set out in paragraph BC10. We continue to think using the closing rate to translate amounts results in those amounts being measured at a current measuring unit for the reasons in paragraph BC10.

21. Respondents that suggest requiring an entity to apply Alternative II (that is, to restate the results and comparative information of the foreign operation applying the change

in the general price index) did not suggest requiring those entities to also restate the financial position of the foreign operation applying the change in the general price index suggesting they consider that translating financial position amounts (as required applying paragraph 39 of IAS 21) using the closing rate results in those amounts being expressed in terms of a current measuring unit (as also noted in paragraph BC10(b)).

22. The IASB also considered, but decided against, requiring 'Alternative II' to address the accounting matter for translation of a foreign operation. Paragraph BC13 of the Basis for Conclusions states:

> The IASB considered, but decided against, proposing Alternative II for several reasons:
>
> (a) although Alternative II could work for the situation described in the submission (see paragraph BC1), applying it to the related situation (see paragraph BC5) would be complex. The financial statements of an entity described in the related situation are outside the scope of IAS 29. Therefore, Alternative II would provide a solution to address this situation only if the IASB either expanded the scope of IAS 29 or if it introduced an arbitrary rules-based amendment to IAS 29 to include within its scope the financial statements of entities described in the related situation. Alternative II could therefore have wider and unintended consequences.
>
> (b) IAS 21 requires an entity to apply the same translation method in translating its results and financial position and those of a foreign operation to a different presentation currency. Applying Alternative II in circumstances such as those described in the submission while applying a different translation method to the related situation would result in two different translation methods for similar situations.

(c) applying Alternative II, an entity translates its financial position (or that of its foreign operation) using the closing rate at the date of the statement of financial position but translates its results and comparative amounts (or those of its foreign operation) at the spot exchange rate. The entity then restates these results and comparative amounts using a general price index. The IASB has not identified a conceptual reason for requiring an entity to follow different approaches in translating assets and liabilities and income, expenses and comparative amounts for the accounting matter being addressed. In contrast, the proposed translation method would result in an entity applying a consistent translation method to all amounts subject to translation.

(d) compared with the proposed translation method, Alternative II would be costlier for preparers to apply and more difficult for users of financial statements (investors) to understand. Alternative II involves two steps, which would require an entity to use both an exchange rate and a general price index. In comparison, the proposed translation method would, in the IASB's view, be less costly for preparers to apply and easier for investors to understand. The proposed translation method would also facilitate easy translation of amounts to the currency of a non-hyperinflationary economy (an investor would simply need to know the closing rate at the date of the most recent statement of financial position and the amounts subject to translation).

23. We continue to agree with the IASB's reasons for not requiring or allowing an entity to apply Alternative II for the reasons set out in paragraph BC13. We disagree with respondents that say requiring an entity that currently applies Alternative II to apply

the proposed translation method would result in what they view as 'less useful information'. In particular:

(a) for reasons set out in paragraph BC10 of the Basis for Conclusions, we think using the closing rate results in amounts being expressed in terms of a current measuring unit;

(b) applying the proposed translation method and providing the accompanying disclosures will allow investors to more easily translate amounts to a non-hyperinflationary currency;

(c) requiring all entities described in paragraph 2(a)(ii) to apply the proposed translation method will eliminate diversity and increase comparability of information.

Conclusion

24. Based on our analysis, we think no changes are needed in respect of the matter raised. We continue to agree:

(a) with the IASB's view that translating amounts using the closing rate results in those amounts being expressed in terms of a current measuring unit; and

(b) with the IASB's decision to not require or permit an entity to apply 'Alternative II'.

One-way lack of exchangeability

Feedback

25. Paragraph 19A of IAS 21 requires an entity to estimate the spot exchange rate at a measurement date when a currency is not exchangeable into another currency at that date. One respondent says applying the proposed translation method together with paragraph 19A of IAS 21 could result in information that is not useful when there is a one-way lack of exchangeability—that is, a situation in which, for example, Currency

A cannot be exchanged into Currency B but Currency B can be exchanged into Currency A.

26. The example provided in the comment letter (pages 2–3) involves a subsidiary whose functional currency is Euros (which the comment letter assumes as being non-hyperinflationary) that has some transactions denominated in Argentinean pesos (ARS) (which the comment letter assumes as being hyperinflationary). This subsidiary is consolidated into a group whose presentation currency is the ARS. The example also assumes that ARS are not exchangeable to Euros, but Euros are exchangeable into ARS.

27. The respondent says because ARS are not exchangeable into Euros, the subsidiary will apply paragraph 19A of IAS 21 and will translate transactions denominated in ARS to Euros (being the functional currency of the subsidiary) using an estimated exchange rate. Applying the proposed translation method, the parent will then translate those Euro amounts to ARS using the official exchange rate because Euros are exchangeable into ARS.

28. Due to potential differences between the estimated exchange rate and the official exchange rate, the amounts presented in ARS in the consolidated financial statements might differ from the ARS amounts of the subsidiary's transactions. The respondent questions whether this outcome provides useful information. The respondent acknowledges that:

    (a) this outcome is not created by the proposals in the Exposure Draft but results from applying paragraph 19A of IAS 21; and

    (b) similar outcomes might arise in other situations (for example, when an entity whose functional currency is hyperinflationary presents its financial statements in a non-hyperinflationary currency).

Analysis and conclusion

29. We acknowledge the respondent's comment. However, we think no changes are needed in respect of this matter. This is because:

(a) as noted by the respondent, the outcome described is not created by the proposed translation method. In our view, the outcome is also not 'worsened' by requiring affected entities to apply the proposed translation method. The same outcome could arise when the entity described in paragraph 2(a)(ii) of this paper applies paragraph 39 of IAS 21—which it does when applying any of the 3 alternative approaches currently used in practice (see paragraph BC3 of the Basis for Conclusions reproduced in the appendix to this paper) to translate a foreign operation if there is a one-way lack of exchangeability between the two currencies involved.

(b) similar outcomes might arise in other situations. Consequently, developing requirements or application guidance to address situations with one-way lack of exchangeability would go beyond the scope of this project.

Interaction with methods of consolidation

30. A footnote to paragraph 17 of IFRIC 16 *Hedges of a Net Investment in a Foreign Operation* describes two methods of consolidation. The footnote says:

> The direct method is the method of consolidation in which the financial statements of the foreign operation are translated directly into the functional currency of the ultimate parent. The step-by-step method is the method of consolidation in which the financial statements of the foreign operation are first translated into the functional currency of any intermediate parent(s) and then translated into the functional currency of the ultimate parent (or the presentation currency if different).

Feedback

31. Two respondents question whether the proposed translation method would affect the method of consolidation (direct or step-by-step) an entity is able to apply. These respondents question the wording of proposed paragraph 41A of IAS 21 (the proposed translation method) that applies if: '…[an entity's] functional currency is the currency of a non-hyperinflationary economy …' If an entity's foreign operation is itself a group, that group might not have a single functional currency that would make it eligible to apply the proposed translation method.

32. Paragraph 17 of IFRIC 16 explains that differences in amounts of exchange differences could arise depending on whether an entity applies either the direct or step-by-step method of consolidation. One of the abovementioned respondents says that applying the proposed translation method would result in the differences between applying the two methods of consolidation to be different from what is currently the case. They question to what extent the proposed translation method is an improvement to the current requirements.

Analysis

33. Paragraphs 38–43 of IAS 21 are worded from the perspective of an entity translating its financial statements from its functional currency into a different presentation currency. These requirements refer to an entity's functional currency. Applying paragraph 44 of IAS 21, an entity that translates its foreign operation to a different presentation currency applies these same paragraphs (in addition to some other paragraphs) when translating the foreign operation.

34. The question raised (about whether the proposed translation method prevents the use of a particular method of consolidation) is therefore not new and could also arise applying translation methods as currently worded in IAS 21. For example, paragraph 42 of IAS 21 applies to an entity—and applying paragraph 44 of IAS 21, to a foreign operation—whose functional currency is hyperinflationary. If the foreign operation is

a group that does not have a single functional currency, similar challenges could arise in assessing whether to apply paragraph 42 of IAS 21.

35. We acknowledge that the proposed translation method could introduce different differences if an entity applies either the direct or step-by-step method of consolidation than might arise applying existing requirements. However, we have no evidence to suggest any difference between the two consolidation approaches that could arise applying the proposed translation method would result in less useful information.

Conclusion

36. Based on our analysis, we think the matter raised is not a consequence of, and is not made worse by, the proposed translation method and consequently, that no change is needed in respect of the matter raised.

Other matters

37. In Table 1 we summarise and analyse other matters raised by respondents. We think no change is needed in respect of the matters raised.

Table 1—Our analysis of other matters raised by respondents

Comment	Staff analysis
A few respondents continue to request guidance on how to present any differences that arise on consolidation when applying the proposed translation method in the statement(s) of financial performance.	We continue to agree with the IASB's decision to not specify how an entity presents any such differences for the reasons in paragraph BC31 of the Basis for Conclusions. We have not received new information that suggests a need to now address the matter.

Comment	Staff analysis
One respondent says, in their view, in accordance with paragraph 35 of IAS 29 it would be inappropriate to express amounts of a foreign operation in a current measuring unit if that foreign operation's functional currency is non-hyperinflationary. They say the entity should translate such a subsidiary in accordance with paragraph 39 of IAS 21 with no further adjustment.	We disagree with the respondent. Paragraph BC4 of the Basis for Conclusions states, having considered the requirements in IAS 21 and IAS 29 (including paragraph 35 of IAS 29), the IFRS Interpretations Committee (Committee) concluded that an entity could justifiably either restate the results and comparative amounts of a foreign operation, or not do so. BC7 also states that, based on its research, the Committee noted that not expressing amounts in a current measuring units does not result in useful information.
One respondent—a respondent that also raises concerns about the proposals overall—is concerned that the proposals will result in all affected entities being required to change their accounting treatment. They said they have not observed significant diversity in practice.	Developing the proposals, the IASB was aware that its proposals would require all affected entities to change their current accounting treatment. However, for reasons set out in paragraphs BC29–BC32 of the Basis for Conclusions, the IASB concluded the expected benefits of the proposed translation method outweigh their costs. Feedback has not provided evidence that disputes those

Comment	Staff analysis
	reasons. Other feedback on the Exposure Draft did not include evidence that disputes the evidence the IASB (and the Committee) gathered when developing the proposals that supported that diversity in accounting exists.

Staff recommendations

38. Based on our analysis in this paper and Agenda Paper 12B, we recommend that the IASB:

    (a) finalise its proposal to require an affected entity (as described in paragraphs 2(a)(i) and 2(a)(ii) of this paper) to apply the proposed translation method to translate amounts subject to translation, including comparative amounts; and

    (b) require an entity described in paragraph 2(a)(ii) that applies IAS 29—that is, whose functional currency is hyperinflationary—to restate the comparative information of the foreign operation by applying the change in the general price index it applies to corresponding figures in accordance with paragraph 34 of IAS 29.

Question to the IASB

Question for the IASB
1. Does the IASB agree with our recommendations in paragraph 2?

Appendix—Background information

A1. This appendix reproduces paragraphs BC1–BC8 of the Basis for Conclusions which state:

BC1 The IFRS Interpretations Committee (Committee) received a submission about the application of IAS 21 *The Effects of Changes in Foreign Exchange Rates* and IAS 29 *Financial Reporting in Hyperinflationary Economies*. The submission asked how an entity, whose functional and presentation currencies are hyperinflationary, translates the results and financial position of a foreign operation, whose functional currency is non-hyperinflationary. In this situation, the entity applies paragraph 39 of IAS 21 to translate the results and financial position of its foreign operation. Applying this paragraph, the entity:

(a) translates assets and liabilities for each statement of financial position presented at the closing exchange rate at the date of that statement of financial position;

(b) translates income and expenses using exchange rates at the dates of the transactions; and

(c) does not restate comparative amounts.

BC2 Because the entity's functional and presentation currencies are hyperinflationary, the Committee was asked whether, after applying paragraph 39 of IAS 21, the entity is required to apply paragraphs 26 and 34 of IAS 29 to restate the current period income and expenses and all comparative amounts of its foreign operation in terms of the measuring unit current at the end of the reporting period. (The assets and liabilities of the foreign operation are translated using a closing exchange rate—see paragraph BC1— and the Committee was not asked whether the entity is required to restate those amounts.)

BC3 The Committee observed that entities apply diverse accounting treatments. Entities either:

(a) do not restate current period income and expenses and comparative amounts (Alternative I);

(b) restate current period income and expenses and comparative amounts using the change in the general price index (Alternative II); or

(c) restate only the comparative amounts using the change in the general price index (Alternative III).

BC4 Having considered the requirements in IAS 21 and IAS 29, the Committee concluded that an entity could justifiably either restate current period income and expenses and comparative amounts, or not do so.

BC5 In carrying out further research to determine whether to recommend standard-setting, the Committee was alerted to a related situation in which an entity, whose functional currency is that of a non-hyperinflationary economy, presents its financial statements in the currency of a hyperinflationary economy. In this situation, the entity also applies paragraph 39 of IAS 21 to translate its financial statements. IAS 29 applies only to the financial statements of entities whose functional currency is that of a hyperinflationary economy, and therefore, there is no question as to whether this entity is required to then apply IAS 29 to restate income and expenses and comparative amounts in terms of a current measuring unit.

BC6 Stakeholders who were consulted said amounts presented in the currency of a hyperinflationary economy are useful only if expressed in terms of a current measuring unit. This view is consistent with the principles in paragraphs 2 and 7 of IAS 29. In the related situation, income and expenses and comparative amounts would not be restated. In the situation described in the submission, unless an entity applies Alternative II (described in paragraph 10(b)), income and expenses and comparative amounts of the foreign operation would also not be restated.

BC7 The Committee noted that when an entity translates amounts from a functional currency that is the currency of a non-hyperinflationary economy to a presentation currency that is the currency of a hyperinflationary economy, applying the requirements in IAS 21 does not result in useful information. The Committee's research confirmed that this accounting matter is pervasive in many (although not all) jurisdictions that are hyperinflationary economies and could have a material effect on entities affected.

BC8 The Committee discussed and recommended to the IASB the proposed translation method—translating a qualifying entity's financial statements (or the results and financial position of a foreign operation), including comparatives, at the closing rate at the date of the most recent statement of financial position—as a possible solution. The Committee considered this solution would improve the usefulness of the resulting information in a simple and cost-effective manner and remove existing diversity.