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The IASB ED – *Lack of Exchangeability* Summary and Analysis of the Comment Letters Received

Background

1 On 20 April 2021, the IASB published Exposure Draft *Lack of Exchangeability* (the ED), with a 120-day comment period ending on 1 September 2021. In the ED, the IASB proposed to amend IAS 21 *The Effects of Changes in Foreign Exchange Rates*. In response to the ED, on 3 June 2021, EFRAG published its draft comment letter (the DCL) and asked for constituents' views by **26 August 2021.**

2 This paper provides a summary of the comment letters received as the formal responses of constituents' to EFRAG's DCL.

3 The feedback received from EFRAG's outreach activities is summarised in Paper 02-02 for this session.

Summary of responses

4 Till the date of finalising of this paper, six comment letters have been received from the following constituents:

(a) Four National Standard Setters (ASCG, OIC, ANC, DASC);

(b) One European Regulator (ESMA);

(c) One European preparers' organisations (Acteo/Afep/Medef).

Comment letter analysis

5 The details of the responses are provided below.

Analysis of the feedback received from comment letters

6 Till the date of finalisation of this paper, EFRAG has received six comment letters. The detailed analysis of the respondents and their comments is provided in Agenda Paper 02.03 to this meeting.

7 Generally, all respondents broadly support the proposals to amend to IAS 21.

Assessment of whether a currency lacks exchangeability (Question 1 of the ED)

8 All respondents support the objective and process of assessment whether a currency lacks exchangeability.

Estimating spot exchange rate (Question 2 of the ED)

9 All respondents welcome the proposal and in general agreed with the approach. However, they provided the following comments/requests:

(a) The use of an observable exchange rate should rather be required, when it fulfils the condition in paragraph 19A of the ED, rather permitted.

(b) The rationale behind permitting (and not requiring) the use of an observable rate, should be clarified because lack of explanations has created confusion among stakeholders.

(c) Developing a framework to support the estimation process and adding illustrative examples (based on real cases) has been suggested to enhance preparers' understanding.

(d) Guidance on the use of unofficial rates as an input in the estimation process should be clarified.

(e) The ED does not address the situations where a functional currency is that of hyperinflationary economy and the official exchange rate does not enough reflect inflation. The guidance should therefore address the situations and clarify the guidance in IAS 29 *Financial Reporting in Hyperinflationary Economies*.

Disclosures (Question 3 of the ED)

10 All respondents agree (or do not disagree or raise concerns) to the proposed disclosure requirements.

11 None of the respondents proposed additional disclosure requirements on top of the existing and newly proposed ones.

Transition (Question 4 of the ED)

12 All respondents agree (or do not disagree or raise concerns) to the proposed transition requirements.

Response to EFRAG's questions to constituents

13 Two respondents provided comments on EFRAG's questions to constituents

Paragraph 25 - Use of observable rate

14 The use of an observable exchange rate should be permitted as proposed in the ED. In the specific situations where the spot exchange rate is not objectifiable, an entity should have the flexibility to find the most economically reasonable solution in determining the spot exchange rate. Thus, the economic content should have priority over objectivity.

15 In view of another respondent, however, the use of an observable rate should still be permitted rather than required. A disclosure requirement explaining the reason for not applying the observable exchange rate should be considered, provided this additional disclosure would not compromise the entity's situation.

Paragraph 26 – Methods used to estimate spot exchange rates

16 One respondent explained that, if no objectifiable exchange rate exists, the official exchange rate is typically used, even though this exchange rate does not faithfully reflect the prevailing economic conditions.

Paragraph 27 – Functional currency

17 In view of one respondent, in accordance with IAS 21, an entity's functional currency can be changed only if there is a change to the underlying transactions, events, and conditions relevant to the entity. Therefore, an entity assesses whether the lacking exchangeability leads to changes of those underlying transactions, events, and conditions of a foreign operation: If yes, an entity changes the functional currency of this foreign operation by applying IAS 21.

18 In view of another respondent, it was worth investigating even though it may require other amendments to IAS 21's provisions on how an entity determines its functional currency.

Paragraph 28 – Additional guidance regarding the estimation process

19 In view of both respondents, some additional guidance is considered as necessary. This guidance should be in a form of illustrative examples on how an entity would reasonably estimate the exchange rate when there is no observable exchange rate or when the observable exchange rate does not meet the conditions of an estimated spot rate in paragraph 19A.

Paragraph 36 – Additional disclosure requirements

20 In view of one respondent, no additional disclosures, apart from those already proposed, should be considered.