

EFRAG's draft endorsement advice on the amendments to IAS 21 *The Effects of Changes in Foreign Exchange Rates: Lack of Exchangeability*
Cover Note

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG FR TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG FRB or EFRAG FR TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG FRB, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Objective

- 1 The objective of the session is to update the EFRAG FR TEG members on the developments in the IASB's project *Lack of Exchangeability* project, and to receive their comments on, and their recommendation to the EFRAG FRB to approve the draft EFRAG endorsement advice (draft *Letter to the European Commission*) on the amendments to IAS 21 *The Effects of Changes in Foreign Exchange Rates: Lack of Exchangeability* (the Amendments) – later referred to as “the DEA”.

Background of the IASB project

- 2 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 this situation is not temporary.
- 3 The IASB was informed of diverse views on how to determine whether a currency is exchangeable into another currency and the exchange rate to use when it is not. In situations when economic conditions deteriorate rapidly, the diverse views on the application of IAS 21 could lead to material differences in the financial statements of entities affected by a currency that is not exchangeable to a relevant currency.
- 4 Furthermore, for hyperinflationary economies which may also be accompanied by the currency not being exchangeable, IAS 29 *Financial Reporting in Hyperinflationary Economies* requires the reporting entity to firstly restate non-monetary assets and liabilities of the foreign subsidiary to reflect inflation by applying a general price index before retranslating subsidiary's financial statement into reporting currency.
- 5 On 20 April 2021, in order to respond to the issues related with exchangeability of a currency, the IASB proposed to amend IAS 21 and to specify:
 - (a) when a currency is exchangeable into another currency and, consequently, when it is not;
 - (b) how an entity determines the exchange rate to apply when a currency is not exchangeable; and
 - (c) the disclosures an entity provides when a currency is not exchangeable.

- 6 On 15 August 2023, following a comment period, the IASB issued the Amendments. The Amendments are available on the IASB website. For a short time and for the purpose of the endorsement process, the Amendments are also provided on EFRAG's website [here](#).

Background of the EFRAG discussions

- 7 On 14 September 2021, EFRAG issued its comment letter where, in principle, EFRAG agreed with the IASB's proposals to amend IAS 21 to address the issue of insufficient guidance applicable to the situations where a currency is not exchangeable into another currency. EFRAG considered that the proposals would lead to a reduction of divergency in practice and an increase in transparency about what method is applied.
- 8 EFRAG raised several requests to clarify the proposals in order to better align the proposals with the existing guidance.

EFRAG's initial assessment on the Amendments

- 9 EFRAG's initial assessment is that the Amendments satisfy the criteria for endorsement for use in the EEA and that endorsing the Amendments is conducive to the European public good.
- 10 Therefore, EFRAG recommends their endorsement.

Summary of the recent EFRAG's discussion on the DEA

- 11 In September 2023, EFRAG discussed the draft version of the DEA with FIWG and IAWG. Their members provided limited drafting suggestions and noted that the amendments provide clarifying guidance however the pervasiveness of the issue addressed in the amendments is low.

Question to EFRAG FR TEG members:

- 12 Do you have observations on the Amendments, and comments or drafting suggestions on EFRAG's DEA on the Amendments?
- 13 Do you recommend the DEA for the EFRAG FRB to approve?
- 14 Do you agree with the proposed 70-day comment period?

Next steps

- 15 The EFRAG will seek EFRAG FRB approval of the DEA by written procedure.
- 16 EFRAG Secretariat proposes a **70-day comment period** starting on 28 September 2023. This comment period would allow EFRAG FR TEG to discuss the draft of the final endorsement advice on 20 December and to proceed with the EFRAG FRB's approval in a form of written procedure in early January 2024.

Agenda Papers

- 17 In addition to this cover note:
- (a) Agenda Paper 04-02 Exchangeability DEA - Draft Letter to EC
 - (b) Agenda Paper 04-03 Exchangeability DEA – Invitation to comment
- have been provided for the session.
- 18 The Amendments are available on the IASB website. For a short time and for the purpose of the endorsement process, the Amendments are also provided on EFRAG's website [here](#).