© DRSC e.V	Zimmerstr. 30	10969 Berlin	Tel.: (030) 20 64 12 - 0	Fax: (030) 20 64 12 - 15
Internet: www.drsc.de			E-Mail: info@drsc.de	

Diese Sitzungsunterlage wird der Öffentlichkeit für die FA-Sitzung zur Verfügung gestellt, so dass dem Verlauf der Sitzung gefolgt werden kann. Die Unterlage gibt keine offiziellen Standpunkte des FA wieder. Die Standpunkte des FA werden in den Deutschen Rechnungslegungs Standards sowie in seinen Stellungnahmen (Comment Letters) ausgeführt.
Diese Unterlage wurde von einem Mitarbeiter des DRSC für die FA-Sitzung erstellt.

IFRS-FA – öffentliche SITZUNGSUNTERLAGE

Sitzung:	**30. IFRS-FA / 01.09.2014 / 10:45 – 11:45 Uhr**
TOP:	**03 – Interpretationsthemen**
Thema:	**Aktuelle Interpretationsthemen**
Unterlage:	**30_03_IFRS-FA_Interpret_CN**

1 Sitzungsunterlagen für diesen TOP

1 Für diesen Tagesordnungspunkt (TOP) der Sitzung liegen folgende Unterlagen vor:

Nummer	Titel	Gegenstand
30_03	30_03_IFRS-FA_Interpret_CN	Cover Note

Stand der Informationen: 12.08.2014.

2 Ziel der Sitzung

2 Der IFRS-FA hat in seiner 29. Sitzung diverse Interpretationsthemen erörtert. Es wurde beschlossen, zu zwei vorläufigen Entscheidungen (TAD) Stellung zu nehmen. Es handelt sich um die zu IAS 21 / IAS 29 (*Foreign exchange restrictions and hyperinflation*) und die zu IAS 19 (*Remeasurement at a plan amendment or curtailment*). In dieser 30. Sitzung soll der entsprechend erstellte **Stellungnahmeentwurf abschließend besprochen** werden. Die Kommentierungsfrist beim IFRS IC endet am 29. September 2014. D.h. die Stellungnahme wird nach der 30. Sitzung im Umlaufverfahren finalisiert.

3 Im nachfolgenden Abschnitt 3 sind ggf. hilfreiche Hintergrundinformationen zu den IFRS IC-Entscheidungen enthalten.

3 Informationen im Detail

3.1 IAS 21 / IAS 29 – *Foreign exchange restrictions and hyperinflation*

4 Das IFRS IC hatte im Juli 2014 über den Sachverhalt vorläufig entschieden; der Wortlaut der Entscheidung lautet wie folgt (Auszug IFRIC Update 7/2014):

> The IFRS IC received a request for guidance on the translation and consolidation of the results and financial position of foreign operations in Venezuela. The issue arises because of strict foreign exchange controls in Venezuela. This includes the existence of several official exchange rates that may not fully reflect the local rate of hyperinflation and of restrictions over the amount of local currency that can be exchanged.
>
> Concerns were raised that using an official exchange rate to translate an entity's net investment in a foreign operation in Venezuela appeared not to appropriately reflect the financial performance and position of the foreign operation in the group's consolidated financial statements.
>
> The IFRS IC identified two primary accounting issues:
>
> a. which rate should be used to translate the entity's net investment in the foreign operation when there are multiple exchange rates?
>
> b. what rate should be used when there is a longer-term lack of exchangeability?
>
> With respect to the first issue, the IFRS IC observed very little diversity in practice regarding the principle to use when determining which of multiple rates should be used to translate an entity's net investment in a foreign operation. The IFRS IC noted that predominant practice is to apply by extension the principle in IAS 21.26, which gives guidance on which exchange rate to use when reporting foreign currency transactions in the functional currency when several exchange rates are available. Hence, despite the widespread applicability, the IFRS IC [decided] not to take the first issue onto its agenda.
>
> With respect to the second issue, the IFRS IC observed that this issue is widespread and has led to some diversity in practice. A longer-term lack of exchangeability is not addressed by the requirements in IAS 21, and so it is not entirely clear how IAS 21 applies in such situations. However, the Interpretations Committee thought that addressing this issue is a broader-scope project than it could address (because of related cross-cutting issues). Accordingly the IFRS IC [decided] not to take this issue onto its agenda.
>
> However, the IFRS IC noted that several existing disclosure requirements in IFRS would apply when the impact of foreign exchange controls is material to understanding the entity's financial performance and position. Relevant disclosure requirements in IFRS include:
>
> a. disclosure of significant accounting policies and significant judgements in applying those policies (IAS 1.117-124);
>
> b. disclosure of sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year, which may include a sensitivity analysis (IAS 1.125-133); and

c. disclosure about the nature and extent of significant restrictions on an entity's ability to access or use assets and settle the liabilities of the group, or its joint ventures or associates (IFRS 12.10, 13, 20 and 22).

5 Die ursprüngliche Anfrage ging im Frühjahr 2014 beim IFRS IC ein und betrifft die Verwendung staatlich vorgegebener Wechselkurse (teils auch Wechselkontingente) in einem hochinflationären Umfeld. Im Mai 2014 hatte das IFRS IC einen *Outreach Request* hierzu gestartet. Dabei wurde der Sachverhalt wie folgt übermittelt und mit folgenden Fragen versehen:

0. Introduction

The IFRS IC has received a submission requesting guidance on the translation and consolidation of the results and financial position of foreign operations in Venezuela under IAS 21 *The Effects of Changes in Foreign Exchange Rates*. Concerns arise that, because of strict foreign exchange controls over the exchange of the Venezuelan Bolivar Fuerte (VEF) combined with a hyperinflationary economy, applying IAS 21 (and IAS 29 *Financial Reporting in Hyperinflationary Economies)* may not reflect the underlying economics of the foreign operation.

We would appreciate your input to help identify the extent to which entities with foreign operations in (i) Venezuela, and (ii) any other countries with foreign exchange controls or restrictions, experience similar issues when applying IAS 21; and whether there is any divergence in practice under similar circumstances. We are particularly interested in receiving details of examples of other entities with foreign operations that share the same key features as the issue in the submission.

1. Background of issue

The submitter notes that various issues arise when international groups account for foreign operations in Venezuela that have a VEF functional currency. This is because Venezuela is a hyperinflationary economy with strict foreign exchange controls over the exchange of VEF.

There are several official exchange rate mechanisms for the conversion of VEF, each with different exchange rates, available depending upon specific circumstances. We understand that there have been recent developments in this area and that there are currently three such exchange mechanisms in Venezuela, as summarised in the appendix below. We understand that the volume of VEF which can be exchanged using these official exchange rate mechanisms (into say US$) is restricted, such that in practice entities may not be able to exchange all of their VEF cash balances using the available rates.

Entities whose functional currency is that of a hyperinflationary economy are required under IAS 29 to state their financial statements in terms of the measuring unit current at the end of the reporting period by applying a general price index. Groups consolidating such subsidiaries translate these inflation-adjusted subsidiary financial statements into the group's presentation currency (for example US$) at the closing exchange rate in accordance with IAS 21. The submitter notes that:

- prevalent practice is to translate foreign operations into the group's presentation currency using official exchange rates.
- for operations with a VEF functional currency the official CENCOX fixed exchange rate has typically been used as the closing rate under IAS 21 on the basis that it was the only official exchange mechanism available to a group.
- in the submitter's experience, such a rate is only available for a relatively limited volume of currency in practice, such that a Venezuelan subsidiary may have more cash in VEF than it is able to convert into US$ (and hence repatriate) using the official exchange rate mechanisms.

- due to foreign exchange controls the official exchange rates for VEF (in particular the fixed CEN-COX and variable SICAD I rates) do not reflect the local rate of hyperinflation.

As a consequence, the submitter is concerned that, from an economic perspective, the group financial statements appear:

- On translation of the foreign operation's functional currency financial statements into the group's presentation currency: * to overstate the Venezuelan subsidiary's assets and liabilities (including local cash held in VEF); ** to overstate income from the Venezuelan operations (which is further compounded by the IAS 29 inflation-adjustments in the Venezuelan entity's financial statements).
- On translation of non-VEF denominated monetary balances into VEF in the foreign (Venezuelan) operation's financial statements: to understate foreign exchange losses (or gains) in profit or loss arising on US$ (or other non VEF) denominated balances in Venezuela. Those balances include intercompany balances that eliminate on consolidation, as the foreign exchange gains and losses that arise in the Venezuelan subsidiary remain on consolidation (unless they are considered to be part of the group's net investment in the foreign operation).

2. Key accounting issues

The submitter requests that the IFRS IC review the current approach for translating and consolidating foreign operations in Venezuela to address the concerns noted above. The key accounting issues in this scenario appear to arise over which exchange rate should be used for:

(i) the translation of the foreign operation's functional currency financial statements into the group's presentation currency; and

(ii) the translation of non-functional currency denominated monetary balances in the foreign operation into the foreign operation's own functional currency.

The first accounting question raised is which rate(s) should be used when multiple official exchange rates are available. (Note that guidance is already given in IAS 21 paragraph 26 for the translation of foreign currency denominated balances in the foreign operation's own financial statements when several exchange rates are available.)

We understand that the second accounting issue is about whether a rate other than an official rate can or should be used for accounting purposes in circumstances when currency conversions are restricted (and therefore in practice none of the official rates are available for immediate delivery).

The submitter also requested guidance on whether the IAS 29 inflation adjustments in the local financial statements can or should be reversed in the consolidated financial statements to better reflect the underlying business performance of the foreign subsidiary. This is primarily an issue if the closing rate for the purposes of IAS 21 does not reflect the local rate of hyperinflation.

Appendix: Exchange rate mechanisms in Venezuela

There are currently the following official exchange rate mechanisms for exchanging VEF:

- CENCOEX (previously CADIVI): The official fixed exchange rate (6.3VEF/ 1US$) is available to specific industries (companies importing essential supplies) in limited quantities. We have been told that remittances at this rate have been small in practice.
- SICAD I: A variable rate auction system created in 2013 is available to entities in specific industry sectors (for non-essential supplies) for a limited volume of VEF. In January 2014 the types of transactions SICAD I could be used for was expanded to include international investment and finance transactions. The average rate achieved in each auction has been published by the Central Bank of Venezuela since December 2013. At 31 March 2014 the SICAD I rate was 10.7 VEF/ 1 US$.

- SICAD II: A regulated variable rate system introduced in March 2014 permits foreign exchange barter transactions in cash and bonds in the private sector with fewer restrictions. The exchange rate has been published daily by the Central Bank. At 31 March 2014 this rate was 50.85 VEF/1 US$. We understand that this mechanism is intended to more closely resemble a market-driven exchange rate; however we have been told that to date there has been limited foreign exchange volumes through SICAD II.

***Q1**: In your jurisdiction(s) are you aware of any entities that have significant foreign operations with a functional currency that is subject to foreign exchange controls (which is often combined with high or hyper inflationary economies)? If so, please give examples that you have seen in practice, briefly explaining the prevalence and circumstances of those cases.*

***Q2**: If you answered 'yes' to Q1, please could you give the following information about each of the examples identified in Q1 above, to the extent you can:*

(a) Do such entities experience similar issues and how do the fact patterns differ from that summarised above?

(b) What is their experience of repatriating local cash from those countries?

(c) If there are several exchange rates available, what exchange rates are used for (i) translating the foreign operation into the group's presentation currency and (ii) translating non-functional currency denominated monetary items in the foreign operation's own financial statements and why? Are you aware of any diversity in practice within or across industries or jurisdictions and why this might be?

(d) Is it common for such groups to use any alternative measures (including non-GAAP measures) to explain their results because of the consequences of applying an official exchange rate that is subject to exchange controls? If so, what are these?

6 Die DRSC-Antwort vom 13. Juni 2014 hierzu lautete wie folgt:

Zu Q1: Yes, we are aware of such foreign operations under the circumstances as described in the submission. To our knowledge, those circumstances are particular for Venezuela and do not appear in other countries in a similar manner.

Zu Q2:

ad a) See our answer to Q1.

ad b)+c) All three official rates are potentially used, subject to particular facts and circumstances. This is the case for (i) as well as for (ii). However, translating non-VEW denominated monetary balances (issue (ii)) is the main issue we observed. Unofficial rates do not appear to be used.

ad d) This translation effect is not substantial compared to the total result. Thus, we do not see need for, and use of, alternative measures for explaining the consequences of this translation.

3.2 Zu IAS 19 – *Remeasurement at a plan amendment or curtailment*

7 Das IFRS IC hatte im Juli 2014 über den Sachverhalt vorläufig entschieden; der Wortlaut der Entscheidung lautet wie folgt (Auszug IFRIC Update 7/2014):

> The IFRS IC received a request to clarify the accounting treatment in accordance with IAS 19 for issues related to the remeasurement of the net defined benefit liability (asset) (hereafter 'net DBL') in the event of a plan amendment or curtailment in IAS 19.
>
> The IFRS IC discussed this issue at its May 2014 meeting. At that meeting it tentatively agreed to develop an amendment to require an entity to:
>
> a. take account of the remeasurement of the net DBL at the event date when determining net interest for the post-event period; and
> b. use the updated actuarial assumptions for the calculation of current service cost and net interest for the post-event period.
>
> The IFRS IC thought that this would result in more relevant information and greater consistency between IAS 19 and paragraph B9 of IAS 34 *Interim Financial Reporting*, if an entity remeasures the net DBL during a period because of a significant event (plan amendment, curtailment or settlement) or a significant market fluctuation.
>
> At this meeting, the IFRS IC reaffirmed that the benefits expected from the proposed amendment are clear: it would provide more relevant information and enhance comparability and understandability. It noted that additional costs resulting from the proposal would not outweigh the expected benefits, because of the existing requirement to remeasure the net DBL in IAS 19 and IAS 34 when significant events or changes occur.
>
> The IFRS IC noted that the proposal would not change how frequently an entity should remeasure the net DBL during a period. The frequency of remeasurement is determined in accordance with the existing guidance such as paragraphs 58 and 99 of IAS 19 and paragraph B9 of IAS 34. This proposal intends to clarify that an entity should determine current service cost and net interest for the remaining portion of the reporting period after a remeasurement, using the updated assumptions and taking account of significant changes in the net DBL.
>
> The IFRS IC noted that the requirement to remeasure the net DBL is determined on a plan-by-plan basis (not a country basis or an overall entity basis). The IFRS IC also noted concerns with the wording in IAS 19.BC58–BC64 and asked that the proposed amendment should address these points.
>
> The IFRS IC concluded that the proposed amendment to IAS 19 meets the criteria for Annual Improvements. It requested the staff to revise its proposed amendment to IAS 19 to clarify the intended requirements and to reflect the points raised during this meeting.

8 Die ursprüngliche Anfrage ging Anfang 2014 beim IFRS IC ein und betrifft die bilanziellen Auswirkungen von Kürzungen oder Änderungen an Pensionsplänen unter IAS 19. Im Februar 2014 hatte das IFRS IC einen *Outreach Request* hierzu gestartet. Dabei wurde der Sachverhalt wie folgt übermittelt und mit folgenden Fragen versehen:

If a significant plan amendment or curtailment of a defined benefit plan occurs should an entity:

- Recognise the remeasurement of the net defined benefit liability (asset) ('net DBL') required for the separate calculation of the amendment or curtailment gain or loss (Issue 1)?
- Revise any actuarial assumptions for the calculation of service cost and interest cost in the post-plan amendment or curtailment period (Issue 2)?

Note: Issue 1 is not an issue whether an entity should recognise the remeasurement gain or loss at end of interim period. Issue 1 would affect a calculation of net interest in the post-curtailment period.

1. Background of the issues

When a plan amendment or curtailment occurs, an entity remeasures the net DBL using the current fair value of plan assets and current actuarial assumptions (including current market interest rates and other current market prices) reflecting the benefits offered under the plan before the plan amendment or curtailment, as the first step in determining the past service cost (IAS 19.99).

The net DBL is therefore determined three times in connection with an event, as follows:

(i) The 'expected amount' of the net DBL before the event, based on actuarial assumptions at the end of the prior year and cash movements.

(ii) The net DBL *before* the event remeasured using: (*) the current fair value of plan assets; and (**) current actuarial assumptions, reflecting the benefits offered under the plan *before* the event.

(iii) The net DBL *after* the event remeasured using: (*) the current fair value of plan assets; and (**) current actuarial assumptions, reflecting the benefits offered under the plan *after* the event.

The difference between the amount of the DBO in (ii) and (iii) is the past service cost (IAS 19.102). The difference between (i) and (ii) does not include any effect of the event. There is a diversity of views and the arguments for and against its recognition are set out below (***Issue 1*****)**.

There is also diversity about whether some or all of the actuarial assumptions which are used in determining current service cost and net interest for the post-event period should be updated to the current actuarial assumptions (including current market interest rates and other current market prices), reflecting the benefits offered under the plan after the event (i.e. those used in measuring the amount of (iii)) (***Issue 2***).

2. The fact pattern

Entity X accounts for its defined benefit plan in accordance with IAS 19 (2011) in its financial statements for the year ending 31 December 2013. Accordingly, on 1 January 2013 X determined the defined benefit cost for 2013. On 20 March 2013, X commits to a restructuring plan that reduces by half the number of employees covered by the defined benefit plan. The restructuring plan meets the criteria in IAS 37 and, as a result, a curtailment loss (past service cost) is recognised on 20 March 2013.

3. Divergent views identified by the submitter:

The submitter observed the diversified views as the table below explains.

Issue 1	Issue 2	Remeasure net DBL on the statement of financial position by recognising total gain/loss?	Update the actuarial assumptions to determine current service cost and net interest?	
			Financial assumptions	Demographic assumptions
View 1	View A	No	No	No
View 1	View C	No	No	Yes
View 2	View A	Yes	No	No
View 2	View B	Yes	Yes	Yes
View 2	View C	Yes	No	Yes

Note: The number of employees for whom current service cost will arise is not a demographic assumption as described in IAS 19.75-98, but instead a matter of fact in each period of service. The number of employees is therefore updated for the post-event period, even if the actuarial assumptions are not updated.

<u>View 1: Net DBL remeasurement is not recognised at curtailment</u>

Under this view, the net DBL is NOT remeasured to the amount of (iii). The difference between the expected net DBL amount of (i) and the remeasured net DBL amount before the event of (ii) is not recognised (in OCI) at the time of the event. The remeasurement is performed solely to exclude the effect of the remeasurement from past service cost. As a result, the carrying amount of the net DBL after the event is the expected amount of (i) less the difference between the amounts of (ii) and (iii), i.e. less the past service cost. The proponents of this view believe that it is most consistent with the IASB's intentions as summarised above described in IAS 19.BC64.

<u>View 2: Net DBL remeasurement is recognised at curtailment</u>

Under this view, the net DBL is remeasured to the amount of (iii). Proponents of View 2 point out that, as highlighted in the first sentence of IAS 19.BC60, remeasurements should be recognised in the period in which they arise. They therefore believe that the remeasurement gain or loss (i.e. the difference between (i) and (ii)) should be recognised (in OCI) when that remeasurement is performed.

<u>View A: No assumptions are updated to determine current service costs and net interest in the post-plan amendment or curtailment period</u>

Under this view the actuarial assumptions are not updated to the current actuarial assumptions for the post-event period. Actuarial assumptions are only updated during the year-end assessment together with remeasuring the net DBL. The proponents of this view believe that it is most consistent with the IASB's intentions as described in IAS 19.BC63 and BC64.

<u>View B: All actuarial assumptions (financial and demographic) are updated to determine current service costs and net interest in the post-plan amendment or curtailment period</u>

Proponents of View B point out that a plan amendment or curtailment may have a significant impact on an actuarial assumption(s), such as the rate of employee turnover. Therefore, not updating actuarial assumptions would result in an inappropriate measurement of current service cost for the remainder of the

reporting period which does not reflect the present situation. Proponents of updating the actuarial assumptions generally also support recognising the remeasurement gain or loss (i.e. View 2 under Issue 1). Supporters of this approach note that IAS 19.BC64 does not form part of the standard itself, which is silent. They also point to IAS 34.IE.B9 which indicates that the actuarially determined pension cost rate calculated at the end of the prior period should be adjusted for significant one-off events, such as plan amendments, curtailments and settlements.

View C: The financial assumptions are not updated but the demographic assumptions are, to determine current service costs and net interest in the post-plan amendment or curtailment period

Only the demographic assumptions, which include the rate employee of turnover, are updated and the financial assumptions remain the same. Proponents of this view believe that IAS 19.80 clearly requires the financial assumptions to be based on market expectations at the end of the [previous] reporting period, but silently implies the demographic assumptions being updated when a plan amendment or curtailment occurs. Supporters of View C also point to IAS 34.IE.B9.

4. Questions

Q1. *In your jurisdictions, are curtailment or plan amendments common? If yes, are you aware of any difficulties or challenges in your jurisdiction to decide;*

- *whether an entity recognises remeasurement gain or loss at a plan amendment or curtailment (Issue1), or/and*
- *whether an entity recognises update assumptions to determine current service costs and net interest in the post-plan amendment or curtailment period (Issue2)?*

Q2. *If 'Yes' to Q1, what is the prevalent interpretation for each issue? In addition, if possible, could you please briefly describe the rationale for that prevalent interpretation/ treatment?*

Q3. *If 'Yes' to Q1, to what extent do you observe diversity in practice in respect of each issue?*

9 Die DRSC-Antwort vom 4. März 2014 hierzu lautete wie folgt:

Zu Q1: Unfortunately, this time we could not ask a very broad variety of constituents (as we are used to do) for input on this request. However, those comments received still cover companies from all sectors and with a wide range in terms of size.

Zu Q2: Issue 1: View 2 is the prevalent approach. Issue 2: View A is the prevalent approach.

Zu Q3: No, we are not aware of diversity in practice.