

STAFF PAPER

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Project	Foreign Currency Translation		
Paper topic	Cover paper		
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Introduction

1. The primary purpose of this set of papers on foreign currency translation is to review work carried out by other national standard setters in this area (notably the Korea Accounting Standards Board (KASB)) to assist the IASB in determining whether it wishes to pursue a longer term project in respect of accounting for foreign currency translations and if so, the scope of such a project.
2. This paper is for information only. It provides some background to the issues, introduces the four related Agenda Papers (8A(a) - 8A(d)) and summarises the staff recommendations in those Agenda Papers.

Background

3. IAS 21 *The Effects of Changes in Foreign Exchange Rates* was originally issued by the International Accounting Standards Committee (IASC) in 1983. It was revised by the IASC in 1993 as a result of the ‘Comparability of Financial Statements’ project, which substantially narrowed the amount of accounting choices available to entities.
4. The IASB adopted IAS 21 in 2001 and made some minor piecemeal revisions to it in 2003 as part of its Improvements to International Accounting Standards project. However the IASB did not reconsider the fundamental approach in IAS 21. A minor amendment was subsequently made to IAS 21 in 2005.

5. In 2011, the KASB formally raised concerns with the IASB that current accounting standards relating to the translation of foreign currency transactions into the functional currency might not reflect the true economic substance. This was with particular reference to times of significant changes in exchange rates due to financial crises. This was, for example, experienced in the 1997 Asian financial crisis and the 2008 global financial crisis.
6. This matter had been raised by the KASB with members of the IASB on earlier occasions, as well as at meetings of the Emerging Economies Group (EEG) and the Asian-Oceanian Standard-Setters Group (AOSSG) which were attended by IASB representatives. It was identified in the 2011 Agenda Consultation Request for Views as one of a broad range of issues that had been brought to the attention of the IASB.¹ At its meeting in May 2012 the IASB added this topic to the list of issues being examined in its Research Programme, with the view to considering the matters raised by the KASB when IASB staff became available.
7. That analysis has now been undertaken and is encapsulated in Agenda Papers 8A(a) – 8A(c).

Agenda Paper 8A(a): Long-term monetary items

8. Agenda Paper 8A(a) explores the KASB's proposal for a narrow-scope amendment to IAS 21 to permit or require an alternative to the closing rate for translating foreign currency long-term monetary items in entity accounts in certain restricted and rare circumstances, such as when there are significant exchange rate fluctuations due to exceptional and temporary external shocks (for example, financial crises).

Agenda Paper 8A(b): Proposal for comprehensive review

9. The KASB also requested that the IASB undertake a more comprehensive review of IAS 21, in particular for translating foreign currency transactions into an entity's functional currency, to clarify the translation objective and methods from a conceptual viewpoint. It prepared a Research Report to provide the foundation for carrying out the basic research for such a review. Some of these ideas were developed further by

¹ See Agenda Papers 8A(a) and 8A(b) for a summary of the response to that Request for Views.

the KASB as part of its response to the Discussion Paper *A Review of the Conceptual Framework*. The two papers prepared by the KASB are considered in Agenda Paper 8A(b).

Agenda Paper 8A(c): Other issues

10. In addition, a few other specific narrow-scope issues relating to IAS 21 have been raised to the IFRS Interpretations Committee (the ‘Interpretations Committee’) in the past, but not taken onto its agenda. These issues together with other narrow-scope, largely practical, issues raised by the KASB and its Working Group, are reviewed in Agenda Paper 8A(c) to determine if any of them should be considered further by the IASB as separate narrow-scope projects.

Agenda Paper 8A(d): The KASB papers

11. Agenda Paper 8A(d) contains copies of the KASB’s proposals and papers referred to above for reference only.

Staff recommendations

12. Some interesting points are made in the KASB’s papers. However for the reasons given in Agenda Papers 8A(a) - 8A(c), the staff recommend that the IASB:
- (a) does not pursue a narrow-scope amendment to IAS 21 to introduce a limited exception to the use of the closing rate for long-term monetary items (Agenda Paper 8A(a));
 - (b) does not undertake a comprehensive review of the conceptual basis for IAS 21, but instead to consider the need for specific narrow-scope or other amendments to IAS 21 as and when the need arises and to monitor the situation as part of future agenda consultations (Agenda Paper 8A(b)); and
 - (c) does not revisit previous issues related to IAS 21 that have been discussed by the Interpretations Committee or pursue any other specific issues identified in the KASB’s Research Report, with the possible exception of:

- (i) the current foreign exchange restrictions and hyperinflation issue in Venezuela, depending on the outcome of the Interpretations Committee’s discussions at its November meeting;
 - (ii) the issue concerning the reclassification of cumulative translation adjustments on the partial disposal of an investment in a foreign subsidiary. The staff recommends that the IASB does not actively pursue this issue as a separate narrow-scope project, but wait until the principles for the use of other comprehensive income in the Conceptual Framework are finalised (Agenda Paper 8A(c)).
13. If the IASB agrees with these staff recommendations, we will remove the Foreign Currency Translation project from the list of active issues on the current Research Programme and thank the KASB formally for providing the IASB with its helpful analysis.

Consequences of removing the project from the Research Programme

14. It is important to emphasise that removing the project from the Research Programme does not mean that the IASB has closed all consideration of IAS 21. On the contrary, doing so ensures that the IFRS Interpretations Committee is able to consider any requests for interpretation on their own merit—without the uncertainty of assessing whether that matter is being considered as part of an active project to replace IAS 21.
15. In a similar manner, the IASB can now also be more open to consider matters brought to its attention that could be addressed through narrow-scope amendments. The recent limited-scope amendment to IAS 41 *Agriculture* for bearer plants is an example where a change was able to be made on a timelier basis than would have been possible if the IASB had set out to replace IAS 41 in a major project.