International Accounting Standard IAS 21

The Effects of Changes in Foreign Exchange Rates

August 2023

ILLUSTRATIVE EXAMPLES

Illustrative Examples accompanying IAS 21 *The Effects of Changes in Foreign Exchange Rates*

Illustrative Examples accompanying IAS 21 have been added. For ease of reading, new text is not underlined.

These examples accompany, but are not part of, IAS 21. They illustrate aspects of IAS 21 but are not intended to provide interpretative guidance.

Introduction

IE1 These examples illustrate how an entity might apply some of the requirements in IAS 21 in hypothetical situations based on the limited facts presented. Although some aspects of the examples might be present in actual fact patterns, fact patterns in the examples are simplified, and an entity would need to evaluate all relevant facts and circumstances when applying IAS 21. The examples do not illustrate all the requirements in IAS 21, nor do they create additional requirements.

Exchangeability

IE2 Examples 1–3 illustrate how an entity assesses whether a currency is exchangeable (Step I as set out in paragraphs 8, 8A–8B and A2–A10). Examples 4–5 illustrate how an entity estimates the spot exchange rate when a currency is not exchangeable (Step II as set out in paragraphs 19A and A11–A17). In all five examples:

(a) Entity X's functional and presentation currency is PC. Entity X prepares consolidated financial statements.

(b) Entity X has a subsidiary, Entity Y, that is a foreign operation. Entity Y's functional currency is LC, the currency of the jurisdiction in which Entity Y operates. The relevant authority administers the exchangeability of LC for other currencies.

Step I: Assessing whether a currency is exchangeable (paragraphs 8, 8A–8B and A2–A10)

Example 1—Time frame

IE3 The relevant authority in Entity Y's jurisdiction makes PC available to entities in exchange for LC only after completion of an administrative process. The authority requires entities wishing to obtain PC to explain how they intend to use PC when submitting a request for PC. In usual circumstances, an entity obtains PC after N days—that is, N days is the time the authority needs, under its administrative process, to perform checks and provide PC.

IE4 Entity X considers N days to be a normal administrative delay applying to a transaction to exchange LC for PC through this exchange mechanism. Subject to the other requirements in paragraphs A2–A10, Entity X considers LC to be exchangeable into PC if Entity X is able to obtain PC within N days of requesting it.

Example 2—Markets or exchange mechanisms

IE5 The relevant authority in Entity Y's jurisdiction is unable to meet demand for PC and temporarily stops making PC available through the exchange mechanism it administers. In the absence of this exchange mechanism, individual resellers settle transactions to exchange LC for PC at an exchange rate that is not set by the authority. These exchange transactions do not create enforceable rights and obligations, and no other markets or exchange mechanisms exist in which a transaction to exchange LC for PC would create such rights and obligations.

IE6 In assessing whether LC is exchangeable into PC, Entity X considers only markets or exchange mechanisms in which a transaction to exchange LC for PC would create enforceable rights and obligations. Entity X concludes that LC is not exchangeable into PC because the exchange transactions with individual resellers do not create enforceable rights and obligations, and no other markets or exchange mechanisms exist in which a transaction to exchange LC for PC would create such rights and obligations.

Example 3—Purpose of obtaining the other currency

IE7 The relevant authority in Entity Y's jurisdiction prevents entities from obtaining PC for purposes other than importing food and medicine.

IE8 In translating the results and financial position of Entity Y, Entity X assesses whether it is able to obtain PC for the purpose of realising its net investment in Entity Y. Because Entity X is prevented from obtaining PC for this purpose, Entity X concludes that LC is not exchangeable into PC. Entity X's ability to obtain PC for the purpose of importing food and medicine is irrelevant to the assessment.

Step II: Estimating the spot exchange rate when a currency is not exchangeable (paragraphs 19A and A11–A16)

Example 4—Using an observable exchange rate for another purpose (paragraphs A11–A14)

Fact pattern

IE9 At 31 December 20X1 the relevant authority in Entity Y's jurisdiction prevents entities from obtaining PC for the purpose of realising a net investment in an entity operating in that jurisdiction. Other than that restriction, entities are able to obtain PC and the LC:PC exchange rate is free-floating. Only one exchange rate applies to transactions for exchanges of LC for PC; it is updated several times a day.

IE10 At the measurement date of 31 December 20X1 Entity X is unable to obtain PC to realise its net investment in Entity Y. Therefore, Entity X concludes that LC is not exchangeable into PC.

Estimating the spot exchange rate

IE11 Because Entity X concludes that LC is not exchangeable into PC, Entity X is required to estimate the spot exchange rate that meets the objective in paragraph 19A.

IE12 Applying paragraphs A11–A14, Entity X considers whether it might use the observable LC:PC exchange rate for the purpose of realising a net investment in an entity. To do so, it assesses whether that observable exchange rate meets the objective in paragraph 19A and considers:

(a) *whether several exchange rates exist*—only one observable exchange rate exists between LC and PC.

(b) *the purpose for which the currency is exchangeable*—Entity X is able to obtain PC for any transaction other than a transaction that would result in the realisation of its net investment in Entity Y.

(c) *the nature of the exchange rate*—the observable exchange rate is free-floating.

(d) *the frequency with which exchange rates are updated*—the observable exchange rate is updated several times a day.

IE13 Considering these factors, Entity X determines that the observable LC:PC exchange rate meets the objective in paragraph 19A. Therefore, Entity X may use that observable exchange rate as the estimated spot exchange rate when it translates the results and financial position of Entity Y.

Example 5—Using the first subsequent exchange rate (paragraphs A11–A12 and A15–A16)

Fact pattern

IE14 At 31 December 20X1 the jurisdiction in which Entity Y operates is subject to hyperinflation. The relevant authority in Entity Y's jurisdiction prevents entities from obtaining PC for the purpose of realising a net investment in an entity operating in that jurisdiction. However, from 30 April 20X2, the authority allows entities to obtain PC for that purpose.

IE15 At the measurement date of 31 December 20X1 Entity X is unable to obtain PC to realise its net investment in Entity Y. Therefore, Entity X concludes that LC is not exchangeable into PC.

Estimating the spot exchange rate

IE16 Because Entity X concludes that LC is not exchangeable into PC, Entity X is required to estimate the spot exchange rate that meets the objective in paragraph 19A.

IE17 Applying paragraphs A11–A12 and A15–A16, Entity X considers whether it might use the first exchange rate at which it is able to obtain the other currency after exchangeability of the currency is restored (first subsequent exchange rate). To do so, it assesses whether that first subsequent exchange rate meets the objective in paragraph 19A and considers:

(a) *the time between the measurement date and the date at which exchangeability is restored*—exchangeability is restored four months after the measurement date.

(b) *inflation rate*—the jurisdiction in which Entity Y operates is subject to hyperinflation.

IE18 Considering these factors, Entity X determines that the first subsequent exchange rate does not reflect the prevailing economic conditions at the measurement date. Therefore, the first subsequent exchange rate does not meet the objective in paragraph 19A for the purpose of realising Entity X's net investment in Entity Y. However, Entity X could adjust that rate, as necessary, to estimate a rate that meets the objective in paragraph 19A for realising its net investment in Entity Y.