

IFRS in Focus

IASB issues Exposure Draft on First-time Adoption of IFRSs after a period of Severe Hyperinflation

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The Bottom Line

- The ED would affect entities preparing IFRS financial statements after a period of severe hyperinflation.
- The ED proposes that when an entity's date of transition to IFRSs is on, or after, the functional currency normalisation date, the entity may elect to measure assets and liabilities at fair value on the date of transition to IFRSs and use that fair value as the deemed cost of those assets and liabilities in the opening IFRS statement of financial position.
- The ED proposes that if an entity elects to measure assets and liabilities at fair value and to use that fair value as the deemed cost in its opening IFRS statement of financial position, the entity's first IFRS financial statements would describe the circumstances of how and why the functional currency became subject to severe hyperinflation and the circumstances that led to those conditions ceasing.
- The comment period ends on 30 November 2010.

The proposals

On 30 September 2010, the International Accounting Standards Board (IASB) published an exposure draft, ED/2010/12 *Severe Hyperinflation*, which sets out proposed guidance on how an entity should resume presenting IFRS-compliant financial statements after a period in which it was unable to comply with IFRSs because it had a functional currency that was subject to severe hyperinflation.

The ED is intended to apply in the following circumstances:

- An entity is unable to prepare IFRS-compliant financial statements because it operates in a severe hyperinflationary economy.
- During the severe hyperinflation, there is neither a reliable general price index nor a functional currency that can be exchanged into a relatively stable currency.
- Subsequently, the functional currency of the entity changes to another currency or the conditions that led to the functional currency being subject to severe hyperinflation cease (referred to as "normalisation").

In the above circumstances, the entity would meet the criteria to be a first-time adopter when it is able to present IFRS-compliant financial statements even if the entity had applied IFRSs prior to the period of severe hyperinflation.

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The ED proposes to add an exemption to IFRS 1 *First-time Adoption of International Reporting Standards* such that when an entity's date of transition to IFRSs is on, or after, the functional currency normalisation date, the entity may elect to measure assets and liabilities at fair value on the date of transition to IFRSs and use that fair value as the deemed cost of those assets and liabilities in the opening IFRS statement of financial position.

Any adjustments arising from this election are accounted for in accordance with paragraph 11 of IFRS 1, and the entity should recognise those adjustments directly in retained earnings (or, if appropriate, in another category of equity) at the date of transition to IFRSs.

An entity that elects to measure assets and liabilities at fair value and to use that fair value as the deemed cost in its opening IFRS statement of financial position subsequent to currency normalisation would be required to disclose in its first IFRS financial statements an explanation of how, and why, the entity had, and then ceased to have, a functional currency that was subject to severe hyperinflation.

With respect to comparative information, the IASB noted that entities should consider whether the disclosure of non-IFRS comparative information in accordance with IFRS 1 paragraph 22 would provide more useful information to users of the financial statements.

Observation

The ED addresses very narrow circumstances in which reliable measurement in accordance with IFRSs is not possible as a result of severe hyperinflation. Accounting by parents, investors and venturers for their investments in entities that are subject to severe hyperinflation is not addressed.

Effective date

The ED comment period ends on 30 November 2010. The ED does not specify an effective date; however, earlier application would be permitted.

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