



# IFRS Notes

**IFRIC 22 clarifies the  
transaction date to  
determine the exchange  
rate**

21 December 2016

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## Introduction

On 8 December 2016, the IFRS Interpretations Committee of the International Accounting Standards Board (IASB) issued IFRS Interpretation, IFRIC 22, *Foreign Currency Transactions and Advance Consideration* (the Interpretation) which clarifies the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income, when an entity has received or paid advance consideration in a foreign currency.

## Background

Paragraph 21 of International Accounting Standard (IAS) 21, *The Effects of Changes in Foreign Exchange Rates* requires an entity to record a foreign currency transaction, on initial recognition in its functional currency, by applying to the foreign currency amount, the spot exchange rate between the functional currency and the foreign currency at the date of the transaction. The date of the transaction is the date on which the transaction first qualifies for recognition in accordance with International Financial Reporting Standards (IFRS).

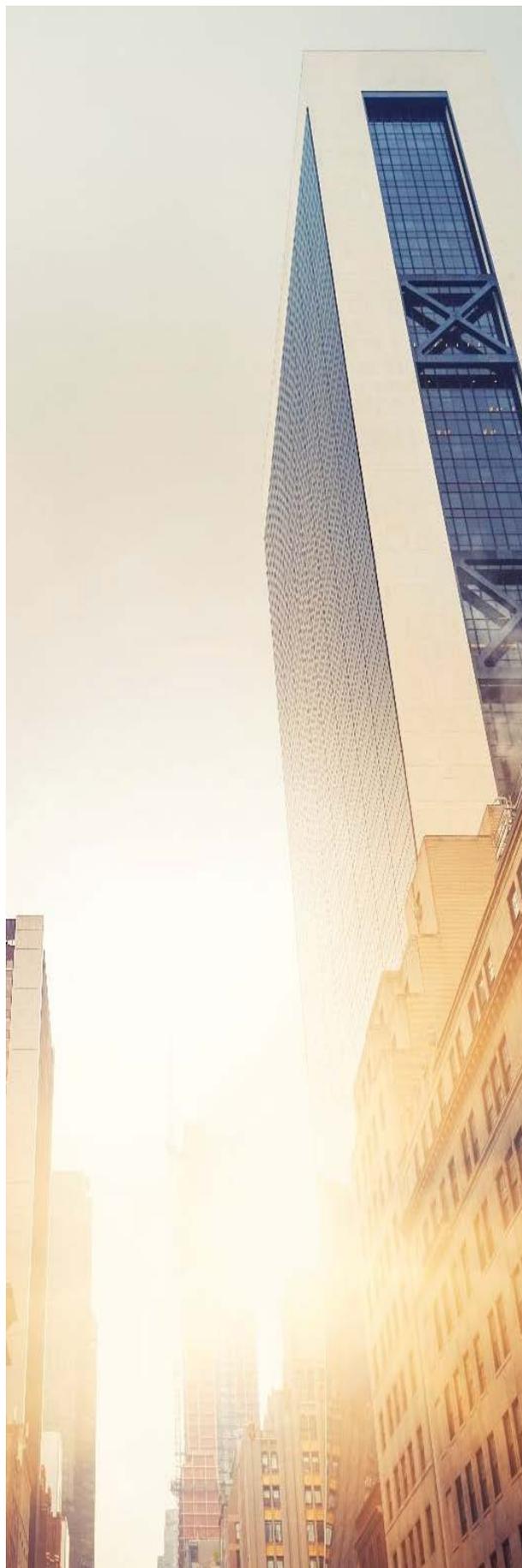
However, there are circumstances when an entity pays or receives consideration in advance in a foreign currency. This gives rise to a non-monetary asset or non-monetary liability before recognition of the related asset, expense or income.

The related asset, expense or income (or part of it) is the amount recognised by applying relevant IFRS, resulting in the derecognition of the non-monetary asset or non-monetary liability arising from the advance consideration.

The Interpretations Committee considered how to determine the exchange rate to be used in applying IAS 21, specifically when an entity receives advance consideration in a foreign currency. IAS 21 does not address such a circumstance. Consequently, the Interpretations Committee issued a draft Interpretation '*Foreign Currency Transactions and Advance Considerations*' on 21 October 2015.

Based on the comments received by the Interpretations Committee, recently, IASB issued IFRIC 22 and clarified the date to be used for translation when a foreign currency transaction involves an advance payment or receipt.

This issue of IFRS Notes provides an overview of IFRIC 22.



## Key highlights of IFRIC 22

### Date of transaction

As per IFRIC 22, 'the date of transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.'

In case there are multiple payments or receipts in advance, the entity should determine a date of the transaction for each payment or receipt of advance consideration.

The interpretation can be understood with the help of the example below:

On 1 March 2018, entity A enters into a contract with a supplier B to purchase a machine for business use. Entity A pays the supplier a fixed purchase price of USD1,000 on 1 April 2018 and takes the delivery of the machine on 15 April 2018.

Entity A would recognise a non-monetary asset translating USD1,000 into its functional currency at the spot exchange rate between the functional currency and the foreign currency on 1 April 2018. Therefore, on applying the provisions of IAS 21, entity A does not update the translated amount of that non-monetary asset.

Further, on 15 April 2018 i.e. on receipt of machine, the entity A would derecognise the non-monetary asset and recognise the machine as property, plant and equipment in accordance with IAS 16, *Property, Plant and Equipment* at the same exchange rate used at the date of initial recognition of the non-monetary asset (i.e. exchange rate as at 1 April 2018).

### Scope

#### Inclusion

IFRIC 22 applies to a foreign currency transaction (or part of it), when an entity recognises a non-monetary asset or non-monetary liability arising from payment or receipt of advance consideration before the entity recognises the related asset, expense or income (or part of it).

#### Exclusion

IFRIC 22 does not apply when an entity measures the related asset, expense or income on initial recognition at:

- a) fair value or
- b) the fair value of the consideration paid or received at a date other than the date of initial recognition of the non-monetary asset or

non-monetary liability arising from advance consideration (for example, the measurement of goodwill applying IFRS 3, *Business Combinations*).

Further, IFRIC 22 does not apply to the following:

- a) insurance contracts (including reinsurance contracts) that an entity issues or reinsurance contracts that it holds and
- b) income taxes.

### Effective date

IFRIC 22 is applicable for annual periods beginning on or after 1 January 2018. Early application is permitted.

If an entity applies the Interpretation for an earlier period, disclosure of the fact is required.

### Transitional provisions

An entity could apply IFRIC 22 initially either:

- a) **retrospectively** applying IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors* or
- b) **prospectively** to all assets, expenses and income in the scope of the Interpretation initially recognised on or after:
  - i. the beginning of the reporting period in which an entity first applies the Interpretation or
  - ii. the beginning of a prior reporting period presented as comparative information in the financial statements of the reporting period in which an entity first applies the Interpretation.

On **prospective** application of IFRIC 22, an entity should apply the Interpretation to assets, expenses and income initially recognised on or after the beginning of the reporting period (as given in (i) or (ii) above) for which non-monetary assets or non-monetary liabilities (arising from advance consideration) have been recognised before that date.

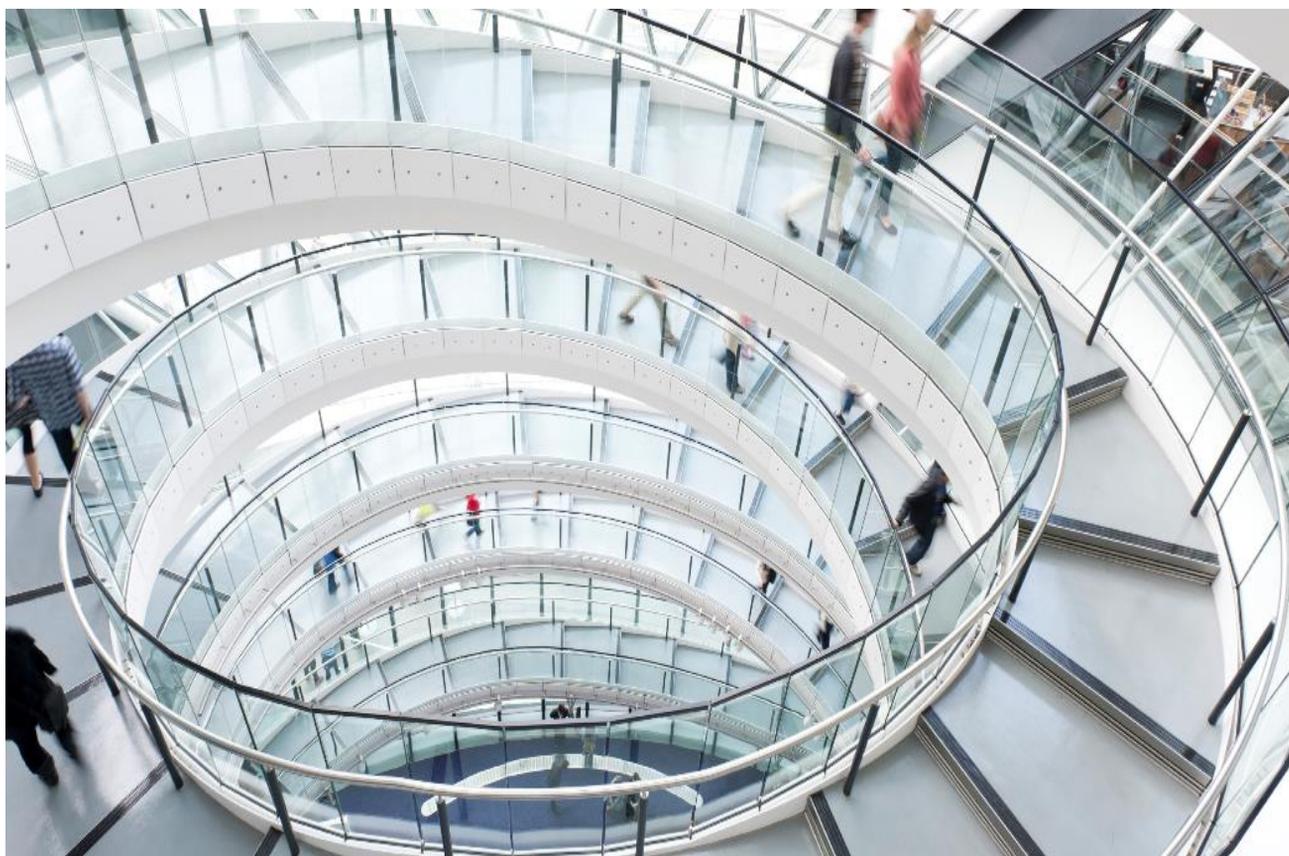
## Our comments

IFRIC 22 provides key guidance as to the exchange rate to be used when reporting revenue in circumstances in which the customer makes a foreign-currency payment in advance. However, it still does not explain what exchange rate(s) should be used to identify and report a significant financing component (nor the revenue related to that component) to be separately recognised once IFRS 15, *Revenue from contracts with customers* becomes applicable. Additionally, the Interpretation is expected to have potential impact in the following areas:

- **Statement of profit and loss:** There could be a significant impact on the statement of profit and loss for companies that currently translate acquired assets at the spot rate prevailing on a date after consideration is paid, e.g. the delivery date.

With respect to revenue and expense transactions, there would not be any effect in aggregate, but amounts reported within individual line items may get affected.

- **Changes in accounting systems:** Affected entities may be required to update their accounting systems in order to report their foreign currency transactions in accordance with the provisions of IFRIC 22.
- **Cash and non-cash foreign currency transactions:** The Basis for Conclusions on IFRIC 22 point out that the interpretation is applicable to both cash and non-cash foreign currency transactions. For example, non-cash consideration received by an entity, such as equity instruments or an item of inventory, that has a fair value determined in a foreign currency, in exchange for the provision of services is also within the scope of the interpretation.
- **Relevance to companies transitioning to Ind AS:** We expect this interpretation issued by the IASB to be incorporated as an amendment to the Indian Accounting Standards (Ind AS) within the next year. Accordingly, we encourage companies in India that are transitioning to Ind AS to apply this interpretation in developing their Ind AS accounting policies in the year of transition. Paragraph 12 of Ind AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors* permits entities to consider the most recent pronouncements of the IASB when selecting their Ind AS accounting policies to the extent that these do not conflict with the requirements in Ind AS. Therefore, Indian companies may consider earlier application of this interpretation. This would enable companies to avoid changes in accounting policies when the interpretation is formally introduced within Ind AS.



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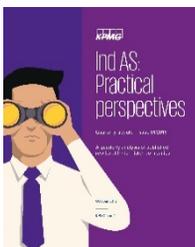
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The website provides information and resources to help board and audit committee members, executives, management, stakeholders and government representatives gain insight and access to thought leadership publications that are based on the evolving global financial reporting framework.

## Ind AS - Practical perspectives



**KPMG in India's Ind AS - Practical perspectives through aims to put a finger on the pulse of India Inc's adoption of Ind AS and capture emerging trends and practices.**

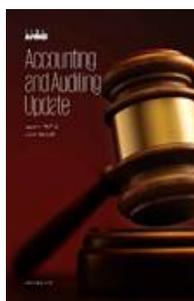
Our impact assessment is based on Nifty 50 companies which would be the first group of companies to report Ind AS

results. The Nifty 50 companies have started reporting their financial results for the quarter ended 30 September 2016.

Out of the companies comprising Nifty 50 index, eight companies are banks, one is Non-Banking Financial Company (NBFC) and two companies follow a different date of transition to Ind AS. Therefore, our analysis would comprise the remaining 39 companies.

This can be accessed on KPMG in India website - ['Ind AS- Practical perspectives' webpage](#)

## Missed an issue of our Accounting and Auditing Update or First Notes



### Issue no. 5/2016 – December 2016

This month the Accounting and Auditing Update focusses on the recent updates from the regulators in India and emerging new trends in the field of accounting and auditing. This edition includes a detailed analysis on the recent notified sections of the Companies Act, 2013 relating to restructuring, amalgamation and winding-up of companies. The notification of these sections was much awaited and our article discusses the key provisions of the recently notified sections along with our comments.

This publication also carries an article on revised guidance note on reports or certificates for special purposes issued by the Institute of Chartered Accountants of India. The article provides an overview of the key elements of the guidance note and highlights additional considerations for management of entities and practitioners.

Ind AS 110, *Consolidated Financial Statements* provides wider definition of control in comparison to Accounting Standards. The revised definition is expected to impact the current structures and give rise to certain practical issues while preparing consolidated financial statements. Our article highlights some of these issues and explains the accounting under Ind AS with the help of examples.

Additionally, this publication carries an article on low-interest and interest-free loans under Ind AS 109, *Financial Instruments*. The article on this topic explains the accounting with the help of illustrative examples and a detailed flowchart. Our publication also carries a regular synopsis of regulatory updates.



### Provisions relating to merger, amalgamation and winding-up, etc. are notified under the Companies Act, 2013

#### 12 December 2016

On 7 December 2016, the Ministry of Corporate Affairs (MCA) issued a notification, whereby certain sections of the Companies Act, 2013 (2013 Act) were notified to come into force. These sections amongst others, relate to:

- reduction of capital and variations of shareholders' right;
- compromises, arrangements and amalgamations.

In addition to the above, certain winding-up sections were also notified by MCA. The notification states that the aforementioned sections would come into force on 15 December 2016.

MCA has also on 7 December 2016 notified the Companies (Transfer of Pending Proceedings), Rules 2016 (Transfer Rules) and also issued the Companies (Removal of Difficulties) Fourth Order, 2016 (Difficulties Order) to facilitate a smooth transition of the proceedings initiated under the Companies Act, 1956 (1956 Act) and pending before any district court or high courts to the National Company Law Tribunal (NCLT).

This issue of First Notes aims to provide an overview of these notifications.

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