



**INTERNATIONAL FEDERATION
OF ACCOUNTANTS**

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Agenda Item

4

DATE: February 11, 2008
MEMO TO: Members of the IPSASB
FROM: Matthew Bohun-Aponte
SUBJECT: ED 33, Proposed Changes to IPSAS 4, The Effects of Changes in Foreign Exchange Rates

OBJECTIVE OF THIS SESSION

To **approve** the amended IPSAS 4, “The Effects of Changes in Foreign Exchange Rates.”

AGENDA MATERIAL:

Papers

- 4.1 Analysis of responses to ED 33;
- 4.2 Responses to ED 33; and
- 4.3 Draft IPSAS 4, “The Effects of Changes in Foreign Exchange Rates.”

ACTION REQUIRED

The IPSASB is asked to:

- **review** the analysis in this memo and the attached analysis of responses;
- **review** the attached draft IPSAS 4; and
- **approve** the IPSAS for publication.

BACKGROUND

After its meeting in July 2007, the IPSASB approved ED 33, “Proposed Amendments to IPSAS 4, The Effects of Changes in Foreign Exchange Rates”. The amendments were proposed to converge IPSAS 4 with IAS 21, “The Effects of Changes in Foreign Exchange Rates” which had been amended by the IASB in December 2005. ED 33 was published on the IFAC website in August 2007 with a request for comments to be submitted by December 31, 2007. The amendments proposed to IPSAS 4 are not wide ranging and relate to the translation of a net investment in a foreign operation.

To date four responses have been received on ED 33. This is a particularly low level of response. Staff have followed up with members, technical advisors and regular respondents to determine if any responses have failed to reach the IPSASB’s e-mail center. At the date of this memorandum, Staff have identified three responses that were not recorded in the IPSASB e-mail center. These responses have been incorporated in the analysis and Staff is working with New York-based IFAC colleagues to ascertain

whether there might be other unrecorded responses. Any such responses will be distributed electronically or tabled at the Toronto Meeting.

Notwithstanding the above, the follow up indicates that constituents thought that the amendments were minimal, and that they did not cause concern to constituents who generally elected not to respond. Staff also note that when a constituent e-mails a response, they frequently send a paper copy via regular mail as well; we have received no responses via regular mail either.

In analyzing the responses to ED 33 and developing the attached draft IPSAS, staff have focused on the “Guidelines for Modifying IASB Documents” established by the IPSASB at recent meetings. In particular, staff were trying to determine whether the issues raised by the respondents raised public sector specific issues that warrant a departure from the IAS.

ANALYSIS

Overall

The respondents to ED 33 support the issuing of the amended IPSAS 4. They also responded positively to the specific matter for comment on whether the changes made to IAS 21 are appropriate for the public sector and should be reflected in IPSAS 4.

Step One: Are there any public sector issues that warrant departure?

The respondents raised several issues which they argued were public sector specific. For example respondent 3 argues that selection of the presentation currency may be limited by legislation in the public sector. Staff are of the view that this is not only an issue in the public sector, and governments can prescribe the presentation currency for any entity that is required to publish financial statements.

Respondent 1 raised issues relating to determining whether or not an entity is a controlled entity. In staff’s view these issues are not specific to the public sector, and cannot be addressed as part of this project. They would need to be considered in any review of IPSAS 6, “Consolidated and Separate Financial Statements.”

Respondent 3 raised issues regarding the use of terminology such as “significant” which he argues is not clear. Respondent 3 also suggested that commentary might be clarified in certain places (for example, paragraphs 44 and 50). Whilst staff acknowledge that the some terms are not explained in great detail in the IPSAS (for example, paragraphs 55 and 63), these terms and commentary mirror IAS 21. Staff are of the view that such terminology issues need to be addressed as part of the Conceptual Framework project, rather than during the updating of an IPSAS.

Staff have provided responses to the arguments presented by the respondents in attachment 5.2. Staff are of the view that none of the issues that the respondents raised are specific to the public sector, or require that the draft IPSAS needs to be modified in light of these responses.

Step Two: Are the departures so significant that a public sector specific project should be initiated?

Staff are not proposing any departures.

Step Three: Modify IASB Documents

Staff have provided a draft IPSAS 4, “The Effects of Changes in Foreign Exchange Rates” as attachment 5.3. This document modifies IAS 21 for the language used in the IPSASs. The draft IPSAS also has the definitions in alphabetical order and explanatory material relating to the definitions follows this order. Definitions in IAS 21 are not in strict alphabetical order.

Step Four: Issue IPSAS converged (to varying degrees) with IASB Documents

Staff recommend that the IPSASB approve the draft IPSAS 4, attached at item 5.3 for issue to replace IPSAS 4, issued in 2000 and revised in 2006.

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| ACTION: Review the attached analysis, responses and draft IPSAS, approve the IPSAS for issue. |
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**Matthew Bohun-Aponte
TECHNICAL MANAGER**

ATTACHMENT 1 – SUMMARY OF RESPONDENTS' VIEWS ON ED 33
AMENDMENTS TO IPSAS 4, "THE EFFECTS OF CHANGES IN FOREIGN
EXCHANGE RATES"

SUMMARY OF OVERALL VIEW

| | | |
|------------------|---|---|
| SUPPORT | A | 4 |
| DOES NOT SUPPORT | B | 0 |
| NO CLEAR VIEW | C | 0 |
| TOTAL | | 4 |

| | NAME | VIEW | RESPONDENT COMMENT |
|---|---|------|--|
| 1 | Joseph Maresca | A | Respondent supports the issuance of the standard; however, he feels that more guidance is needed in relation to the selection of presentation currency, determining the existence of hyperinflation, and whether control exists. |
| 2 | Pricewaterhouse Coopers Ghana | A | PwC Ghana supports the changes proposed, in particular the changes noted in the Summary of Main Changes. |
| 3 | Perry Pahladsingh | A | More guidance is needed on the nature of the reporting entity and the economic entity. |
| 4 | Chartered Institute for Public Finance and Accountancy | A | |

SPECIFIC MATTER FOR COMMENT

Do you agree that the changes made to the equivalent IAS 21 in December 2005 are appropriate for the public sector and therefore should be reflected in IPSAS 4 as proposed?

| | | |
|-------------------------|---|----------|
| Agree | A | 4 |
| Disagree | B | 0 |
| No clear view expressed | C | 0 |
| TOTAL | | 4 |

| | NAME | VIEW | RESPONDENT COMMENT |
|---|-------------------|-------------|---------------------------|
| 1 | Joseph Maresca | A | |
| 2 | PwC Ghana | A | |
| 3 | Perry Pahladsingh | A | |
| 4 | CIPFA | A | |

OTHER COMMENTS

1 – Joseph Maresca

Implementation of this amendment will involve judgments on very complex issues; such as, hyperinflation and the "Presentation Currency". P. 22/ 43 onward could be clarified by requiring a footnote to explain the rationale for selecting the Presentation Currency. This will provide better information for readers of the financial statements.

In addition, IN 5 should provide further discussion on the meaning and application of a “controlled entity.” For instance, a controlled entity is determinable by reference to a controlling financial interest. A corporate ownership (direct or indirect) of > 50% of an affiliate's voting common stock is a strong indicator of control.

Other circumstances can negate parental control as in bankruptcy, court supervised reorganization or host country expropriation. A foreign subsidiary in a country having significant production or tax restrictions may in reality be subject to the authority of the host country rather than the parent or controlling interest.

Also, a corporation owning less than 50% of another's voting common stock may control the affiliate effectively if the remaining stock is widely dispersed among individual shareholders who do not attend shareholder meetings or vote by proxy. Effective control of an investee is possible if management of the investor company owns a substantial number of shares of the investee or solicits proxies from strategic shareholders.

Staff Response: Paragraph 62 requires entities which select a presentation currency that is different from the functional currency to disclose that fact, together with the disclosure of the functional currency and the rationale for using a different presentation currency. Selection of the functional currency or presentation currency does not seem to staff to be more complex or onerous for public sector entities than for other entities, therefore staff cannot discern a public sector reason for any additional requirements or guidance.

IPSAS 6, “Consolidated and Separate Financial Statements” provides guidance on determining whether and in what circumstances an entity is controlled. Staff do not think that there is a public sector reason for providing additional guidance in this IPSAS.

2 – PwC Ghana

No additional comments.

3 – Perry Pahladsingh

The use of adjectives like ‘significant’ should be clearly explained. I refer for example to par. 55 (significant changes) and par. 63 (significant foreign operations). Alternatively, you may consider using the materiality concept, as laid-out in IPSAS1. I therefore would recommend the following introduction. International Public Sector Standard 4, “The Effects of Changes in Foreign Exchange Rates” (IPSAS 4) is set out in paragraphs 1 - 73. All the paragraphs have equal authority. IPSAS 4 should be read in the context of the Basis for Conclusion (if any), and the “Preface to International Public Sector Accounting Standards.” IPSAS 4, “Accounting Policies, Changes in Accounting Estimates and Errors” provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Staff response: The rubric and the use of the term “significant” are consistent with IAS 21, and the respondent has not presented a public sector specific rationale for varying from the IAS. Usage of particular terms is a matter to be raised in the context of the Conceptual Framework project.

- a. In par. 11 – 14 of the proposed amendments to IPSAS4, the factors are mentioned to be considered for an entity to determine its functional currency. When determining the functional currency in the public sector, one additional factor may be national jurisdictional or legislative requirements to record accounts in the currency of the domicile of the other entity, i.e. the foreign operation, or the reporting entity. Then, by law or regulations, the functional currency shall be determined, irrespective or despite the factors mentioned in par. 11 – 12.

A more complicating situation to the example of par. 13 (a) may be when the activities of the foreign operation are carried out as an extension of the reporting entity (rather than being carried out with a significant degree of autonomy) under the supervision or command of an entity which uses another functional currency. This could be under the supervision or command of e.g. a supranational or

international public sector entity. This may lead to an additional factor to be considered in determining the functional currency.

In par. 14 a hierarchy has been made clear between the determining factors in par. 11 (primary factors) and par. 12 and 13 (secondary factors). However, one may have the impression that par. 11 and 12 refer to an entity, where as par. 13 refers to a foreign operation. Some further clarification would be appreciated.

- b. In par. 16 the last sentence is not very clear in its meaning and purpose, e.g. which standard is meant with 'this Standard'. I would advise some rephrasing to make more clear the purpose of par. 10.
- c. In par. 21 the summary of the approach required by IPSAS4 has been detailed. The following may be unclear: 'This Standard permits the presentation currency of a reporting entity to be any currency (or currencies). The financial performance and financial position of any individual entity within the reporting entity whose functional currency differs from the presentation currency are translated in accordance with paragraph 43-59.' One would have thought this would be applicable to an associate, joint venture, branch or controlled entity as defined in a foreign operation. However, when reading the quoted text, one may get the impression that this would be applicable to all entities, even beyond a foreign operation. The phrase 'any individual entity within the reporting entity' should considered to be rephrased to more specifically focus on a foreign operation, as may be the actual approach referred to. Again this also refers to my initial comment on the definition of an entity.
- d. In par. 22 IPSAS4 allows a stand-alone entity, preparing its financial statements or an entity preparing separate financial statements in accordance with IPSAS6: Consolidated and Separate Financial Statements, to present its financial statements in any currency (or currencies). The phrase '.. in any currency (or currencies).', is unclear. It could give the impression an entity can use more than one currency as its presentation currency, which would not be very obvious. Therefore, rephrasing of par. 22 would be advisable.
- e. Par. 25 states that the date of a transaction is 'the date on which the transaction first qualifies for recognition in accordance with International Public Sector Accounting Standards.' This is not further detailed. In case of a foreign loan the date of the transaction could be the date of the agreement. In case of services delivered or goods received, the date of the transaction may not be that straightforward. This may be complicated if goods are returned and services or goods are delivered in instalments.
- f. In par. 39 reference has been made to the situation in which an entity keeps its books and records in a currency other than its functional currency. When the entity prepares its financial statements all amounts must be translated into the functional currency, according to the proposed amendments to IPSAS 4. This

could imply that a foreign operation would have to prepare its financial statements in a functional currency, even when it has to keep its accounts in the currency as determined by law or regulations and therefore not relevant for the reporting entity (who may use another presentation currency). The added value in this situation to have prepared by the foreign operation financial statements in a functional currency, other than the currency used to keep its books and records, is unclear. More clarification to prepare the general purpose financial statements and the users' needs in this respect is therefore important.

- g. Par. 43 refers to a 'common currency'. More clarification of a 'common currency' in connection with the presentation currency would be appreciated.
- h. In par. 44 reference has been made to 'a different presentation currency'. One would assume this is meant to refer to 'the presentation currency'.
- i. Par. 50 refers to the translation of a foreign operation. I would like to give for your consideration to rephrase the paragraph to make it more straightforward: translation should be undertaken in the presentation currency of the reporting entity.
- j. Par. 54 refers to the situation in which there is a difference between the reporting date of the reporting entity and the foreign operation, then the assets and liabilities of the foreign operation should be translated at the exchange rate at the reporting date of the foreign operation. One would however expect the translation to be undertaken at the date of the reporting entity. Therefore clarification of this suggested approach is highly recommended.
- k. In par. 55 adjustments are limited to significant changes in exchange rates up to the reporting date of the reporting entity in accordance with IPSAS6. Please note that transactions concerning huge amounts affected by not significant changes exchange rates may have a material effect on the financial performance and financial position. I therefore would suggest to refer to the concept of materiality, as has been detailed in IPSAS1.
- l. Please note that bequest may also be an example of disposal of a foreign operation, as referred to in par. 58.

Staff Response: Staff are unaware of any situation in which an asset of a public sector entity could be disposed of as a bequest.

- m. In par. 63 reference has been made to a 'significant foreign operation'. Could you indicate what is meant by 'a significant foreign operation', and how this distinguishes between other foreign operations ?
- n. In par. 66 the situation has been laid out in which an entity displays its financial statements or other financial information in a currency that is different from either

its functional currency or its presentation currency. It should be made more clear that this information is supplementary to the financial statements as complying with IPSAS, and therefore I would suggest that this cannot concern the financial statements of the entity under IPSAS.

Staff Response: In paragraphs a – k, m and n, Dr. Pahladsingh raises interesting points regarding the interpretation of IPSAS 4, which apply equally to IAS 21. Staff cannot identify any public sector specific issues in these paragraphs that require an amendment to the proposed IPSASs. The points raised by Dr. Pahladsingh apply equally to private sector entities as to public sector entities. In line with the IPSASB's "Guidelines for the Modification of IASB Documents" staff do not recommend any changes to IPSAS 4 as a result of these comments.

4 – Chartered Institute for Public Finance and Accountancy.

No additional Comments.

Matthew Bohun-Aponte

From: Joseph S. Maresca [Joemath@Mindspring.com]
Sent: Friday, November 30, 2007 10:05 AM
To: Joseph S. Maresca; edcomments
Subject: Re: Commentary on Draft 33- Amendment IPSAS #4 due 12-30-07

----- **From:** [Joseph S. Maresca](#) **Dr. Joseph S. Maresca**

To: Edcomments@ifac.org

Sent: Friday 11-30-07

Subject: Re: Commentary on IPSAS #4 (Draft 33)

GENERALLY, there is agreement with the issuance except for the comments provided.

Implementation of this amendment will involve judgments on very complex issues; such as, hyperinflation and the "Presentation Currency". P. 22/ 43 onward could be clarified by requiring a footnote to explain the rationale for selecting the Presentation Currency. This will provide better information for readers of the financial statements.

In addition, IN 5 should provide further discussion on the meaning and application of a **controlled entity**. For instance, a controlled entity is determinable by reference to a controlling financial interest. A corporate ownership (direct or indirect) of > 50% of an affiliate's voting common stock is a strong indicator of control.

Other circumstances can negate parental control as in bankruptcy, court supervised reorganization or host country expropriation. A foreign subsidiary in a country having significant production or tax restrictions may in reality be subject to the authority of the host country rather than the parent or controlling interest.

Also, a corporation owning less than 50% of another's voting common stock may control the affiliate effectively if the remaining stock is widely dispersed among individual shareholders who do not attend shareholder meetings or vote by proxy. Effective control of an investee is possible if management of the investor company owns a substantial number of shares of the investee or solicits proxies from strategic shareholders.

Dr. Joseph S. Maresca

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The Technical Director
International Public Sector Accounting Standards Board
277 Wellington Street, 4th Floor
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20 December 2007

Exposure draft 33 - Amendments to IPSAS 4, "The Effects of Changes in Foreign Exchange Rates"

Dear Sir,

Thank you for the opportunity to respond to the International Public Sector Accounting Standards Board's (IPSASB) Exposure Draft 33: "The Effects of Changes in Foreign Exchange Rates"

PricewaterhouseCoopers Ghana is committed to the Board's agenda to produce high quality standards for the Public Sector.

We broadly agree with the amendments proposed by the IPSASB as a result of the IASB's revision of IAS 21. They are appropriate for the public sector and therefore should be reflected in IPSAS 4 as proposed.

Governments and Public sector institutions are currently investing in several organizations across continents where translation differences represents a material component of the financial statements produced by their foreign subsidiaries.

Please find attached a detailed response to your specific matter for comment.

Should you require any comments or questions which needs further clarification, please contact me on email: charles.a.egan@gh.pwc.com.

Yours sincerely,

For: PricewaterhouseCoopers (Gh) Ltd



Charles Egan
Country leader

SPECIFIC AREAS FOR COMMENTS

Net Investment in a Foreign Operation

☐ To clarify in paragraph 19 that an entity that has a monetary item, which is, in substance, a part of the entity's net investment in a foreign operation, may be any controlled entity of the economic entity. An example is also provided to illustrate this clarification. Previously, IPSAS 4 did not make this clear.

We agree with this clarification and the example makes it even clearer.

Recognition of Exchange Differences

☐ To require in paragraph 38 that exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation are recognized initially in a separate component of net assets/equity in the financial statements that include the foreign operation and the reporting entity, irrespective of whether the monetary item is denominated in the functional currency of the reporting entity, or in the functional currency of the foreign operation, or in a currency other than the functional currency of either the reporting entity or the foreign operation. Previously, IPSAS 4 required such exchange differences to be recognized in surplus or deficit in the financial statements including the foreign operation and the reporting entity when the monetary item is denominated in a currency other than the functional currency of either the reporting entity or the foreign operation

The revision is appropriate and provides a fair presentation to both shareholders and other users of financial statements of Public sector organizations. In addition, the amendments to IPSAS 4 based on the IASB's revision of IAS 21 would enhance financial reporting in public sector organizations with net investment in several foreign operations. Previously the initial recognition of exchange differences in the income statement of the reporting entity could be seen as misleading to shareholders and other users of financial information of the reporting entity. We therefore agree with this amendment.

Other Changes

☐ To amend the Introduction and the Basis for Conclusions as a result of the amendments to this Standard.

☐ To make minor editorial changes to improve the style or the consistency with other IPSASs.

No comment.

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International Public Sector Accounting Standards Board (IPSASB)
International Federation of Accountants
To the attention of the Technical Director
Ms. S. Fox
277 Wellington Street
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Ontario M5V 3H2
Canada
Via email: publicsectorpubs@ifac.org

December 31, 2007

Subject : Proposed Amendments to IPSAS 4: The Effects of Changes in Foreign
Exchange Rates

Dear Ms Fox,

Thank you for giving me the opportunity to comment on proposed amendments to IPSAS 4: The Effects of Changes in Foreign Exchange Rates. I highly welcome the proposed amendments to the current International Public Sector Accounting Standard 4, as this will bring it in line with the concurring International Accounting Standard 21: The Effects of Changes in Foreign Exchange Rates.

Please find attached my detailed comments. After an introduction I will raise some overriding issues and give my detailed views on the proposed amendments; I will conclude my views with addressing the specific matter for comment.

I trust you find the attached comments useful. I am willing to give my ongoing support for further development of accounting principles, by commenting on future Consultation Papers and Exposure Drafts.

If you need any information regarding my comments please feel free to contact me.
May 2008 be a very successful year for you.

Yours truly,

Perry Pahladsingh

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1 Introduction

I am pleased to have the opportunity to comment on proposed amendments to the International Public Sector Accounting Standard 4: The Effects of Changes in Foreign Exchange Rates. I support the suggested views in the amendments regarding accounting and disclosure to bring it in line with the concurring International Accounting Standard 21: The Effects of Changes in Foreign Exchange Rates (published as Net Investment in a Foreign Operation), issued by the International Accounting Standards Board in December 2005. The objective of the IASB's amendment to IAS21 was in response to concerns raised by constituents about the requirements in previous IAS21 for dealing with exchange differences arising on a monetary item that forms part of the reporting entity's net investments in a foreign operation.

I truly believe that disclosure of information and measurement (only if feasible at reasonable cost) regarding the effects of changes in foreign exchange rates in financial statements is key to determine whether the financial statements present a 'true and fair view' of an entity in the Public Sector. Including information on the effects of changes in foreign exchange rates assures general purposes financial statements to adequately describe an entity's financial performance and use of financial resources.

2 Overriding issues

When studying the amendments to IPSAS4 the issue of the entity-concept comes forward. In connection with the entity, a foreign operation is defined in IPSAS4 as 'an entity that is a controlled entity, associate, joint venture or branch of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity'. The fact that neither in IPSAS1 nor in the Preface to the IPSAS an entity has been defined or explained, makes it difficult to distinguish with a foreign operation. This is especially apparent if part of the reporting entity's activities are undertaken in another jurisdiction than the domicile of that entity.

Also, a definition of the entity is key in further aligning reporting requirements through financial statements of entities and operations in the public sector. This underlines the necessity of a sound conceptual framework.

More guidance and illustrative examples relevant for the public sector would be appreciated.

Further the use of adjectives like 'significant' should be clearly explained. I refer for example to par. 55 (significant changes) and par. 63 (significant foreign operations). Alternatively, you may consider to use the materiality concept, as laid-out in IPSAS1. I therefore would recommend the following introduction. *International Public Sector Standard 4, "The Effects of Changes in Foreign Exchange Rates" (IPSAS 4) is set out in paragraphs 1- 73. All the paragraphs have equal authority. IPSAS 4 should be read in the context of the Basis for Conclusion (if any), and the "Preface to International Public Sector Accounting Standards." IPSAS 4, "Accounting Policies, Changes in Accounting Estimates and Errors" provides a basis for selecting and applying accounting policies in the absence of explicit guidance.*

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3 Detailed views

- a. In par. 11 – 14 of the proposed amendments to IPSAS4, the factors are mentioned to be considered for an entity to determine its functional currency.

When determining the functional currency in the public sector, one additional factor may be national jurisdictional or legislative requirements to record accounts in the currency of the domicile of the other entity, i.e. the foreign operation, or the reporting entity. Then, by law or regulations, the functional currency shall be determined, irrespective or despite the factors mentioned in par. 11 – 12.

A more complicating situation to the example of par. 13 (a) may be when the activities of the foreign operation are carried out as an extension of the reporting entity (rather than being carried out with a significant degree of autonomy) under the supervision or command of an entity which uses another functional currency. This could be under the supervision or command of e.g. a supranational or international public sector entity. This may lead to an additional factor to be considered in determining the functional currency.

In par. 14 a hierarchy has been made clear between the determining factors in par. 11 (primary factors) and par. 12 and 13 (secondary factors). However, one may have the impression that par. 11 and 12 refer to an entity, where as par. 13 refers to a foreign operation. Some further clarification would be appreciated.

- b. In par. 16 the last sentence is not very clear in its meaning and purpose, e.g. which standard is meant with 'this Standard'. I would advise some rephrasing to make more clear the purpose of par. 10.
- c. In par. 21 the summary of the approach required by IPSAS4 has been detailed. The following may be unclear: 'This Standard permits the presentation currency of a reporting entity to be any currency (or currencies). The financial performance and financial position of any individual entity within the reporting entity whose functional currency differs from the presentation currency are translated in accordance with paragraph 43-59.' One would have thought this would be applicable to an associate, joint venture, branch or controlled entity as defined in a foreign operation. However, when reading the quoted text, one may get the impression that this would be applicable to all entities, even beyond a foreign operation. The phrase 'any individual entity within the reporting entity' should be considered to be rephrased to more specifically focus on a foreign operation, as may be the actual approach referred to. Again this also refers to my initial comment on the definition of an entity.
- d. In par. 22 IPSAS4 allows a stand-alone entity, preparing its financial statements or an entity preparing separate financial statements in accordance with IPSAS6: Consolidated and Separate Financial Statements, to present its financial statements in any currency (or currencies). The phrase '.. in any currency (or currencies).', is unclear. It could give the impression an entity can use more than one currency as its presentation currency, which would not be very obvious. Therefore, rephrasing of par. 22 would be advisable.

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- e. Par. 25 states that the date of a transaction is 'the date on which the transaction first qualifies for recognition in accordance with International Public Sector Accounting Standards.' This is not further detailed. In case of a foreign loan the date of the transaction could be the date of the agreement. In case of services delivered or goods received, the date of the transaction may not be that straightforward. This may be complicated if goods are returned and services or goods are delivered in instalments.
- f. In par. 39 reference has been made to the situation in which an entity keeps its books and records in a currency other than its functional currency. When the entity prepares its financial statements all amounts must be translated into the functional currency, according to the proposed amendments to IPSAS 4. This could imply that a foreign operation would have to prepare its financial statements in a functional currency, even when it has to keep its accounts in the currency as determined by law or regulations and therefore not relevant for the reporting entity (who may use another presentation currency). The added value in this situation to have prepared by the foreign operation financial statements in a functional currency, other than the currency used to keep its books and records, is unclear. More clarification to prepare the general purpose financial statements and the users' needs in this respect is therefore important.
- g. Par. 43 refers to a 'common currency'. More clarification of a 'common currency' in connection with the presentation currency would be appreciated.
- h. In par. 44 reference has been made to 'a different presentation currency'. One would assume this is meant to refer to 'the presentation currency'.
- i. Par. 50 refers to the translation of a foreign operation. I would like to give for your consideration to rephrase the paragraph to make it more straightforward: translation should be undertaken in the presentation currency of the reporting entity.
- j. Par. 54 refers to the situation in which there is a difference between the reporting date of the reporting entity and the foreign operation, then the assets and liabilities of the foreign operation should be translated at the exchange rate at the reporting date of the foreign operation. One would however expect the translation to be undertaken at the date of the reporting entity. Therefore clarification of this suggested approach is highly recommended.
- k. In par. 55 adjustments are limited to significant changes in exchange rates up to the reporting date of the reporting entity in accordance with IPSAS6. Please note that transactions concerning huge amounts affected by not significant changes exchange rates may have a material effect on the financial performance and financial position. I therefore would suggest to refer to the concept of materiality, as has been detailed in IPSAS1.
- l. Please note that bequest may also be an example of disposal of a foreign operation, as referred to in par. 58.
- m. In par. 63 reference has been made to a 'significant foreign operation'. Could you indicate what is meant by 'a significant foreign operation', and how this distinguishes between other foreign operations ?

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- n. In par. 66 the situation has been laid out in which an entity displays its financial statements or other financial information in a currency that is different from either its functional currency or its presentation currency. It should be made more clear that this information is supplementary to the financial statements as complying with IPSAS, and therefore I would suggest that this cannot concern the financial statements of the entity under IPSAS.

4 Specific Matters for Comment

1. *Do you agree that the changes made to the equivalent IAS21 in December 2005 are appropriate for the public sector and therefore should be reflected in IPSAS4 as proposed ?*

Considering my detailed comments, I would think that alignment with IAS21 is important. I therefore agree that the proposed changes are appropriate.

3 Robert Street Telephone: 020 7543 5600
London Facsimile: 020 7543 5700
WC2N 6RL www.cipfa.org.uk

Our ref: Tech4/SC0075

Stephenie Fox
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21 December 2007

Dear Stephenie Fox

IPSASB Exposure Draft 33 Amendments to IPSAS 4, "The Effects of Changes in Foreign Exchange Rates"

CIPFA welcomes the opportunity to comment on this exposure draft, which has been reviewed by CIPFA's Accounting and Auditing Standards Panel.

The extant IPSAS 4 closely reflects IAS 21 as at 31 December 2003. Rather than reflecting substantive differences or significant interpretations, IPSAS 4

- provides commentary using public sector examples
- uses public sector terminology in place of 'for profit' terminology
- adapts transitional provisions in IFRS 1 'First-time adoption of IFRS' to the context of first time adoption of accrual IPSASs.

The proposals in ED 33 will preserve these helpful adaptations, while bringing IPSAS 4 in line with IAS 21 as at 31 December 2005.

Furthermore, we understand that at its November 2007 meeting the Board determined that its Convergence Project will seek to reduce the timing gap between IFRS changes and consequential IPSAS updates, so that by December 2009 the body of accruals IPSAS will be framed with regard to extant IFRS as at December 2008. We strongly support the Board's work in bringing its standards onto a more up to date basis.

Our response to the question in the Request for Comment is set out below:

1. Do you agree that the changes made to the equivalent IAS 21 in December 2005 are appropriate for the public sector and therefore should be reflected in IPSAS 4 as proposed?

CIPFA agrees that the changes are appropriate for the public sector and should be reflected in IPSAS 4 as proposed.

I hope this is a helpful contribution to IPSASB's finalisation of the standard.

Yours sincerely

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REQUEST FOR COMMENTS

~~The International Public Sector Accounting Standards Board, an independent standard setting body within the International Federation of Accountants (IFAC), approved this Exposure Draft, *Proposed Amendments to IPSAS 4, "The Effects of Changes in Foreign Exchange Rates"*, for publication in August 2007. The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form.~~

~~Please submit your comments, preferably by email, so that they will be received by **December 31, 2007**. All comments will be considered a matter of public record. Comments should be addressed to:~~

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International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street, 4th Floor
Toronto, Ontario M5V 3H2 CANADA~~

~~Email responses should be sent to: publicsectorpubs@ifac.org~~

~~Copies of this exposure draft may be downloaded free of charge from the IFAC website at <http://www.ifac.org>.~~

International Public Sector Accounting Standards Board
International Federation of Accountants
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This International Public Sector Accounting Standard was prepared by the International Public Sector Accounting Standards Board (IPSASB), an independent standard-setting body within the International Federation of Accountants (IFAC). The objective of the IPSASB is to serve the public interest by developing high quality accounting standards for use by public sector entities around the world in the preparation of general purpose financial statements. This will enhance the quality and transparency of public sector financial reporting and strengthen public confidence in public sector financial management.

This publication may be downloaded free-of-charge from the IFAC website: <http://www.ifac.org>. The approved text is published in the English language.

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ACKNOWLEDGMENT

This ~~Exposure Draft of an amended~~ International Public Sector Accounting Standard is drawn primarily from International Accounting Standard IAS 21 (revised in 2003, as amended in 2005), “The Effects of Changes in Foreign Exchange Rates” published by the International Accounting Standards Board (IASB).

Extracts from IAS 21 are reproduced in this publication of the International Public Sector Accounting Standards Board of the International Federation of Accountants with the permission of the International Accounting Standards Committee Foundation (IASCF).

The approved text of the IFRSs is that published by the IASB in the English language, and copies may be obtained directly from IASB Publications Department, 30 Cannon Street, London EC4M 6XH, United Kingdom.

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Internet: <http://www.iasb.org>.

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PROPOSED AMENDMENTS TO IPSAS 4, “THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES”

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INTRODUCTION

Introduction to the International Public Sector Accounting Standards

The International Federation of Accountants' International Public Sector Accounting Standards Board (IPSASB) develops accounting standards for public sector entities referred to as International Public Sector Accounting Standards (IPSASs). The IPSASB recognizes the significant benefits of achieving consistent and comparable financial information across jurisdictions and it believes that the IPSASs play a key role in enabling these benefits to be realized. The IPSASB strongly encourages governments and national standard-setters to engage in the development of its Standards by commenting on the proposals set out in Exposure Drafts.

The IPSASB issues IPSASs dealing with financial reporting under the cash basis of accounting and the accrual basis of accounting. The accrual basis IPSASs are based on the International Financial Reporting Standards (IFRSs), issued by the International Accounting Standards Board (IASB), where the requirements of those Standards are applicable to the public sector. They also deal with public sector specific financial reporting issues that are not dealt with in IFRSs.

The adoption of IPSASs by governments will improve both the quality and comparability of financial information reported by public sector entities around the world. The IPSASB recognizes the right of governments and national standard-setters to establish accounting standards and guidelines for financial reporting in their jurisdictions. The IPSASB encourages the adoption of IPSASs and the harmonization of national requirements with IPSASs. Financial statements should be described as complying with IPSASs only if they comply with all the requirements of each applicable IPSAS.

Due Process and Timetable

An important part of the process of developing IPSASs is for the IPSASB to receive comments on the proposals set out in Exposure Drafts from governments, public sector entities, auditors, standard setters and other parties with an interest in public sector financial reporting. Accordingly, each proposed IPSAS is first released as an Exposure Draft, inviting interested parties to provide their comments. Exposure Drafts will usually have a comment period of four months, although longer periods may be used for certain Exposure Drafts. Upon the closure of the comment period, the IPSASB will consider the comments received on the Exposure Draft and may modify the proposed IPSAS in the light of the comments received before proceeding to issue a final Standard.

Background and Purpose of the Exposure Draft

In late 1997, the IPSASB's predecessor—the Public Sector Committee (PSC)¹—commenced a program for the development of IPSASs based on International Accounting Standards (IASs) on issue at August 1997, or their subsequently revised versions, to the extent the requirements of the IASs are relevant for the public sector. The IPSASs maintained the requirements, structure and text of the IASs unless there was a public sector specific reason for a departure. The first phase of the standards development program was completed in late 2002.

In late 2003, as a consequence of the IASB's General Improvements Project, the PSC initiated its General Improvements Project with the objective of updating 11 IPSASs to converge with improved equivalent IASs issued in December 2003. The 11 improved IPSASs, including IPSAS4, "The Effects of Changes in Foreign Exchange Rates", were approved by the IPSASB in November 2006 and were issued in December 2006.

The objective of this Exposure Draft is to update IPSAS 4 to reflect the IASB's amendment to IAS 21, "The Effects of Changes in Foreign Exchange Rates" (published as *Net Investment in a Foreign Operation*) in December 2005. The objective of the IASB's amendment to IAS 21 was in response to concerns raised by constituents about the requirements in previous IAS 21 for dealing with exchange differences arising on a monetary item that forms part of the reporting entity's net investment in a foreign operation.

¹ The PSC was reconstituted as the IPSASB by the IFAC Board in November 2004.

~~Until the proposed IPSAS 4 becomes effective, the requirements of the current version of IPSAS 4 remain in force.~~

~~Presentation of the Proposed Amendments to IPSAS 4~~

~~The Exposure Draft presents a marked-up copy of the full text of IPSAS4. The proposed changes are identified in mark-up.~~

REQUEST FOR COMMENTS

~~The Exposure Draft proposes amendments to IPSAS 4. Comments are invited on the proposals in this Exposure Draft by December 31, 2007. The IPSASB invites comments on all the changes proposed in the Exposure Draft, and would particularly welcome comments to the questions set out in the “Specific Matter for Comment” section.~~

~~Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.~~

Specific Matter for Comment

~~The IPSASB would particularly value comments on the following question:~~

- ~~1. Do you agree that the changes made to the equivalent IAS 21 in December 2005 are appropriate for the public sector and therefore should be reflected in IPSAS 4 as proposed?~~

SUMMARY OF MAIN CHANGES TO IPSAS 4

~~THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES~~

The main changes proposed are:

Net Investment in a Foreign Operation

To clarify in paragraph 19 that an entity that has a monetary item, which is, in substance, a part of the entity's net investment in a foreign operation, may be any controlled entity of the economic entity. An example is also provided to illustrate this clarification. Previously, IPSAS 4 did not make this clear.

Recognition of Exchange Differences

To require in paragraph 38 that exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation are recognized initially in a separate component of net assets/equity in the financial statements that include the foreign operation and the reporting entity, irrespective of whether the monetary item is denominated in the functional currency of the reporting entity, or in the functional currency of the foreign operation, or in a currency other than the functional currency of either the reporting entity or the foreign operation. Previously, IPSAS 4 required such exchange differences to be recognized in surplus or deficit in the financial statements including the foreign operation and the reporting entity when the monetary item is denominated in a currency other than the functional currency of either the reporting entity or the foreign operation.

Other Changes

To amend the Introduction and the Basis for Conclusions as a result of the amendments to this Standard.

To make minor editorial changes to improve the style or the consistency with other IPSASs.

IPSAS 4—THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES

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International Public Sector Accounting Standard 4, “The Effects of Changes in Foreign Exchange Rates” (IPSAS 4) is set out in paragraphs 1-73. All the paragraphs have equal authority. IPSAS 4 should be read in the context of its objective and the Basis for Conclusions, the “Preface to the International Public Sector Accounting Standards.” IPSAS 3, “Accounting Policies, Changes in Accounting Estimates and Errors” provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Introduction

- IN1. International Public Sector Accounting Standard (IPSAS) 4, “The Effects of Changes in Foreign Exchange Rates,” replaces IPSAS 4, “The Effects of Changes in Foreign Exchange Rates” (issued December 2006), and should be applied for annual reporting periods beginning on or after MM DD, YYYY. Earlier application is encouraged.

Reasons for Revising IPSAS 4

- IN2. The International Public Sector Accounting Standards Board developed this revised IPSAS 4 as a response to the International Accounting Standards Board’s amendment to IAS 21 (published as *Net Investment in a Foreign Operation*) in December 2005 and its own policy to converge public sector accounting standards with private sector standards to the extent appropriate.
- IN3. In developing this revised IPSAS 4, the IPSASB adopted the policy of amending the IPSAS for those changes made to the former IAS 21, “The Effects of Changes in Foreign Exchange Rates” made as a consequence of the IASB’s amendment in December 2005, except where the original IPSAS had varied from the provisions of IAS 21 for a public sector specific reason; such variances are retained in this IPSAS 4 and are noted in the Comparison with IAS 21.

Changes from Previous Requirements

- IN4. The main changes from the previous version of IPSAS 4 are described below.

Net Investment in a Foreign Operation

- IN5. The Standard clarifies that an entity that has a monetary item, which is, in substance, a part of the entity’s net investment in a foreign operation, and therefore accounts for such item in accordance with the requirements of this Standard, may be any controlled entity of the economic entity.

Recognition of Exchange Differences

- IN6. The Standard requires that when a monetary item forms part of a reporting entity’s net investment in a foreign operation and is denominated in a currency other than the functional currency of either the reporting entity or the foreign operation, exchange differences arising on this monetary item are recognized initially in a separate component of net assets/equity in the financial statements that include the foreign operation and the reporting entity. Previously, such exchange differences were required to be recognized in surplus or deficit in the financial statements including the foreign operation and the reporting entity.

Objective

1. An entity may carry on foreign activities in two ways. It may have transactions in foreign currencies or it may have foreign operations. In addition, an entity may present its financial statements in a foreign currency. The objective of this Standard is to prescribe how to include foreign currency transactions and foreign operations in the financial statements of an entity and how to translate financial statements into a presentation currency.
2. The principal issues are which exchange rate(s) to use and how to report the effects of changes in exchange rates in the financial statements.

Scope

3. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard:**
 - (a) **in accounting for transactions and balances in foreign currencies, except for those derivative transactions and balances that are within the scope of the relevant international or national accounting standards dealing with the recognition and measurement of financial instruments;**
 - (b) **in translating the financial performance and financial position of foreign operations that are included in the financial statements of the entity by consolidation, proportionate consolidation or by the equity method; and**
 - (c) **in translating an entity's financial performance and financial position into a presentation currency.**
4. International or national accounting standards dealing with the recognition and measurement of financial instruments apply to many foreign currency derivatives and, accordingly, these are excluded from the scope of this Standard. However, those foreign currency derivatives that are not within the scope of these international or national accounting standards (e.g., some foreign currency derivatives that are embedded in other contracts) are within the scope of this Standard. In addition, this Standard applies when an entity translates amounts relating to derivatives from its functional currency to its presentation currency.
5. This Standard does not apply to hedge accounting for foreign currency items, including the hedging of a net investment in a foreign operation. Accordingly, entities may apply the relevant international or national accounting standards dealing with hedge accounting.
6. **This Standard applies to all public sector entities other than Government Business Enterprises.**
7. The "Preface to International Public Sector Accounting Standards" issued by the International Public Sector Accounting Standards Board (IPSASB) explains that Government Business Enterprises (GBEs) apply International Financial Reporting Standards (IFRSs) which are issued by the International Accounting Standards Board (IASB). GBEs are defined in IPSAS 1, "Presentation of Financial Statements."
8. This Standard applies to the presentation of an entity's financial statements in a foreign currency and sets out requirements for the resulting financial statements to be described as complying with International Public Sector Accounting Standards. For translations of financial information into a foreign currency that do not meet these requirements, this Standard specifies information to be disclosed.

9. This Standard does not apply to the presentation in a cash flow statement of cash flows arising from transactions in a foreign currency, or to the translation of cash flows of a foreign operation (see IPSAS 2, “Cash Flow Statements”).

Definitions

10. The following terms are used in this Standard with the meanings specified:

Closing rate is the spot exchange rate at the reporting date.

Economic entity means a group of entities comprising a controlling entity and one or more controlled entities.

Exchange difference is the difference resulting from translating a given number of units of one currency into another currency at different exchange rates.

Exchange rate is the ratio of exchange for two currencies.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s length transaction.

Foreign currency is a currency other than the functional currency of the entity.

Foreign operation is an entity that is a controlled entity, associate, joint venture or branch of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity.

Functional currency is the currency of the primary economic environment in which the entity operates.

Monetary items are units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency.

Net investment in a foreign operation is the amount of the reporting entity’s interest in the net assets/equity of that operation.

Presentation currency is the currency in which the financial statements are presented.

Spot exchange rate is the exchange rate for immediate delivery.

Terms defined in other International Public Sector Accounting Standards are used in this Standard with the same meaning as in those other Standards, and are reproduced in the Glossary of Defined Terms published separately.

Functional Currency

11. The primary economic environment in which an entity operates is normally the one in which it primarily generates and expends cash. An entity considers the following factors in determining its functional currency:
- (a) the currency:
 - (i) that revenue is raised from, such as taxes, grants, and fines;
 - (ii) that mainly influences sales prices for goods and services (this will often be the currency in which sales prices for its goods and services are denominated and settled); and
 - (iii) of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services.

- (b) the currency that mainly influences labor, material and other costs of providing goods and services (this will often be the currency in which such costs are denominated and settled).
12. The following factors may also provide evidence of an entity's functional currency:
 - (a) the currency in which funds from financing activities (i.e., issuing debt and equity instruments) are generated.
 - (b) the currency in which receipts from operating activities are usually retained.
 13. The following additional factors are considered in determining the functional currency of a foreign operation, and whether its functional currency is the same as that of the reporting entity (the reporting entity, in this context, being the entity that has the foreign operation as its controlled entity, branch, associate or joint venture):
 - (a) whether the activities of the foreign operation are carried out as an extension of the reporting entity, rather than being carried out with a significant degree of autonomy. An example of the former is when a department of defense has a number of overseas bases which conduct activities on behalf of a national government. The defense bases might conduct their activities substantially in the functional currency of the reporting entity. For example, military personnel may be paid in the functional currency and receive only a small allowance in local currency. Purchases of supplies and equipment might be largely obtained via the reporting entity with purchases in local currency being kept to a minimum. Another example would be an overseas campus of a public university which operates under the management and direction of the domestic campus. In contrast, a foreign operation with a significant degree of autonomy may accumulate cash and other monetary items, incur expenses, generate revenue and perhaps arrange borrowings, all substantially in its local currency. Some examples of government-owned foreign operations which may operate independently of other government agencies include tourist offices, petroleum exploration companies, trade boards and broadcasting operations. Such entities may be established as Government Business Enterprises.
 - (b) whether transactions with the reporting entity are a high or a low proportion of the foreign operation's activities.
 - (c) whether cash flows from the activities of the foreign operation directly affect the cash flows of the reporting entity and are readily available for remittance to it.
 - (d) whether cash flows from the activities of the foreign operation are sufficient to service existing and normally expected debt obligations without funds being made available by the reporting entity.
 14. When the above indicators are mixed and the functional currency is not obvious, management uses its judgment to determine the functional currency that most faithfully represents the economic effects of the underlying transactions, events and conditions. As part of this approach, management gives priority to the primary indicators in paragraph ~~114~~ before considering the indicators in paragraphs ~~124~~ and ~~134~~, which are designed to provide additional supporting evidence to determine an entity's functional currency.
 15. An entity's functional currency reflects the underlying transactions, events and conditions that are relevant to it. Accordingly, once determined, the functional currency is not changed unless there is a change in those underlying transactions, events and conditions.

16. If the functional currency is the currency of a hyperinflationary economy, the entity's financial statements are restated in accordance with IPSAS 10, "Financial Reporting in Hyperinflationary Economies." An entity cannot avoid restatement in accordance with IPSAS 10 by, for example, adopting as its functional currency a currency other than the functional currency determined in accordance with this Standard (such as the functional currency of its controlling entity).

Monetary Items

17. The essential feature of a monetary item is a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency. Examples include: social policy obligations and other employee benefits to be paid in cash; provisions that are to be settled in cash; and cash dividends or similar distributions that are recognized as a liability. Conversely, the essential feature of a non-monetary item is the absence of a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency. Examples include: amounts prepaid for goods and services (e.g., prepaid rent); goodwill; intangible assets; inventories; property, plant and equipment; and provisions that are to be settled by the delivery of a non-monetary asset.

Net Investment in a Foreign Operation

18. An entity may have a monetary item that is receivable from or payable to a foreign operation. An item for which settlement is neither planned nor likely to occur in the foreseeable future is, in substance, a part of the entity's net investment in that foreign operation, and is accounted for in accordance with paragraphs 37 and 38. Such monetary items may include long-term receivables or loans. They do not include trade receivables or trade payables.
19. The entity that has a monetary item receivable from or payable to a foreign operation described in paragraph 18 may be any controlled entity of the economic entity. For example, an entity has two controlled entities, A and B. Controlled entity B is a foreign operation. Controlled entity A grants a loan to controlled entity B. Controlled entity A's loan receivable from controlled entity B would be part of the controlled entity A's net investment in controlled entity B if settlement of the loan is neither planned nor likely to occur in the foreseeable future. This would also be true if controlled entity A were itself a foreign operation.

Summary of the Approach Required by this Standard

20. In preparing financial statements, each entity—whether a stand-alone entity, an entity with foreign operations (such as a controlling entity) or a foreign operation (such as a controlled entity or branch)—determines its functional currency in accordance with paragraphs ~~1144~~ - ~~1646~~. The entity translates foreign currency items into its functional currency and reports the effects of such translation in accordance with paragraphs 23 –42 and 59.
21. Many reporting entities comprise a number of individual entities (e.g., an economic entity is made up of a controlling entity and one or more controlled entities). Various types of entities, whether members of an economic entity or otherwise, may have investments in associates or joint ventures. They may also have branches. It is necessary for the financial performance and financial position of each individual entity included in the reporting entity to be translated into the currency in which the reporting entity presents its financial statements. This Standard permits the presentation currency of a reporting entity to be any currency (or currencies). The financial performance and financial position of any individual entity within the

reporting entity whose functional currency differs from the presentation currency are translated in accordance with paragraphs 43-59.

22. This Standard also permits a stand-alone entity preparing financial statements or an entity preparing separate financial statements in accordance with IPSAS 6, “Consolidated and Separate Financial Statements” to present its financial statements in any currency (or currencies). If the entity’s presentation currency differs from its functional currency, its financial performance and financial position are also translated into the presentation currency in accordance with paragraphs 43-59.

Reporting Foreign Currency Transactions in the Functional Currency

Initial Recognition

23. A foreign currency transaction is a transaction that is denominated or requires settlement in a foreign currency, including transactions arising when an entity:
- (a) buys or sells goods or services whose price is denominated in a foreign currency;
 - (b) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or
 - (c) otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.
24. **A foreign currency transaction shall be recorded, on initial recognition in the 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.**
25. The date of a transaction is the date on which the transaction first qualifies for recognition in accordance with International Public Sector Accounting Standards. For practical reasons, a rate that approximates the actual rate at the date of the transaction is often used, for example, an average rate for a week or a month might be used for all transactions in each foreign currency occurring during that period. However, if exchange rates fluctuate significantly, the use of the average rate for a period is inappropriate.
26. Exchange rate changes may have an impact on cash or cash equivalents held or due in a foreign currency. The presentation of such exchange differences is dealt with in IPSAS 2. Although these changes are not cash flows, the effect of exchange rate changes on cash or cash equivalents held or due in a foreign currency are reported in the cash flow statement in order to reconcile cash and cash equivalents at the beginning and the end of the period. These amounts are presented separately from cash flows from operating, investing and financing activities and include the differences, if any, had those cash flows been reported at end-of-period exchange rates.

Reporting at Subsequent Reporting Dates

27. **At each reporting date:**
- (a) **foreign currency monetary items shall be translated using the closing rate;**
 - (b) **non-monetary items that are measured in terms of historical cost in a foreign currency shall be translated using the exchange rate at the date of the transaction; and**

- (c) **non-monetary items that are measured at fair value in a foreign currency shall be translated using the exchange rates at the date when the fair value was determined.**
28. The carrying amount of an item is determined in conjunction with other relevant International Public Sector Accounting Standards. For example, property, plant and equipment may be measured in terms of fair value or historical cost in accordance with IPSAS 17, "Property, Plant and Equipment." Whether the carrying amount is determined on the basis of historical cost or on the basis of fair value, if the amount is determined in a foreign currency it is then translated into the functional currency in accordance with this Standard.
29. The carrying amount of some items is determined by comparing two or more amounts. For example, the carrying amount of inventories held for sale is the lower of cost and net realizable value in accordance with IPSAS 12, "Inventories." Similarly, in accordance with IPSAS 21, "Impairment of Non-Cash-Generating Assets," the carrying amount of a non-cash generating asset for which there is an indication of impairment is the lower of its carrying amount before considering possible impairment losses and its recoverable service amount. When such an asset is non-monetary and is measured in a foreign currency, the carrying amount is determined by comparing:
- (a) the cost or carrying amount, as appropriate, translated at the exchange rate at the date when that amount was determined (i.e., the rate at the date of the transaction for an item measured in terms of historical cost); and
 - (b) the net realizable value or recoverable service amount, as appropriate, translated at the exchange rate at the date when that value was determined (e.g., the closing rate at the reporting date).
- The effect of this comparison may be that an impairment loss is recognized in the functional currency but would not be recognized in the foreign currency, or vice versa.
30. When several exchange rates are available, the rate used is that at which the future cash flows represented by the transaction or balance could have been settled if those cash flows had occurred at the measurement date. If exchangeability between two currencies is temporarily lacking, the rate used is the first subsequent rate at which exchanges could be made.

Recognition of Exchange Differences

31. As noted in paragraph 55, this Standard does not deal with hedge accounting for foreign currency items. Guidance in relation to hedge accounting, including the criteria for when to use hedge accounting, can be found in the relevant international or national accounting standards dealing with the recognition and measurement of financial instruments.
32. **Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous financial statements shall be recognized in surplus or deficit in the period in which they arise, except as described in paragraph 37.**
33. When monetary items arise from a foreign currency transaction and there is a change in the exchange rate between the transaction date and the date of settlement, an exchange difference results. When the transaction is settled within the same accounting period as that in which it occurred, all the exchange difference is

recognized in that period. However, when the transaction is settled in a subsequent accounting period, the exchange difference recognized in each period up to the date of settlement is determined by the change in exchange rates during each period.

34. The treatment of foreign currency exchange rate changes in a cash flow statement is described in paragraph 26.
35. **When a gain or loss on a non-monetary item is recognized directly in net assets/equity, any exchange component of that gain or loss shall be recognized directly in net assets/equity. Conversely, when a gain or loss on a non-monetary item is recognized in surplus or deficit, any exchange component of that gain or loss shall be recognized in surplus or deficit.**
36. Other Standards require some gains and losses to be recognized directly in net assets/equity. For example, IPSAS 17 requires some gains and losses arising on a revaluation of property, plant and equipment to be recognized directly in net assets/equity. When such an asset is measured in a foreign currency, paragraph 27 (c) of this Standard requires the revalued amount to be translated using the rate at the date the value is determined, resulting in an exchange difference that is also recognized in net assets/equity.
37. **Exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation (see paragraph 1818) shall be recognized in surplus or deficit in the separate financial statements of the reporting entity or the individual financial statements of the foreign operation, as appropriate. In the financial statements that include the foreign operation and the reporting entity (e.g., consolidated financial statements when the foreign operation is a controlled entity), such exchange differences shall be recognized initially in a separate component of net assets/equity and recognized in surplus or deficit on disposal of the net investment in accordance with paragraph 57.**
38. When a monetary item forms part of a reporting entity's net investment in a foreign operation and is denominated in the functional currency of the reporting entity, an exchange difference arises in the foreign operation's individual financial statements in accordance with paragraph 32. If such an item is denominated in the functional currency of the foreign operation, an exchange difference arises in the reporting entity's separate financial statements in accordance with paragraph 32. If such an item is denominated in a currency other than the functional currency of either the reporting entity or the foreign operation, an exchange difference arises in the reporting entity's separate financial statements and in the foreign operation's individual financial statements in accordance with paragraph 32. Such exchange differences are reclassified to the separate component of net assets/equity in the financial statements that include the foreign operation and the reporting entity (i.e., financial statements in which the foreign operation is consolidated, proportionately consolidated or accounted for using the equity method).
39. When an entity keeps its books and records in a currency other than its functional currency, at the time the entity prepares its financial statements all amounts are translated into the functional currency in accordance with paragraphs 23-30. This produces the same amounts in the functional currency as would have occurred had the items been recorded initially in the functional currency. For example, monetary items are translated into the functional currency using the closing rate, and non-monetary items that are measured on a historical cost basis are translated using the exchange rate at the date of the transaction that resulted in their recognition.

Change in Functional Currency

40. **When there is a change in an entity's functional currency, the entity shall apply the translation procedures applicable to the new functional currency prospectively from the date of the change.**
41. As noted in paragraph ~~15~~¹⁵, the functional currency of an entity reflects the underlying transactions, events and conditions that are relevant to the entity. Accordingly, once the functional currency is determined, it can be changed only if there is a change to those underlying transactions, events and conditions. For example, a change in the currency that mainly influences the sales prices or the provision of goods and services may lead to a change in an entity's functional currency.
42. The effect of a change in functional currency is accounted for prospectively. In other words, an entity translates all items into the new functional currency using the exchange rate at the date of the change. The resulting translated amounts for non-monetary items are treated as their historical cost. Exchange differences arising from the translation of a foreign operation previously classified in net assets/equity in accordance with paragraphs 37 and 44(c) are not recognized in surplus or deficit until the disposal of the operation.

Use of a Presentation Currency other than the Functional Currency

Translation to the Presentation Currency

43. An entity may present its financial statements in any currency (or currencies). If the presentation currency differs from the entity's functional currency, it translates its financial performance and financial position into the presentation currency. For example, when an economic entity contains individual entities with different functional currencies, the financial performance and financial position of each entity are expressed in a common currency so that consolidated financial statements may be presented.
44. **The financial performance and financial position of an entity whose functional currency is not the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:**
- (a) **assets and liabilities for each statement of financial position presented (i.e., including comparatives) shall be translated at the closing rate at the date of that statement of financial position;**
 - (b) **revenue and expenses for each statement of financial performance (i.e., including comparatives) shall be translated at exchange rates at the dates of the transactions; and**
 - (c) **all resulting exchange differences shall be recognized as a separate component of net assets/equity.**
45. In translating the cash flows, that is the cash receipts and cash payments, of a foreign operation for incorporation into its cash flow statement, the reporting entity shall comply with the procedures in IPSAS 2. IPSAS 2 requires that the cash flows of a controlled entity which satisfies the definition of a foreign operation shall be translated at the exchange rates between the functional currency and the foreign currency at the dates of the cash flows. IPSAS 2 also outlines the presentation of unrealized gains and losses arising from changes in foreign currency exchange rates on cash and cash equivalents held or due in a foreign currency.
46. For practical reasons, a rate that approximates the exchange rates at the dates of the transactions, for example an average rate for the period, is often used to translate

revenue and expense items. However, if exchange rates fluctuate significantly, the use of the average rate for a period is inappropriate.

47. The exchange differences referred to in paragraph 44 (c) result from:
- (a) translating revenue and expenses at the exchange rates at the dates of the transactions and assets and liabilities at the closing rate. Such exchange differences arise both on revenue and expense items recognized in surplus or deficit and on those recognized directly in net assets/equity.
 - (b) translating the opening net assets/equity at a closing rate that differs from the previous closing rate.

These exchange differences are not recognized in surplus or deficit because the changes in exchange rates have little or no direct effect on the present and future cash flows from operations. When the exchange differences relate to a foreign operation that is consolidated but is not wholly-owned, accumulated exchange differences arising from translation and attributable to minority interests are allocated to, and recognized as part of, minority interest in the consolidated statement of financial position.

48. **The financial performance and financial position of an entity whose functional currency is the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:**
- (a) **all amounts (i.e., assets, liabilities, net assets/equity items, revenue and expenses, including comparatives) shall be translated at the closing rate at the date of the most recent statement of financial position, except that**
 - (b) **when amounts are translated into the currency of a non-hyperinflationary economy, comparative amounts shall be those that were presented as current year amounts in the relevant prior year financial statements (i.e., not adjusted for subsequent changes in the price level or subsequent changes in exchange rates).**
49. **When an entity's functional currency is the currency of a hyperinflationary economy, the entity shall restate its financial statements in accordance with IPSAS 10 before applying the translation method set out in paragraph 48, except for comparative amounts that are translated into a currency of a non-hyperinflationary economy (see paragraph 48(b)). When the economy ceases to be hyperinflationary and the entity no longer restates its financial statements in accordance with IPSAS 10, it shall use as the historical costs for translation into the presentation currency the amounts restated to the price level at the date the entity ceased restating its financial statements.**

Translation of a Foreign Operation

50. Paragraphs 51-56, in addition to paragraphs 43-49, apply when the financial performance and financial position of a foreign operation are translated into a presentation currency so that the foreign operation can be included in the financial statements of the reporting entity by consolidation, proportionate consolidation or the equity method.
51. The incorporation of the financial performance and financial position of a foreign operation with those of the reporting entity follows normal consolidation procedures, such as the elimination of balances and transactions within an economic entity (see IPSAS 6 and IPSAS 8, "Interests in Joint Ventures").
52. However, a monetary asset (or liability) within an economic entity, whether short-term or long-term, cannot be eliminated against the corresponding liability (or asset)

within an economic entity without showing the results of currency fluctuations in the consolidated financial statements. This is because the monetary item represents a commitment to convert one currency into another and exposes the reporting entity to a gain or loss through currency fluctuations. Accordingly, in the consolidated financial statements of the reporting entity, such an exchange difference continues to be recognized in surplus or deficit or, if it arises from the circumstances described in paragraph 37, it is classified as net assets/equity until the disposal of the foreign operation.

53. When the financial statements of a foreign operation are as of a date different from that of the reporting entity, the foreign operation often prepares additional statements as of the same date as the reporting entity's financial statements. When this is not done, IPSAS 6 allows the use of a different reporting date provided that the difference is no greater than three months and adjustments are made for the effects of any significant transactions or other events that occur between the different dates.
54. When there is a difference between the reporting date of the reporting entity and the foreign operation, the assets and liabilities of the foreign operation are translated at the exchange rate at the reporting date of the foreign operation.
55. Adjustments are made for significant changes in exchange rates up to the reporting date of the reporting entity in accordance with IPSAS 6. The same approach is used in applying the equity method to associates and joint ventures and in applying proportionate consolidation to joint ventures in accordance with IPSAS 7, "Investments in Associates" and IPSAS 8.
56. **Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation shall be treated as assets and liabilities of the foreign operation. Thus they shall be expressed in the functional currency of the foreign operation and shall be translated at the closing rate in accordance with paragraphs 44 and 48.**

Disposal of a Foreign Operation

57. **On the disposal of a foreign operation, the cumulative amount of the exchange differences deferred in the separate component of net assets/equity relating to that foreign operation shall be recognized in surplus or deficit when the gain or loss on disposal is recognized.**
58. An entity may dispose of its interest in a foreign operation through sale, liquidation, repayment of contributed capital or abandonment of all, or part of, that entity. The payment of a dividend or similar distribution is part of a disposal only when it constitutes a return of the investment, for example when the dividend or similar distribution is paid out of pre-acquisition surplus. In the case of a partial disposal, only the proportionate share of the related accumulated exchange difference is included in the gain or loss. A write-down of the carrying amount of a foreign operation does not constitute a partial disposal. Accordingly, no part of the deferred foreign exchange gain or loss is recognized in surplus or deficit at the time of a write-down.

Tax Effects of Exchange Differences

59. For reporting entities subject to income taxes, guidance on the treatment of tax effects associated with the gains and losses on foreign currency transactions and exchange differences arising on translating the financial performance and financial position of an entity (including a foreign operation) into a different currency can be

found in the relevant international or national accounting standards dealing with income taxes.

Disclosure

60. **In paragraphs 62 and 64-66 references to “functional currency” apply, in the case of an economic entity, to the functional currency of the controlling entity.**
61. **The entity shall disclose:**
 - (a) **the amount of exchange differences recognized in surplus or deficit except for those arising on financial instruments measured at fair value through surplus or deficit in accordance with the relevant international or national accounting standards dealing with the recognition and measurement of financial instruments; and**
 - (b) **net exchange differences classified in a separate component of net assets/equity, and a reconciliation of the amount of such exchange differences at the beginning and end of the period.**
62. **When the presentation currency is different from the functional currency, that fact shall be stated, together with disclosure of the functional currency and the reason for using a different presentation currency.**
63. **When there is a change in the functional currency of either the reporting entity or a significant foreign operation, that fact and the reason for the change in functional currency shall be disclosed.**
64. **When an entity presents its financial statements in a currency that is different from its functional currency, it shall describe the financial statements as complying with International Public Sector Accounting Standards only if they comply with all the requirements of each applicable Standard including the translation method set out in paragraphs 44 and 48.**
65. **An entity sometimes presents its financial statements or other financial information in a currency that is not its functional currency without meeting the requirements of paragraph 64. For example, an entity may convert into another currency only selected items from its financial statements. Or, an entity whose functional currency is not the currency of a hyperinflationary economy may convert the financial statements into another currency by translating all items at the most recent closing rate. Such conversions are not in accordance with International Public Sector Accounting Standards and the disclosures set out in paragraph 66 are required.**
66. **When an entity displays its financial statements or other financial information in a currency that is different from either its functional currency or its presentation currency and the requirements of paragraph 64 are not met, it shall:**
 - (a) **clearly identify the information as supplementary information to distinguish it from the information that complies with International Public Sector Accounting Standards;**
 - (b) **disclose the currency in which the supplementary information is displayed; and**
 - (c) **disclose the entity’s functional currency and the method of translation used to determine the supplementary information.**

Transitional Provisions

First-time Adoption of Accrual Accounting

67. **A reporting entity need not comply with the requirements for cumulative translation differences that existed at the date of first adoption of accrual accounting in accordance with International Public Sector Accounting Standards. If a first-time adopter uses this exemption:**
- (a) **the cumulative translation differences for all foreign operations are deemed to be zero at the date of first adoption to International Public Sector Accounting Standards; and**
 - (b) **the gain and loss on a subsequent disposal of any foreign operation shall exclude translation differences that arose before the date of first adoption to International Public Sector Accounting Standards, and shall include later translation differences.**
68. **This Standard requires entities to:**
- (a) **classify some translation differences as a separate component of net assets/equity; and**
 - (b) **on disposal of a foreign operation, to transfer the cumulative translation difference for that foreign operation to the statement of financial performance as part of the gain or loss on disposal.**

The transitional provisions provide first-time adopters of IPSASs with relief from this requirement.

Transitional Provisions for All Entities

69. **An entity shall apply paragraph 56 prospectively to all acquisitions occurring after the beginning of the financial reporting period in which this International Public Sector Accounting Standard is first applied. Retrospective application of paragraph 56 to earlier acquisitions is permitted. For an acquisition of a foreign operation treated prospectively but which occurred before the date on which this Standard is first applied, the entity shall not restate prior years and accordingly may, when appropriate, treat goodwill and fair value adjustments arising on that acquisition as assets and liabilities of the entity rather than as assets and liabilities of the foreign operation. Therefore, those goodwill and fair value adjustments either are already expressed in the entity's functional currency or are non-monetary foreign currency items, which are reported using the exchange rate at the date of the acquisition.**
70. **All other changes resulting from the application of this International Public Sector Accounting Standard shall be accounted for in accordance with the requirements of IPSAS 3, "Accounting Policies, Changes in Accounting Estimates and Errors".**

Effective Date

71. **An entity shall apply this International Public Sector Accounting Standard for annual periods beginning on or after MM DD, YYYY. Earlier application is encouraged. If an entity applies this Standard for a period beginning before MM DD, YYYY, it shall disclose that fact.**
72. **When an entity adopts the accrual basis of accounting, as defined by International Public Sector Accounting Standards, for financial reporting purposes, subsequent to**

this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Withdrawal of IPSAS 4 (issued 2006)

73. This Standard supersedes IPSAS 4, "The Effects of Changes in Foreign Exchange Rates" issued in 2006.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, IPSAS 4, “The Effects of Changes in Foreign Exchange Rates.” This Basis for Conclusions only notes the IPSASB’s reasons for departing from provisions of the related International Accounting Standard.

Background

- BC1. The International Public Sector Accounting Standards Board (IPSASB)’s International Financial Reporting Standards (IFRSs) Convergence Program is an important element in IPSASB’s work program. The IPSASB’s policy is to converge the accrual basis International Public Sector Accounting Standards (IPSASs) with IFRSs issued by the International Accounting Standards Board (IASB) where appropriate for public sector entities.
- BC2. Accrual basis IPSASs that are converged with IFRSs maintain the requirements, structure and text of the IFRSs, unless there is a public sector specific reason for a departure. Departure from the equivalent IFRS occurs when requirements or terminology in the IFRS are not appropriate for the public sector, or when inclusion of additional commentary or examples is necessary to illustrate certain requirements in the public sector context. Differences between IPSASs and their equivalent IFRSs are identified in the ‘comparison with IFRS’ included in each IPSAS. The Comparison with IAS 21 references only the version of IAS 21 that was revised in 2003 and amended in 2005².
- BC3. In May 2000 the IPSASB’s predecessor, the Public Sector Committee (PSC)³, issued the first version of IPSAS 4, “The Effects of Changes in Foreign Exchange Rates”, which was based on IAS 21, “The Effects of Changes in Foreign Exchange Rates” (1993). In December 2006 the IPSASB revised IPSAS 4, which was based on IAS 21 (Revised 2003), as part of its General Improvements Project. In December 2005 the IASB issued an amendment to IAS 21 (published as *Net Investment in a Foreign Operation*).³
- BC4. In early 2007, the IPSASB initiated a continuous improvements project to update existing IPSASs to be converged with the latest related IFRSs to the extent appropriate for the public sector. As part of the project, the IPSASB reviewed the IASB’s amendment to IAS 21 issued in December 2005 and generally concurred with the IASB’s reasons for amending the IAS and with the amendment made. (The IASB’s Basis for Conclusions as a result of the amendment is not reproduced here. Subscribers to the IASB’s *Comprehensive Subscription Service* can view the Basis for Conclusions on the IASB’s website at www.iasb.org).
- BC5. IAS 21 has been further amended as a consequence of IFRSs and revised IASs issued after December 2005. IPSAS 4 does not include the consequential amendments arising from IFRSs or revised IASs issued after December 2005. This is because the IPSASB has not yet reviewed and formed a view on the applicability

² The International Accounting Standards (IASs) were issued by the IASB’s predecessor – the International Accounting Standards Committee. The Standards issued by the IASB are entitled International Financial Reporting Standards (IFRSs). The IASB has defined IFRSs to consist of IFRSs, IASs and Interpretations of the Standards. In some cases, the IASB has amended, rather than replaced, the IASs, in which case the old IAS number remains.

³ The PSC became the IPSASB when the IFAC Board changed the PSC’s mandate to become an independent standard-setting board in November 2004.

of the requirements in those IFRSs and the revisions to those IASs to public sector entities.

Table of Concordance

This table shows how the contents of the superseded version of IPSAS 4 and the current version of IPSAS 4 correspond. Paragraphs are treated as corresponding if they broadly address the same matter even though the guidance may differ.

| Superseded IPSAS 4 paragraphs | Current IPSAS 4 paragraph |
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| Superseded IPSAS 4 paragraphs | Current IPSAS 4 paragraph |
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| None | 19 |

Comparison with IAS 21

International Public Sector Accounting Standard IPSAS 4, “The Effects of Changes in Foreign Exchange Rates” is drawn primarily from International Accounting Standard IAS 21, “The Effects of Changes in Foreign Exchange Rates” (revised in 2003, as amended in 2005). The main differences between IPSAS 4 and IAS 21 are as follows:

- Commentary additional to that in IAS 21 has been included in paragraphs 11, 13, 26, 45, 67, 68, 72 of IPSAS 4 to clarify the applicability of the standards to accounting by public sector entities.
- IPSAS 4 uses different terminology, in certain instances, from IAS 21. The most significant examples are the use of the terms “revenue,” “economic entity,” “statement of financial performance,” “statement of financial position” and “net assets/equity” in IPSAS 4. The equivalent terms in IAS 21 are “income,” “group,” “income statement,” “balance sheet” and “equity.”⁴
- IPSAS 4 contains an additional transitional provision allowing an entity, when first adopting IPSASs, to deem cumulative translation differences existing at the date of first adoption of accrual IPSASs as zero (paragraph 67). This transitional provision is adapted from IFRS 1, “First-time Adoption of International Financial Reporting Standards.”

⁴ Note that the IASB’s ED issued in March 2006 of proposed amendments to IAS 1 *Presentation of Financial Statements* proposed changes in some terms, which will result in changes in terms used in other IFRSs/IASs, including IAS 21. Once IAS 1 is issued, any changes required as a result will be made prior to the issuance of amended IPSAS 4.