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Lack of Exchangeability – What is Changing?

Ind AS 21 (*The Effects of Changes in Foreign Exchange Rates*) – *inter alia* - sets out the exchange rate that an entity uses when it reports foreign currency transactions or balances in the functional currency, translates the results and financial position of a foreign operation in a different currency, or translates its own results and financial position into a presentation currency.

Until the recent amendment in May 2025, paragraph 26 of Ind AS 21 specified the exchange rate to be used when exchangeability between two currencies is temporarily

lacking; however, it didn't provide specific guidance for situations where lack of exchangeability was not temporary.

This article seeks to provide an insight on what has changed after the recent amendment to Ind AS 21 and how the revised Standard helps entities (a) assess whether a given currency is exchangeable into another currency, and (b) determine the spot exchange rate when exchangeability is lacking. The article also sheds light on the key disclosure requirements arising from the amendment.

Introduction and Background

At the outset, it may be recalled that IAS 21 *The Effects of Changes in Foreign Exchange Rates* and the corresponding converged Indian Accounting Standard (Ind AS 21) provide guidance on the exchange rate that an entity uses, when:

- it reports foreign currency transactions or balances in the functional currency;
- it translates the results and financial position of a foreign operation in a different currency; and
- it translates its results and financial position into a presentation currency.

Before the recent amendment, these Standard provided guidance on the exchange rate to be used when exchangeability between two currencies was *temporarily lacking*. However, there was no explicit guidance on the determination of the exchange rate when the lack of

exchangeability was *not temporary*. Accordingly, this led to diversity in practice.

Genesis of the Issue

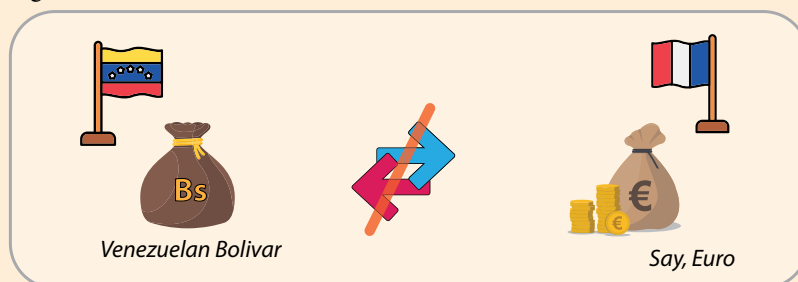
The genesis of the amendment lies in a submission received by the IFRS Interpretations Committee regarding how to determine the exchange rate when there is a long-term lack of exchangeability. The question before the IFRS IC arose from a specific situation faced by an entity in the context of its operations in Venezuela.

Accordingly, the IFRS IC recommended that the International Accounting Standards Board (IASB) develop a narrow-scope amendment to IAS 21 to address this issue.

Developments at the Standard-Setting Bodies

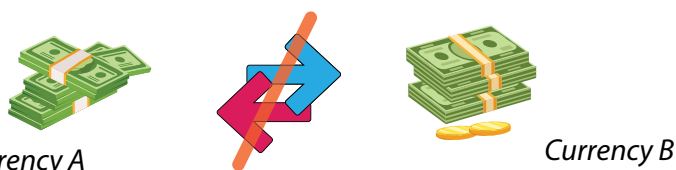
Following the above recommendation, the IASB issued amendments to IAS 21 in August 2023, specifically addressing the issue of lack of exchangeability. Subsequently, corresponding amendments to Ind AS 21 were considered and formally issued by the Ministry of Corporate Affairs (MCA)

Fig. 1



Source: Self-compiled

Fig. 2



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on 7th May 2025. These amendments reflect the standard-setters' response to extensive feedback from users of financial statements, who had raised concerns regarding the inconsistency in accounting practices in situations involving a lack of exchangeability between currencies, as illustrated in Fig. 2.

Moreover, the amendment requires an entity to provide more useful information in their financial statements when a currency cannot be exchanged into another currency.

Key Requirement under the Amendment

The amendments mainly require an entity to:

- assess (i) when a currency is exchangeable into another currency; and
- estimate the spot exchange rate when a currency is not exchangeable into another currency.

This is illustrated in Fig. 3.

The amendment also includes application guidance to (i) assist

“When evaluating whether a currency is exchangeable into another currency, the entity must assess its ability to obtain the other currency, rather than its intention or decision to do so.”

entities in assessing whether a currency is exchangeable into another currency, and (ii) support the estimation of the spot exchange rate when a currency is determined to be not exchangeable. In addition, the amendment requires entities to provide *specific disclosures* in cases where the spot exchange rate is estimated due to a lack of exchangeability between currencies.

How to Apply the Two-step Approach under the Amendment – a Deep Dive:

Step 1: Determining whether the currency is exchangeable into another currency

The amendment introduces a definition of the term 'exchangeable' in paragraph 8. According to the requirements of paragraph 8, a currency is considered exchangeable into another currency when the entity is:

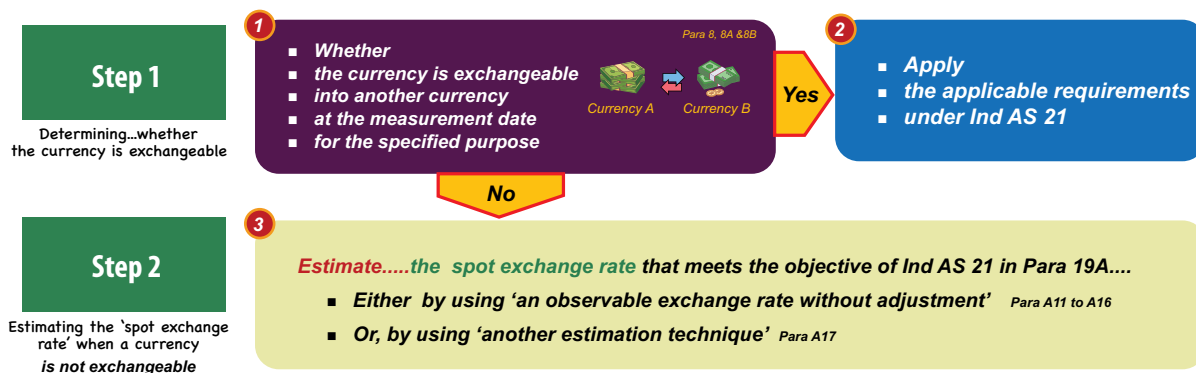
- able to obtain the other currency;
- within a timeframe that reflects a normal administrative delay;
- through a market or exchange mechanism; and
- where the exchange transaction results in enforceable rights and obligations.

Paragraph 8A further clarifies that the assessment of exchangeability must be performed (i) at the measurement date and (ii) for a specified purpose.

In addition, paragraph 8B states that a currency is *not considered* exchangeable into another currency if, at the measurement date and for the specified purpose, the entity can obtain *no more than an insignificant amount of the other currency*. For example, if an entity with the Venezuelan Bolivar as its functional currency has liabilities denominated in euros, it must assess whether the '*total amount of euros obtainable for the purpose of settling those liabilities*' is no more than an insignificant amount relative to the '*aggregate amount of its euro-denominated liabilities*'.

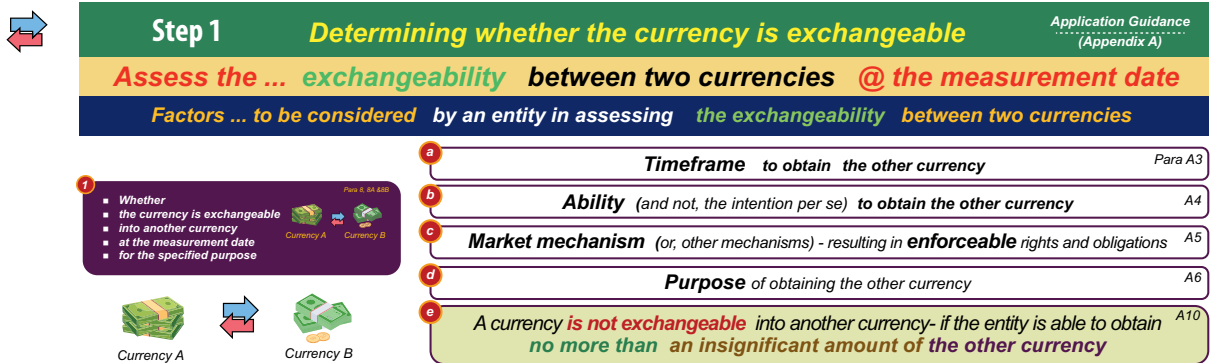
In this regard, it is relevant to note that paragraphs A3 to A10 of Appendix A provide application guidance to assist entities in evaluating whether a

Fig. 3



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Fig. 4



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currency is exchangeable into another currency.

Fig. 4 summarises the key requirements outlining how an entity can assess the exchangeability of a currency.

As can be appreciated from the above, an entity takes into account the following factors when assessing exchangeability of a currency:

Time Frame to Obtain the Other Currency

- Paragraph 8 defines a spot exchange rate as the exchange rate applicable to immediate delivery.
- The amendment clarifies that the existence of a normal administrative delay in obtaining the other currency does not, in itself, prevent a currency from being considered exchangeable into that other currency.
- Further, the determination of what constitutes a normal administrative delay is based on the specific facts and circumstances.

“When a currency is determined to be not exchangeable into another currency at the measurement date for a specified purpose, paragraph 19A of the amended standard mandates that the entity must estimate the spot exchange rate as at the measurement date.”

Ability to Obtain the Other Currency

- When evaluating whether a currency is exchangeable into another currency, the entity must assess its *ability to obtain the other currency, rather than its intention or decision* to do so.
- Additionally, the amendment clarifies that a currency is considered exchangeable into another currency if the entity is able to obtain the other currency, whether directly or indirectly.

Market (or Other Mechanisms) Resulting in Enforceable Rights and Obligations

- The amendment clarifies that, in assessing whether a currency is exchangeable into another

currency, an entity must consider *only those markets or exchange mechanisms* in which a transaction to exchange the currency for the other currency would result in *enforceable rights and obligations*.

- Furthermore, as enforceability is a legal matter, the determination of whether an exchange transaction in a particular market or exchange mechanism gives rise to enforceable rights and obligations depends on the *specific facts and circumstances*.

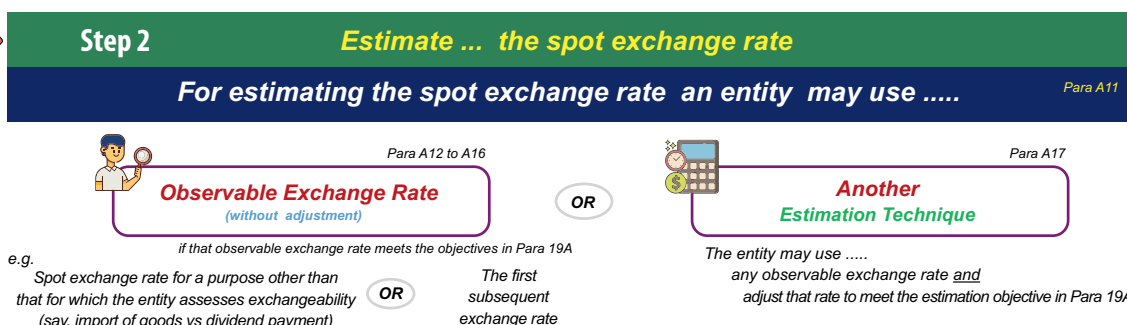
Purpose of Obtaining the Other Currency

- The amendment clarifies that multiple exchange rates may exist for different uses of a currency. As a result, a currency may be exchangeable into another currency

Table 1.

Type of Transaction	Purpose in Obtaining the Other Currency
Reporting foreign currency transactions in the entity's functional currency	To realise or settle individual foreign currency transactions, assets, or liabilities
Translation to a presentation currency other than the entity's functional currency	To realise or settle individual foreign currency transactions, assets, or liabilities
Translation of the results and financial position of a foreign operation into the presentation currency	To realise or settle its net investment in the foreign operation

Fig. 5



Source: Self-compiled

for certain purposes, but not for others.

- Consequently, when assessing exchangeability, the entity is required to determine its purpose in obtaining the other currency, based on the nature of the underlying transaction, as illustrated in Table 1.
- Also, an entity is required to assess exchangeability of a currency into another currency separately for each purpose.

Ability to Obtain Only Limited Amounts of the Other Currency

- The amendment clarifies that a currency is not considered exchangeable into another currency if, for a specified purpose (e.g., paying dividends), the entity is able to obtain no more than an insignificant amount of the other currency.
- For this assessment, the significance of the amount obtained is evaluated by comparing that amount with the total amount of the other currency required for the specified purpose.

Step 2: Estimating the Spot Exchange Rate when a Currency is not Exchangeable into Another

When a currency is determined to be not exchangeable into another currency at the measurement date for a specified purpose, paragraph 19A of the amended standard mandates that the entity must estimate the spot

exchange rate as at the measurement date.

Further, the newly inserted paragraph 19A specifies the objective in estimating the spot exchange rate as follows (emphasis added):

'... An entity's objective in estimating the spot exchange rate is to reflect the rate at which an orderly exchange transaction would take place at the measurement date between market participants under prevailing economic conditions.'

However, the standard does not prescribe detailed requirements for how an entity should estimate the spot exchange rate to meet the objective outlined in paragraph 19A. Instead, it establishes a framework that enables the entity to determine the spot exchange rate as at the measurement date.

Accordingly, paragraph A11 of the application guidance in Appendix A specifies that an entity can use:

- (i) an observable exchange rate without adjustment

e.g. (i) spot exchange rate for a purpose other than that for which an entity assesses exchangeability or (ii) the first exchange rate at which an entity is able to obtain the other currency for the specified purpose after exchangeability of the currency is restored;

or

- (ii) another estimation technique (say, any observable exchange rate adjusted as necessary to meet the objective of paragraph 19A).

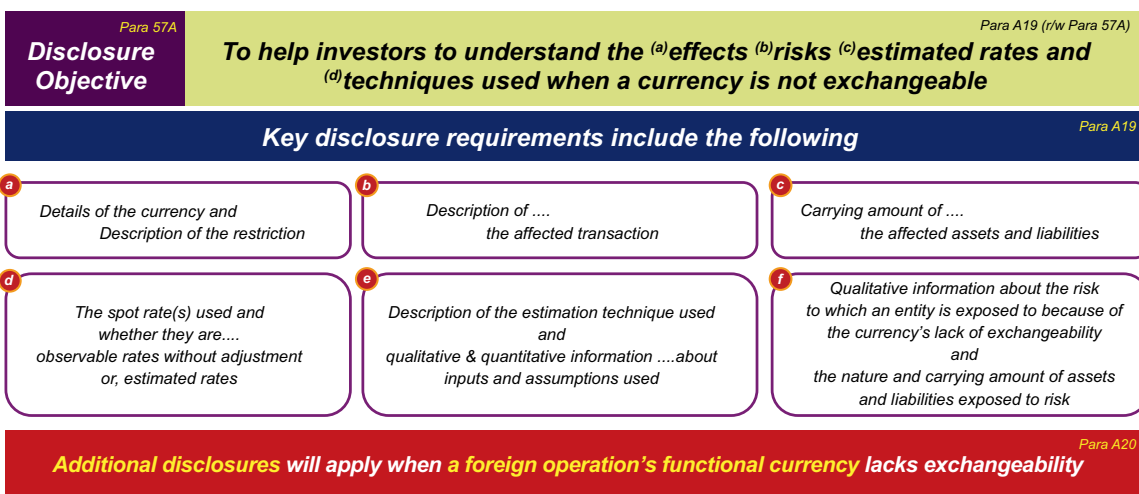
Fig. 5 summarises the key requirements on how an entity can go about estimating the spot exchange rate when a currency is not exchangeable into another.

In jurisdictions experiencing a prolonged lack of exchangeability, it is important to recognize that certain markets or exchange mechanisms such as unofficial or parallel markets may exist without creating enforceable rights and obligations. When assessing whether a currency is exchangeable under Step 1, entities must disregard the availability of the currency in such unofficial markets or mechanisms.

However, if an entity determines under Step 1 that the currency is not exchangeable at the measurement date for a specific purpose and therefore proceeds to Step 2 to estimate the spot exchange rate at that date and for that purpose, it may then refer to observable exchange rates from transactions in unofficial markets or mechanisms that do not establish enforceable rights and obligations. Such observable rates may be used, with appropriate adjustments.

Additionally, in formulating the amendments, the standard-setters have deliberately chosen not to prescribe a hierarchy of observable exchange rates for estimating the spot exchange rate. Although a hierarchy could enhance consistency, it was considered that doing so might introduce unnecessary costs without yielding more useful information.

Fig. 6



Source: Self-compiled

Consequently, while the amendments define a clear objective for estimating the exchange rate, they allow entities discretion in selecting an appropriate approach, based on their specific circumstances.

Key Disclosure Requirements

The amendment has introduced *additional disclosure requirements* when an entity estimates a spot exchange rate because a currency is not exchangeable into another currency. The overarching objective of the new disclosure requirements (as stipulated in paragraph 57A) is 'to enable users of its financial statements to understand how the currency not being exchangeable into the other currency affects, or is expected to affect, the entity's financial performance, financial position and cash flows'.

Put differently, the new disclosure requirements under the amended standard seek to help investors in better understanding the effects, risks and estimated rates and techniques used when a currency is not exchangeable.

Fig 6. summarises the key disclosure requirements under the amended standard (as contemplated under paragraphs A19 and A20 of Appendix A (containing the application guidance).

Effective Date and Transition

From an IFRS perspective, an entity shall apply the amendments for annual reporting periods beginning on or after 1st January 2025 (with earlier application permitted). However, preparers of financial statements applying Ind AS 21 shall apply the amendments for annual reporting periods beginning on or after 1st April 2025 (no provision for earlier application). The date of initial application is the beginning of the annual reporting period in which an entity first applies those amendments and in applying the amendments, an entity is *not permitted* to restate comparative information.

Key Impact and Conclusion

The amendment provides helpful guidance on accounting for a lack of exchangeability and is expected to reduce existing diversity in practice, especially in countries facing currency controls or hyperinflation. While applying the requirements of the amended standard, entities will need to make significant judgement and have a good understanding of the facts and circumstances relating to currencies that suffer from a lack of exchangeability. This will also require entities to evaluate the changes required in

their systems and processes to comply with the requirements of the revised standard (including the disclosure requirements). Since entities are expected to exercise significant judgement, both in assessing exchangeability and in estimating exchange rates, a robust documentation of assumptions, data sources, and rationale will be critical for auditability and regulatory scrutiny. Entities will be required to use a consistent approach when assessing whether a currency can be exchanged into another currency. If this is not possible, entities will be under obligation to provide the required disclosures explaining how the alternative exchange rate was determined, within the framework provided under the amended standard. The amendment provides guidance that will increase the comparability between financial statements and provide more useful information to the user.

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