Applying the proposed two-step approach

Step 1 - Assessing exchangeability

When assessing whether a currency is exchangeable into the other currency, a company would need to consider the following.

- **Time frame** – a normal administrative delay does not preclude a currency from being exchangeable.
- **Ability** – exchangeability is based on the ability to obtain the other currency, not the intention or decision to do so. Therefore, theoretical prices with little or no liquidity in the market would not suffice.
- **Markets or exchange mechanisms** – does the method used to exchange a currency create enforceable rights and obligations? An unofficial or 'black market' could therefore be inappropriate.
- **Purpose** – an official rate might be available for purchasing certain essential goods but not for capital remittance (e.g. dividend payments).This observable rate could be used to translate liabilities for purchasing these essential goods but not for translating shareholder liabilities.
- **Amount** – consider the amount of other currency that it can obtain for a specific purpose in relation to the total amount it requires for that purpose.

Step 2 - Determining an estimated spot rate

Paragraph 19A of IAS 21 would require an estimated spot rate to:

- be accessible if the currency is exchangeable;
- be applied between market participants in an orderly transaction; and
- faithfully reflect the prevailing economic conditions.

A company could use an observable rate relating to another purpose to estimate a rate when exchangeability for a specific purpose is lacking. Further, if exchangeability for *all* purposes is lacking temporarily but resumes after the measurement date, then a company could use that first subsequent exchange rate as its estimated rate. Any estimated rate would need to meet the requirements in paragraph 19A of IAS 21 *The Effects of Changes in Foreign Exchange Rates*.

KPMG