INTERNATIONAL PRACTICES TASK FORCE
Center for Audit Quality Washington Office
November 18, 2014
HIGHLIGHTS

I. Attendance

<u>Task Force Members</u>
Jonathan Guthart, Chair (KPMG)
Cathy Samsel, Vice-Chair (PwC)
Randall Anstine, (Ernst & Young)
Greg Bakeis (PwC)
Rich Davisson (McGladrey & Pullen)
Steven Jacobs (Ernst & Young)
Debra MacLaughlin (BDO USA), via teleconference
Victor Oliveira (Ernst & Young)
Scott Ruggiero (Grant Thornton)
Sondra Stokes (Deloitte & Touche)

<u>Observers</u>
Jill Davis (SEC Staff)
Paul Dudek (SEC Staff)
Ryan Milne (SEC Staff)
Craig Olinger (SEC Staff)
Susan Brooke (Center for Audit Quality Staff)
Kevin Lavin (Center for Audit Quality Staff)
Annette Schumacher Barr (Center for Audit Quality Staff)

<u>Guests</u>
Ignacio Perez (Deloitte & Touche)
Guilaine Saroul (PwC)
Robert Sledge (KPMG)

II. Current Practice Issues

A. Venezuela Currency Issues

See Section IIA in the May 21, 2014 IPTF Highlights for a discussion of Venezuela currency issues, and the disclosures that should be considered by registrants with significant operations in Venezuela. The SEC staff re-acknowledged at the November 18, 2014 meeting that the determination of the appropriate exchange rate to be used for the re-measurement of Venezuela currency should be based on a company's individual facts and circumstances.

B. Monitoring Inflation in Certain Countries

Introduction

Registrants are responsible for monitoring inflation in countries in which they have operations. Application of "highly-inflationary" accounting as defined by ASC 830 is a judgment to be made by the financial statement preparer. The approach and the related assumptions used to monitor country inflation rates are described below. Under ASC paragraph 830-10-45-12, the determination of a highly-inflationary economy begins by calculating the cumulative inflation rate for the three-year period that precedes the beginning of the reporting period, including interim reporting periods. If that calculation results in a cumulative inflation rate in excess of 100%, the economy should be considered highly-inflationary in all instances. However, if that calculation results in the cumulative rate being less than 100%, historical inflation rate trends and other pertinent factors should be considered.

The Task Force discussed three-year cumulative inflation rates for certain countries. Countries were categorized as follows:

1. Countries with three-year cumulative inflation rates exceeding 100%

2. Countries where the three-year cumulative inflation rates had exceeded 100% in recent years

3. Countries (a) with three-year cumulative inflation rates between 70% and 100%; (b) where the last known three-year cumulative inflation rates previously exceeded 100% and current actual inflation data has not been obtained; or (c) with a significant increase in inflation during the current period

Description of how inflation rates are calculated

For all countries, data is extracted from the International Monetary Fund ("IMF") website. IMF data is extracted from www.imf.org as follows:

On the home page, select the "Data and Statistics" tab and then click:

- "World Economic Outlook Databases (WEO)" link
    - ◦ Select the most recent database
    - ▪ Select "By Countries (country-level data)"
        - • Select "All Countries", then click the "continue" button.
            - ◦ Select "Inflation, end of period consumer prices" (both the index and percent change)
                - ▪ Select a date range (e.g., 2010-2014); click "prepare report" and a table is produced with the data; click the "download" link to export to excel. The data table includes the actual and estimated end of period price indices for each country.

The IMF World Economic Outlook ("WEO") report estimates inflation when actual inflation data has not been obtained. The text of the report describes the assumptions and conventions used for the projections in the WEO. The data that are estimated are highlighted. While the IMF data has limitations (projected inflation data and varying dates through which actual data is included in the table), the calculated three-year cumulative inflation allows us to determine which country's calculations require further analysis.

> Note: From time to time the WEO refines or updates previously reported actual Consumer Price Index (hereafter referred to as "Index" or "CPI") data for certain countries.

Using the downloaded table, the three-year cumulative inflation rate is calculated as follows (assuming the current year is end of year 2014): (2014 End of Year CPI– 2011 End of Year CPI) / 2011 End of Year CPI.

It should be noted that the IMF inflation data used to summarize inflation for these IPTF Highlights could be different from the inflation data reported by the respective countries' central banks or governments. The Task Force has not performed procedures to identify any potential differences. Accordingly, this summarized IMF information should be supplemented, to the extent considered necessary, with other pertinent information that may be available.

For registrants that need additional information to monitor inflation for operations in certain countries, it should be noted that annual or month-end CPI information can be obtained from some countries' central bank or government websites or other publicly available information but that data may differ from the inflation data reported by the IMF and may need to be converted because of differences in presentation or other reasons (for example, some countries have reset their base index back to 100 during recent years). While inflation data published by a central bank or government is often more current than the IMF data, each country releases its inflation data at different times and inflation data for some countries may not be otherwise publicly available.

The following information, based on the WEO Database – October 2014, is provided to assist registrants in applying the US GAAP guidance in determining which countries are considered highly-inflationary:

1. Countries with three-year cumulative inflation rates exceeding 100%

- **Belarus -** The three-year cumulative rate as of the end of 2013 was 196% and is projected to be 68% by the end of 2014.

  The three-year cumulative inflation rate at the end of 2013 of 196% was primarily influenced by the high inflation experienced in 2011 of 109% (the CPI index increased from 169.88 at December 31, 2010 to 354.51 at December 31, 2011, and was at 502.80 at the end of December 31, 2013). Accordingly, the economy of Belarus may transition out of highly-inflationary status in 2014.

  The staff would expect registrants to monitor Belarus' reported inflation data to determine when it is appropriate to cease treating the economy as highly-inflationary.

- **Islamic Republic of Iran** – The three year cumulative inflation rate, using the data in the WEO Report was 104% as of the end of 2013 and is projected to be 103% by the end of 2014.

  As indicated in the November 19, 2013 IPTF Highlights, the staff expects registrants to begin treating the economy of Islamic Republic of Iran as highly-inflationary no later than the first reporting period beginning on or after January 1, 2014.

- **Venezuela** - The three-year cumulative inflation rate for Venezuela was 139% for 2013 and the three-year cumulative inflation rate at the end of 2014 is projected to be 218%.

  Based on these inflation rates and discussions with the staff, registrants should continue to treat the economy of Venezuela as highly-inflationary.

- **Sudan** – According to the WEO report, Sudan's cumulative three year inflation rate was 144% at the end of 2013 and is projected to be 164% by the end of 2014. Sudan's data excludes South Sudan after July 9, 2011. Rates for 2012 and onward pertain to the current Sudan.

  As discussed in the May 21, 2014 IPTF Highlights, based on these inflation rates and discussions with the staff, the economy of Sudan should be treated as highly-inflationary no later than the first reporting period beginning on or after January 1, 2014. Registrants that have already issued financial statements for interim periods beginning on or after January 1, 2014 which do not reflect the economy of Sudan as highly-inflationary are encouraged to discuss their facts and circumstances with the SEC staff to the extent a change to highly inflationary would be significant.

2. Countries where the three-year cumulative inflation rates had exceeded 100% in recent years

- **South Sudan** –South Sudan, which became independent of Sudan in July 2011, became a member of the IMF in 2012. Although complete data was not yet available to calculate a three-year cumulative inflation rate through the end of 2012, the two-year cumulative inflation rate was 107% at the end of 2012, based on the index data published at that time in the WEO Report and by the South Sudan National Bureau of Statistics (SSNBS). Data from the October 2013 WEO report and the South Sudan National Bureau of Statistics (SSNBS) had projected three-year cumulative inflation of 129% by the end of 2013.

  However, the actual three-year cumulative inflation rate through the end of 2013 was calculated to be 89%, based on the reported index data in the WEO Report and by the South Sudan National Bureau of Statistics (SSNBS). The three-year cumulative inflation rate is projected to be 23.2% by the end of 2014.

  As indicated in the May 2014 IPTF Highlights based on these inflation rates and discussions with the staff, registrants should cease treating the economy of South Sudan as highly-inflationary as soon as practicable, but no later than the first reporting period beginning on or after April 1, 2014.

3. Countries (a) with projected three-year cumulative inflation rates between 70% and 100%; (b) where the last known three-year cumulative inflation rates previously exceeded 100% and current actual inflation data has not been obtained; or (c) with a significant increase in inflation during the current period

(a) Countries with projected three-year cumulative inflation rates between 70% and 100%

- **Malawi** – The three-year cumulative inflation rate for Malawi was 83% for 2013 and is projected to be 91% by the end of 2014.

(b) Countries where the last known three-year cumulative inflation rates previously exceeded 100% and current actual inflation data has not been obtained

None.

(c) Countries with a significant increase in estimated inflation during 2013

None, outside of countries already discussed above.

<u>Notes:</u>

- **Argentina**

Argentina had an estimated three year cumulative inflation rate of 35% in 2013. The consumer price projections for Argentina were excluded from the October 2014 WEO data because of a "structural break in the data" with the following explanation:

Consumer price data from January 2014 onwards reflect the new national CPI (IPCNu), which differs substantively from the preceding CPI (the CPI for the Greater Buenos Aires Area, CPI-GBA). Because of the differences in geographical coverage, weights, sampling, and methodology, the IPCNu data cannot be directly compared to the earlier CPI-GBA data. Because of this structural break in the data, staff forecasts for CPI inflation are not reported in the Fall 2014 World Economic Outlook. Following a declaration of censure by the IMF on February 1, 2013, the public release of a new national CPI by end-March 2014 was one of the specified actions in the IMF Executive Board's December 2013 decision calling on Argentina to address the quality of its official CPI data. On June 6, 2014, the Executive Board recognized the implementation of the specified actions it had called for by end-March 2014 and the initial steps taken by the Argentine authorities to remedy the inaccurate provision of data. The Executive Board will review this issue again as per the calendar specified in December 2013 and in line with the procedures set forth in the Fund's legal framework.

The Task Force discussed the following observations related to Argentina:

- The reported three-year inflation based on the consumer price index for the Greater Buenos Aires Area (CPI-GBA) was 35% for calendar 2013.
- Last year the IMF highlighted Argentina in the World Economic Outlook (WEO) report, as follows:

    > The IMF issued a declaration of censure and called on Argentina to adopt remedial measures to address the quality of the official CPI-GBA data. The IMF noted that alternative data sources have shown considerably higher inflation rates than the official data since 2008. In this context, the IMF is also using alternative estimates of CPI inflation for the surveillance of macroeconomic developments in Argentina.
- Argentina responded to the IMF's concerns by discontinuing the CPI-GBA, and from January 2014 onwards reports the new national CPI (IPCNU), which differs substantively from the preceding CPI-GBA as noted above.

- Inflation reported in 2014 for the IPCNU was as follows:
  January - 3.7%
  February – 3.4%
  March – 2.6%
  April – 1.8%
  May – 1.4%
  June – 1.3%
  July – 1.4%
  August – 1.3%
  September – 1.4%
  October – 1.2%

  The IPCNU is only available for January 2014 and subsequent periods, and not considered to be determined on the same basis as CPI-GBA data.

The SEC staff noted the IMF's concerns on the accuracy of CPI-GBA data for 2013 and prior periods. Given the apparent lack of any other objectively verifiable inflation data, and the relatively low level of three-year cumulative inflation, the SEC staff had not observed data that supported Argentina being highly inflationary in 2013.

Additionally, the SEC staff noted that it had not observed objectively verifiable data that would indicate the economy of Argentina is highly-inflationary at October 31, 2014. However, the staff noted that an annual projection of the reported inflation during the first seven months of 2014 as per IPCNU would be higher than projections using the previous inflation reported by CPI-GBA.

The staff would expect registrants to monitor the IPCNU inflation data during the remainder of 2014 and consider the level of inflation, in combination with other pertinent factors and data points, in determining whether Argentina should be considered a highly-inflationary economy.

- **Countries not analyzed in the IMF WEO report**

  There may be additional countries with three-year cumulative inflation rates exceeding 100% or that should be monitored which are not included in the above analysis because the sources used to compile this list do not include inflation data for all countries or current inflation data. One such country, for example, is Syria. Numerous other countries that are not members of the IMF are not included in the WEO reports.

III. Staff Matters

A. Definition of a Foreign Business

The staff noted that they have observed instances in which joint venture entities (not incorporated in the U.S.) that were 50% owned by a US company, and 50% owned by persons who were not citizens or residents of the United States, were reported as if they were "foreign businesses" for S-X Rule 3-09 purposes. In these situations, the non-US investor did not consolidate the joint venture entity, but followed the equity method accounting for its interest.

The staff noted that these entities do not qualify as foreign businesses, as they do not meet the "majority owned by persons who are not citizens or residents of the United States" criteria of S-X 1-02(1). The majority owned criteria is usually viewed as the majority of voting shares. However, as provided in the Note to Financial Reporting Manual (FRM) paragraph 6110.4, in its determination of the majority ownership of a business, the staff will consider the ultimate parent entity that would consolidate the business under U.S. GAAP (or IFRS as issued by the IASB for such preparers) and that parent's controlling shareholders.

If financial statements of a joint venture that does not qualify as a "foreign business" are required to be provided to comply with either S-X Rule 3-09 or Rule 3-05, such financial statements must be either prepared under US GAAP, or reconciled to US GAAP under Item 18 of Form 20-F for all years. In contrast, if the entity qualified as a "foreign business", such financial statements are permitted to comply with Item 17 of Form 20-F, which limits reconciliation to US GAAP for acquiree or investee entities whose significance exceeds 30% (for financial statements prepared on a basis other than US GAAP or IFRS as issued by the IASB), and provides that no reconciliation to US GAAP is required for financial statements prepared under IFRS as issued by the IASB, regardless of significance. Consistent with the guidance in FRM paragraph 6410.9, if an acquiree or investee that presents financial statements under IFRS as issued by the IASB does not qualify as a foreign business, but does meet the definition of a foreign private issuer, CF-OCA will consider requests for relief from the US GAAP reconciliation requirement.

(See the Division of Corporation Finance, Financial Reporting Manual (FRM) paragraphs 6110.4 and 6410.9, respectively.)

B. Status update of the staff's Disclosure Effectiveness Initiative

The staff discussed the current project underway at the SEC to review the effectiveness of existing disclosure requirements in Regulation S-K and Regulation S-K. They noted the Division of Corporation Finance is working on potential modifications and improvements in Regulation S-K, and is evaluating Regulation S-X, in particular the non-issuer entity financial statements under Rules 3-05, 3-09, 3-10, and 3-16. In this effort, the staff is looking at existing rules and considering whether there is a better way to provide information to investors regarding acquirees, investees and other non-issuers. For example, the staff is exploring whether more emphasis should be given to pro forma rather than historical information. In addition, the staff is exploring potential options to change the way significance is tested. The staff noted that it would expose for public comment any proposed rule changes before they are implemented. In the meantime, the staff continues to welcome comments and suggestions from the public, including matters related to Form 20-F requirements. Comments may be submitted using the staff's online form or by email at rule-comments@sec.gov.

C. Staff Observations Regarding the Use of IFRS XBRL Taxonomy by FPIs

The staff noted that the SEC has not yet approved XBRL Taxonomy for IFRS as issued by the IASB and the staff does not plan on approving such a taxonomy for this calendar year. IFRS filers cannot comply with XBRL until the SEC approves the XBRL Taxonomy.

IV. Next Meeting

The next meeting of the Task Force has been set for May 19, 2015.