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# Recent Developments Related to the Classification of Argentina as a Highly Inflationary Economy Under U.S. GAAP

This *Financial Reporting Alert* highlights recent developments related to the classification of Argentina's economy as highly inflationary. As discussed below, we would expect entities to account for Argentina as a highly inflationary economy under ASC 830<sup>1</sup> beginning no later than July 1, 2018. This alert will be updated in the future to reflect new developments, as warranted.

## Background

Argentina has continued to experience negative economic trends, as evidenced by (1) multiple periods of increasing inflation rates, (2) devaluation of the peso, and (3) increasing borrowing rates, requiring the Argentinian government to take mitigating actions.

Three-year cumulative estimated consumer price index (CPI) inflation, which is based on published data about Argentina, has consistently exceeded 100 percent since September 2017; however, the wholesale price index (WPI) has not been above 100 percent until May 2018, as discussed below. Because of the lack of consistent monthly reporting of CPI data, various CPIs — such as the City of Buenos Aires index (IPC-BA), the San Luis province index (IPC-SL), and a more recently established national CPI — have been used to obtain three years of comparative CPI data. The IPC-BA and IPC-SL indexes are specific to the city of Buenos Aires

<sup>1</sup> FASB Accounting Standards Codification (ASC) Topic 830, *Foreign Currency Matters*.

and the province of San Luis, respectively, whereas the historical Greater Buenos Aires Area index (CPI-GBA) encompasses the Greater Buenos Aires Metropolitan Region. In accordance with this data, the three-year cumulative CPI, which blends the historical IPC-BA or IPC-SL indexes with the applicable national CPI, has exceeded 100 percent since September 2017 and December 2017, respectively. Furthermore, if a blended approach is used, the three-year cumulative CPI (including the national CPI) has exceeded 100 percent since September 2017.

The Center for Audit Quality's (CAQ's) International Practices Task Force (IPTF) has also closely monitored the WPI. At its November 2017 [meeting](#) with the SEC staff, the IPTF referred to the [discussion document](#), *Monitoring Inflation in Certain Countries*, which stated that "the WPI has consistently provided national coverage and historically has been viewed as the most relevant and reliable inflation measure by practitioners since Argentina moved to International Financial Reporting Standards (IFRS)." As of that meeting, the latest three-year cumulative WPI data as of September 30, 2017, showed the index at 74 percent. The WPI has continued to increase and, as of the May 2018 IPTF meeting, had reached 95 percent. The May 2018 WPI data released on June 14, 2018, shows that the WPI increased to 7.5 percent for the month, resulting in a three-year cumulative WPI of approximately 109 percent as of May 2018.

The first two columns in the table below contain the three-year cumulative inflation rates published by the CAQ IPTF in the May 2018 edition of its [discussion document](#) for the periods ended December 31, 2017, and March 31, 2018. The second two columns show inflation data for the periods ended April 30, 2018, and May 31, 2018, computed on the basis of monthly inflation information published by the [Instituto Nacional de Estadística y Censos de la República Argentina \(INDEC\)](#).

<b>Three-Year Cumulative Indexes</b>	<b>12/31/2017</b>	<b>3/31/2018</b>	<b>4/30/2018</b>	<b>5/31/2018</b>
Various CPI Indexes:	106%	112%	116%	118%
CPI-GBA				
National CPI (IPCNu)				
IPC-BA				
New CPI-GBA				
New national CPI				
Same as above, except the IPC-SL replaces the IPC-BA	104%	110%	114%	116%
WPI	77%	95%	97%	109%

## Highly Inflationary Status

ASC 830-10-45-12 states that the "determination of a highly inflationary economy must begin by calculating the cumulative inflation rate for the three years that **precede the beginning of the reporting period**" (emphasis added). On the basis of currently available data related to inflation, we would expect entities to account for Argentina as a highly inflationary economy under ASC 830 beginning no later than July 1, 2018. Accordingly, entities with a year-end or quarter-end as of June 30, 2018, that have not previously considered Argentina's economy to be highly inflationary should consider its economy to be highly inflationary no later than July 1, 2018. As a result, the financial statements of Argentinian entities will need to be remeasured as if the functional currency were the reporting currency no later than July 1, 2018.

ASC 830-10-45-11 defines a highly inflationary economy as one with a cumulative inflation rate of approximately 100 percent or more over a three-year period. ASC 830-10-45-12 provides additional interpretative guidance on determining whether an economy is highly inflationary.

Under ASC 830, if a country's economy is classified as highly inflationary, a foreign entity operating in that country whose functional currency was the foreign currency is required to change its functional currency to that of its immediate parent company for consolidation purposes.

Once a country's economy is classified as highly inflationary, a decrease in the cumulative three-year rate below 100 percent does not necessarily automatically mean that the country's economy is no longer highly inflationary. ASC 830-10-55-25 (formerly Example B of Topic D-55<sup>2</sup>) describes a situation in which a country's economy should continue to be classified as highly inflationary because there is no evidence to suggest that a drop in the cumulative three-year rate below 100 percent is "other than temporary." Entities should continue to evaluate and assess the economic conditions in Argentina to determine whether a change in circumstance, such a cumulative decrease in the three-year inflation rate, is other than temporary.

## Disclosures

It is critical that entities with material operations in Argentina provide robust disclosures in the notes to the financial statements and, for registrants, in the "Description of Business," "Risk Factors," and MD&A sections of their SEC filings. Entities should also clearly document their accounting conclusions and their underlying rationale for them as part of their internal control review and assessment process.

A registrant should consider additional disclosures in its next current filing related to its Argentinian operations if such disclosures would be material to a user's understanding of the registrant's prospective financial position or performance. We recommend that entities disclose the following in MD&A, the financial statement footnotes, or both, as applicable:

- A description of the overall economic environment in Argentina and its effect on the entity's financial statements both historically and currently. This disclosure would include, as applicable, information about (1) inflation, (2) changes in the entity's revenues and associated costs, and (3) any triggering events, impairment indicators, or impairments.
- The extent of the entity's exposure to Argentinian operations. This disclosure would include the nature of the entity's activities in Argentina (e.g., imports, manufacturing, and size of operations) and other meaningful financial information such as disaggregated financial information about the Argentinian operations (e.g., summarized balance sheets, income statements, and cash flow statements).

Because of the complexity associated with these accounting and disclosure issues, we encourage entities with Argentinian operations to consult with their accounting advisers and legal counsel.

<sup>2</sup> EITF Topic No. D-55, "Determining a Highly Inflationary Economy Under FASB Statement No. 52."

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