Comprehensive Adjustment for Inflation

Finance and Accounting

Proyect
Microsoft Dynamics AX

Prepared for
AXXON

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SUMMARY

This document aims to describe the scope within the Argentine Localization of the legal and professional requirement of preparing financial statements in constant currency.

Professional accounting standards have enabled the restatement of financial statements in constant currency through Resolution JG539/18 of the Argentine Federation of Professional Councils in Economic Sciences, which enables the application of Technical Resolution No. 6.Legal norms support this criterion, with Law No. 27.468 establishing the preparation of financial statements in constant currency and authorizing regulatory bodies to receive said statements.

Additionally, the IFRS (International Financial Reporting Standards) require a restatement in constant currency of financial statements from entities whose functional currency is that of a hyperinflationary economy, defined as 100% cumulative inflation in three years. For the restatement of financial statements, the IAS 29 (International Accounting Standard) is applicable. The IAS 29 requires utilizing a price index that reflects the changes in the purchasing power of the currency.

FINANCIAL INFLATION ADJUSTMENT

This process aims to restate the accounts, mainly Income Statement and Capital, through a periodic routine:

The new routine:

- Will calculate monthly balances for those accounts specifically configured to Adjust for Inflation within the selected period.
- Will calculate and apply coefficients to those monthly balances in order to update them up to the Cut-off Date.
    - This is the amount of the Inflation Adjustment
- Will enable the creation of a Journal without registration so that the user can check the adjustment calculated and,
- Will allow to account for said adjustment in a separate layer from the historical accounting
- The goal is to separate historical accounting from inflation adjustments
- AX manages the concept of "layers" in which the accounting entry is registered. These layers exist in order to obtain reports which are filtered by them.
- Historical accounting in AX is entered into the accounts in the "Current" layer.
- We propose for Inflation Adjustment entries to be accounted for in a different layer, such as the "Operations" or "Taxes" layer, in order to maintain the information separated and to obtain reports:
    - With the historical accounting data, not adjusted for inflation.
    - With the historical accounting data PLUS the inflation adjustments;
    - Or displaying only the Inflation Adjustments, the entries registered in that separate layer.

FIXED ASSETS INFLATION ADJUSTMENT

This process aims to keep updated the value of Fixed Assets in said module and in the accounting, and to restate its original value as well as its amortization up to a cut-off date.

A new value model will be configured to be used in the registration of the adjustment entries, keeping them in a separate layer from the historical accounting.

A new proposal will be created within the Fixed Assets Journal termed "Inflation Adjustment Proposal" that will calculate two movements per each fixed asset using two new Types of Transactions:

- Inflation Adjustment for Acquisition
- Inflation Adjustment for Depreciation

This new proposal must be run every month immediately after executing the historical monthly depreciation:

- It will reverse every Inflation Adjustment for Acquisition and Inflation Adjustment for Depreciation calculated in the current calendar year.
- It will take the original value of the fixed asset, age it, and update it to the Cut-off Date in order to estimate its inflation adjustment
- It will take the original value plus the adjustment estimated in the previous step and will recalculate the accumulated amortization with that new value up to the Cut-off Date.
- It will register two accounting entries per Fixed Asset in the adjusted layer, one with the inflation adjustment of the original value, and another one with the inflation adjustment of the accumulated amortization.

In order to contemplate the impact in the accounting of the Sale or Write-off of the Fixed Asset, a "Derived Value Model" will be associated to the new adjusted value model. Thus, upon sale or write-off of a fixed asset with inflation adjustment entries, the adjustments made in the adjusted layer will be also written off.

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INVENTORY INFLATION ADJUSTMENT

This process aims to keep the Inventory module updated and, in the accounting, it aims to reflect in the Assets the value of the inventory, as well as the value at which those assets were sold or consumed in the Income Statement (Cost of Goods Sold or Consumption).

A new functionality will be added to the periodic routines of Inventory Closing and Adjustment that can only be executed after running Inventory Closings for the whole period of Adjustment for Inflation.

It will consist of two steps:

1. Inflation Adjustment for Inventory Incomings (Transaction Adjustment)
   a. It will survey all entries of merchandise of the accounting year for which the Inflation Adjustment is being estimated up to the cut-off date indicated, and will identify for each of them:
      i. The historical financial cost
      ii. The adjustment to the historical financial cost, since cost may have been adjusted from Availables Adjustment or Transaction Adjustment.
      iii. Previously estimated Inflation Adjustment, if any.
   b. Aging: every line of transaction will be associated to a month of origin that will be used to obtain the inflation rate of that moment.
   c. It will estimate an updating coefficient for every transaction, from its month of origin to the cut-off month, and will apply said coefficient to the sum of the Historical Cost plus the Historical Cost Adjustment.
   d. It will compare the number estimated in the previous step with the Inflation Adjustment previously estimated, if any.
   e. It will use the result of said comparison to register an entry in the Operations layer, in order to restate the inventory incoming in the constant currency of the cut-off date in which the process was run.
2. Inflation Adjustment for Inventory Outgoings (Re-estimation)
   a. It will survey all merchandise outgoings, whether for sale or consumption, of the accounting year for which the Inflation Adjustment is being estimated up to the cut-off date that were settled in the Closing Inventory, and will identify for each of them:
      i. The historical financial cost
      ii. The adjustment to the historical financial cost, since cost may have been adjusted from Availables Adjustment or Transaction Adjustment.
      iii. Previously estimated Inflation Adjustment, if any.
   b. It will identify the Inflation Adjusted Cost of the incoming associated to each outgoing that was estimated in the previous step.
   c. It will compare the Inflation Adjusted Cost of the incoming with the sum of the historical financial cost plus the Adjustment of the historical financial cost of the inventory outgoings. It will then compare said balance with the Inflation Adjustment estimated for said outgoing, if any.
   d. It will use the result of said comparison to register an entry in the Operations layer, in order to complement the cost of each outgoing and to restate it in the constant currency of thecut-off date.