Foreign Currency Financial Statement

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DIFFERENCE IN ACCOUNTING PRINCIPLES

1. Methods used to measure economic activity differ around the world
2. Benefits of adoption of a single set of globally accepted accounting standards
   - Expansion of capital markets across borders
   - Help investors to better evaluate opportunities across borders
   - Reduce reporting costs for companies accessing capital in other countries
   - Increased confidence for users

International Financial Reporting Standards (IFRS)

- Standards published by the International Accounting Standards Board (IASB)
- Widely accepted
- Mandated or permitted in over 100 countries
- FASB is working with the IASB to improve the quality of standards and to "converge" their two sets of standards

New SEC rules

- Allow foreign private issuers to file statements prepared in accordance with IFRS as issued by the IASB without reconciliation to U.S. GAAP (January 4, 2008)

Target date of 2011

- U.S. issuers would be required to prepare financial statements in accordance with IFRS

DETERMINING THE FUNCTIONAL CURRENCY

Date	Currency on Deposit	Current Exchange Rate	Dollar Equivalent
12/31/20X1	£100	$1.80	$180
12/31/20X2	100	1.70	170

Two major issues that must be addressed when financial statements are translated from a foreign currency into U.S. dollars are

1. Which exchange rate should be used to translate foreign currency balances to domestic currency?
2. How should translation gains and losses be accounted for? Should they be included in income?

FIGURE 12–1 Functional Currency Indicators

Indicator	Factors Indicating Foreign Currency (Local Currency) Is the Functional Currency	Factors Indicating U.S. Dollar (Parent's Currency) Is the Functional Currency
Cash flows	Primarily in foreign currency and do not affect parent's cash flows	Directly impact the parent's current cash flows and are readily available to the parent company
Sales prices	Primarily determined by local competition or local government regulation; not generally responsive to changes in exchange rates	Responsive to short-term changes in exchange rates and worldwide competition
Sales markets	Active local sales markets for company's products; possibly, significant amounts of exports	Sales markets mostly in parent's country, or sales contracts are denominated in parent's currency
Expenses	Labor, materials, and other costs are primarily local costs	Production components generally obtained from the parent company's country
Financing	Primarily obtained from, and denominated in, local currency units; entity's operations generate funds sufficient to service financing needs	Primarily from the parent, or other dollar-denominated financing
Intercompany transactions and arrangements	Few intercompany transactions with parent	Frequent intercompany transactions with parent, or foreign entity is an investment or financing arm for the parent

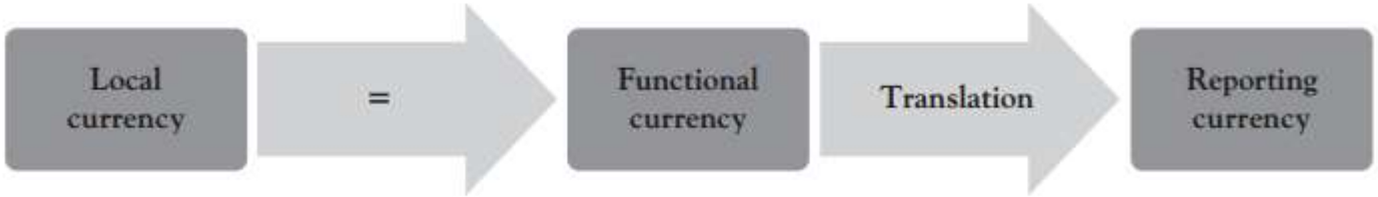
Functional Currency Designation in Highly Inflationary Economies

	Date of Construction		After Hyperinflation	
Amount (pesos)	**Rate**	**Translated Amount**	**Rate**	**Translated Amount**
1,000,000	$0.05	$50,000	$0.00005	$50

TRANSLATION VERSUS REMEASUREMENT OF FOREIGN FINANCIAL STATEMENTS

Three possible scenarios may require the restatement of financial statements from one currency to another via translation and/or remeasurement.

Case 1: The local currency is the functional currency. Simply translate the financial statements from the functional currency to the reporting currency. No further work is necessary because the consolidation and financial reports can now be prepared in the reporting currency.



Case 2: The local currency is not the functional currency, but the functional currency is the reporting currency. Simply remeasure the financial statements from the local currency to the functional currency. No further work is necessary because the consolidation and financial reports can now be prepared in the functional currency (because it is the reporting currency).

Case 3: The local currency is not the functional currency, and the functional currency is different from the reporting currency. First, remeasure the financial statements from the local currency to the functional currency. Second, translate the financial statements from the functional currency to the reporting currency so that the consolidation and financial statements can be prepared in the reporting currency.

The following examples illustrate a situation for each of these three cases in which restatement of the financial statements is not necessary.

Local Currency	Functional Currency	Reporting Currency	Restatement Method (s)
U.S. dollar (USD)	USD	USD	None
Case 1: Mexican peso (MP)	MP	USD	Translate from MP to USD
Case 2: British pound (BP)	USD	USD	Remeasure from BP to USD
Case 3: Uruguayan peso (UP)	Brazilian real (BR)	USD	Remeasure from UP to BR then translate from BR to USD

TRANSLATION OF FUNCTIONAL CURRENCY STATEMENTS INTO THE REPORTING CURRENCY OF THE U.S. COMPANY

Income statement accounts:	
Revenue and expenses	Generally, average exchange rate for period covered by statement
Balance sheet accounts:	
Assets and liabilities	Current exchange rate on balance sheet date
Stockholders' equity	Historical exchange rates

Illustration of Translation and Consolidation of a Foreign Subsidiary

To examine the consolidation of a foreign subsidiary, assume the following facts:[6]

1. On January 1, 20X1, Peerless, a U.S. company, purchased 100 percent of the outstanding capital stock of German Company, a firm located in Berlin, Germany, for $63,000, which is $3,000 above book value. (The proof of the differential is shown at the end of the next section of the chapter.) The excess of cost over book value is attributable to a patent amortizable over 10 years. Balance sheet accounts in a trial balance format for both companies immediately *before* the acquisition are presented in Figure 12–2.
2. The local currency for German Company is the euro (€), which is also its functional currency.
3. On October 1, 20X1, the subsidiary declared and paid dividends of €6,250.
4. The subsidiary received $4,200 in a sales transaction with a U.S. company when the exchange rate was $1.20 = €1. The subsidiary still has this foreign currency on December 31, 20X1.
5. Relevant direct spot exchange rates ($/€1) are:

Date	Rate
January 1, 20X1	$1.20
October 1, 20X1	1.36
December 31, 20X1	1.40
20X1 average	1.30

FIGURE 12–2
Balance Sheet Accounts for the Two Companies on January 1, 20X1 (immediately before acquisition of 100 percent of German Company's stock by Peerless Products, a U.S. company)

	Peerless Products	German Company
Cash	$ 350,000	€ 2,500
Receivables	75,000	10,000
Inventory	100,000	7,500
Land	175,000	0
Plant & Equipment	800,000	50,000
Total Debits	$1,500,000	€70,000
Accumulated Depreciation	$ 400,000	€ 5,000
Accounts Payable	100,000	2,500
Bonds Payable	200,000	12,500
Common Stock	500,000	40,000
Retained Earnings, 12/31/X0	300,000	10,000
Total Credits	$1,500,000	€70,000

FIGURE 12–3
Worksheet to Translate Foreign Subsidiary on January 1, 20X1 (date of acquisition)
Functional Currency Is the European Euro

Item	Trial Balance, €	Exchange Rate, $/€	Trial Balance, $
Cash	2,500	1.20	3,000
Receivables	10,000	1.20	12,000
Inventory	7,500	1.20	9,000
Plant & Equipment	50,000	1.20	60,000
Total Debits	70,000		84,000
Accumulated Depreciation	5,000	1.20	6,000
Accounts Payable	2,500	1.20	3,000
Bonds Payable	12,500	1.20	15,000
Common Stock	40,000	1.20	48,000
Retained Earnings	10,000	1.20	12,000
Total Credits	70,000		84,000

Note: $1.20 is the direct exchange rate on January 1, 20X1.

January 1, 20X1

(1)	Investment in German Company Stock	63,000	
	Cash		63,000

Purchase of German Company Stock.

The differential on January 1, 20X1, the date of acquisition, is computed as follows:

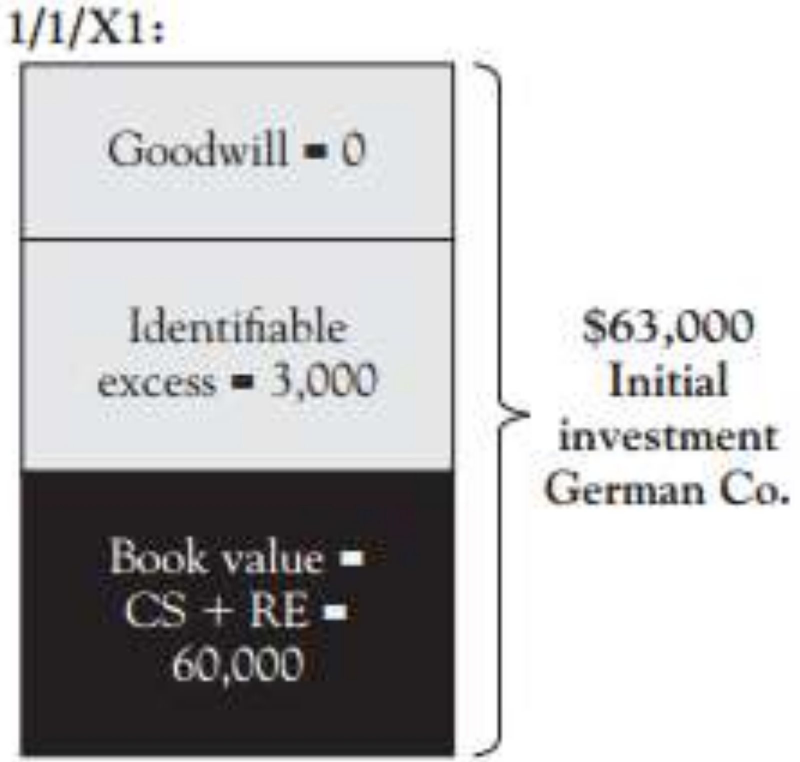
P

1/1/X1
100%

S

Fair value of consideration		$63,000
Book value of shares acquired:		
Common stock—German Co.	$48,000	
Retained earnings—German Co.	12,000	
Total	$60,000	
Percent of German Company's stock acquired by Peerless Corporation	× 1.00	
Book value acquired by Peerless Corporation		60,000
Difference between fair value and book value		$ 3,000

A graphic representation of the acquisition is as follows:



Book Value Calculations:

	Peerless 100%	=	Common Stock	+	Retained Earnings
Book value at acquisition date	60,000		48,000		12,000

This leads to the basic elimination entry:

Basic Elimination Entry:

Common stock	48,000		← Common stock balance
Retained earnings	12,000		← Beginning balance in retained earnings
Investment in German Co.		60,000	← Net book value in investment account

The differential is entirely attributable to the patent, $3,000, so the excess value reclassification entry is as follows:

Excess Value Reclassification Entry:

Patent	3,000		← Excess value assigned to patent
Investment in German Co.		3,000	← Reclassify excess acquisition price

	Investment in German Co.		
Acquisition Price	63,000		
		60,000	Basic elimination entry
		3,000	Excess value reclassification entry
	0		

Finally, we include the optional accumulated depreciation elimination entry:

Optional Accumulated Depreciation Elimination Entry:

Accumulated depreciation	6,000		← Accumulated depreciation at the time of the acquisition netted against cost
Building and equipment		6,000	

FIGURE 12–4 **January 1, 20X1, Worksheet for Consolidated Balance Sheet, Date of Acquisition**

100 Percent Purchase at More Than Book Value

	Peerless Products	German Company	Elimination Entries		Consolidated
			DR	CR	
Balance Sheet					
Cash	287,000	3,000			290,000
Receivable	75,000	12,000			87,000
Inventory	100,000	9,000			109,000
Investment in German Co. Stock	63,000			60,000	0
				3,000	
Patent			3,000		3,000
Land	175,000				175,000
Plant & Equipment	800,000	60,000		6,000	854,000
Less: Accumulated Depreciation	(400,000)	(6,000)	6,000		(400,000)
Total Assets	**1,100,000**	**78,000**	**9,000**	**69,000**	**1,118,000**
Accounts Payable	100,000	3,000			103,000
Bonds Payable	200,000	15,000			215,000
Common Stock	500,000	48,000	48,000		500,000
Retained Earnings	300,000	12,000	12,000		300,000
Total Liabilities & Equity	**1,100,000**	**78,000**	**60,000**	**0**	**1,118,000**

The subsidiary made the following entry on its books when it received the U.S. dollars:

(2)	Foreign Currency Units ($)	3,500	
	Sales		3,500

Record sales and receipt of 4,200 U.S. dollars at spot exchange rate on the date of receipt: €3,500 = $4,200/$1.20 exchange rate.

At the end of the period, the subsidiary adjusted the foreign currency units (the U.S. dollars) to the current exchange rate ($1.40 = €1) by making the following entry:

(3)	Foreign Currency Transaction Loss	500	
	Foreign Currency Units ($)		500

Adjust account denominated in foreign currency units to current exchange rate:

$4,200/$1.40	€3,000
Less: Preadjusted balance	(3,500)
Foreign currency transaction loss	€ (500).

Item	Balance, €	Exchange Rate	Balance, $
Cash	10,750	1.40	15,050
Foreign Currency Units	3,000	1.40	4,200
Receivables	10,500	1.40	14,700
Inventory	5,000	1.40	7,000
Plant & Equipment	50,000	1.40	70,000
Cost of Goods Sold	22,500	1.30	29,250
Operating Expenses	14,500	1.30	18,850
Foreign Currency Transaction Loss	500	1.30	650
Dividends Paid	6,250	1.36	8,500
Total Debits	123,000		168,200
Accumulated Depreciation	7,500	1.40	10,500
Accounts Payable	3,000	1.40	4,200
Bonds Payable	12,500	1.40	17,500
Common Stock	40,000	1.20	48,000
Retained Earnings (1/1)	10,000	(a)	12,000
Sales	50,000	1.30	65,000
Total	123,000		157,200
Accumulated Other Comprehensive Income—Translation Adjustment			11,000
Total Credits			168,200

(*a*) From the January 1, 20X1, translation worksheet.

The foreign currency transaction loss is a component of the subsidiary's net income, and the Foreign Currency Units account is classified as a current asset on the subsidiary's balance sheet. The subsidiary's net income consists of the following elements:

Sales	€ 50,000
Cost of Goods Sold	(22,500)
Operating Expenses	(14,500)
Foreign Currency Transaction Loss	(500)
Net Income	€ 12,500

	Measured in €	Measured in U.S. $
Current ratio:		
Current assets	€29,250	$40,950
Current liabilities	3,000	4,200
Current ratio	9.75	9.75
Cost of goods sold as a percentage of sales:		
Cost of goods sold	€22,500	$29,250
Sales	50,000	65,000
Percent	45%	45%

PEERLESS PRODUCTS AND SUBSIDIARY
Proof of Translation Adjustment
Year Ended December 31, 20X1

	€	Translation Rate	$
Net assets at beginning of year	50,000	1.20	60,000
Adjustment for changes in net assets position during year:			
Net income for year	12,500	1.30	16,250
Dividends paid	(6,250)	1.36	(8,500)
Net assets translated at:			
Rates during year			67,750
Rates at end of year	56,250	1.40	78,750
Change in other comprehensive income—net translation adjustment during year			11,000
Accumulated other comprehensive income—translation adjustment, 1/1			0
Accumulated other comprehensive income—translation adjustment, 12/31 (credit)			11,000

Translated Balance Sheet, 1/1/X1			
Net assets	$60,000	Common stock	$48,000
		Retained earnings	12,000
Total	$60,000	Total	$60,000

The translated balance sheet at the end of the year would be:

Translated Balance Sheet, 12/31/X1			
Net assets	$78,750	Common stock	$48,000
		Retained earnings	19,750
		Accumulated other comprehensive income—translation adjustment	11,000
Total	$78,750	Total	$78,750

Note that the $11,000 is a credit balance in order to make the balance sheet "balance."

October 1, 20X1

(4)	Cash	8,500	
	Investment in German Company Stock		8,500

Dividend received from foreign subsidiary: €6,250 × $1.36 exchange rate.

December 31, 20X1

(5)	Investment in German Company Stock	16,250	
	Income from Subsidiary		16,250

Equity in net income of German Co.: €12,500 × $1.30 average exchange rate.

(6)	Investment in German Company Stock	11,000	
	Other Comprehensive Income—Translation Adjustment		11,000

Parent's share of change in translation adjustment from translation of subsidiary's accounts: $11,000 × 1.00.

	European Euros (€)	Translation Rate	U.S. Dollars ($)
Income Statement			
Differential at beginning of year	2,500	1.20	3,000
Amortization this period (€5,000/5 years)	(500)	1.30	(650)
Remaining balances	2,000		2,350
Balance Sheet			
Remaining balance on 12/31/X1 translated at year-end exchange rates	2,000	1.40	2,800
Difference to other comprehensive income—translation adjustment (credit)			450

(7)	Income from Subsidiary	650	
	Investment in German Company Stock		650

Amortization of patent: $650 = €500 × $1.30 average exchange rate.

(8)	Investment in German Company Stock	450	
	Other Comprehensive Income—Translation Adjustment		450

Recognize translation adjustment on increase in differential.

	Investment in German Company (Dr.)	Investment in German Company (Cr.)		Income from German Company (Dr.)	Income from German Company (Cr.)	
Acquisition 1/1/X1	63,000					
100% Net Income	16,250				16,250	100% Net Income
		8,500	100% Dividends			
German Co. Translation	11,000	650	Excess Value	650		
Differential Translation	450		Amortization			
Balance 12/31/X1	81,550				15,600	Balance 12/31/X1
		67,750	Basic	16,250		
		2,800	Excess Reclass.		650	Excess Value Reclass.
		11,000	OCI			
	0				0	

(9)	Income from Subsidiary	15,600	
	Retained Earnings		15,600

To close net income from subsidiary:
$15,600 = $16,250 − $650.

(10)	Other Comprehensive Income—Trans. Adjustment	11,450	
	Accumulated OCI—Translation Adjustment		11,450

To close other comprehensive income resulting from the investment in the German subsidiary:
$11,450 = $11,000 + $450.

Book Value Calculations:

	Peerless 100%	=	Common Stock	+	Retained Earnings
Beginning book value	60,000		48,000		12,000
+ Net Income	16,250				16,250
− Dividends	(8,500)				(8,500)
Ending book value	67,750		48,000		19,750

This leads to the basic elimination entry:

Basic Elimination Entry:

Common stock	48,000		← Common stock balance
Retained earnings	12,000		← Beginning balance in retained earnings
Income from German Co.	16,250		← German Company's reported income
Dividends declared		8,500	← 100% of German's dividends declared
Investment in German Co.		67,750	← Net book value in investment account

The $3,000 differential is entirely attributable to the patent; nevertheless, because it arises from the acquisition of a foreign subsidiary, we provide these calculations that illustrate the translation adjustment for the differential:

Excess Value (differential) Calculation:

	Total Excess	=	Patent
Beginning excess value	3,000		3,000
− Amortization of differential	(650)		(650)
+ Differential translation adjustment	450		450
Ending excess value	2,800		2,800

Note that the adjustments for $650 and $450 were already explained in entries (7) and (8).

Amortized Excess Value Reclassification Entry:

Operating expense	650		← Amortization of patent
Income from German Co.		650	← Elimination of patent amortization

Excess Value (differential) Reclassification Entry:

Patent	2,800		← Excess value assigned to patent
Investment in German Co.		2,800	← Reclassify excess acquisition price

In addition, we record the other comprehensive income entry illustrated in Chapter 5:

Other Comprehensive Income Entry:

OCI from German Co.	11,000	
Investment in German Co.		11,000

Finally, we include the optional accumulated depreciation elimination entry:

Optional Accumulated Depreciation Elimination Entry:

Accumulated depreciation	6,000		← Accumulated depreciation at the time of the acquisition netted against cost
Building and equipment		6,000	

FIGURE 12–7 **December 31, 20X1, Consolidation Worksheet, Prepared after Translation of Foreign Statements**

	Peerless Products	German Company	Elimination Entries DR	Elimination Entries CR	Consolidated
Income Statement					
Sales	400,000	65,000			465,000
Less: COGS	(170,000)	(29,250)			(199,250)
Less: Operating Expenses	(90,000)	(18,850)	650		(109,500)
Less: Foreign Currency Transaction Loss		(650)			(650)
Income from German Co.	15,600		16,250	650	0
Net Income	**155,600**	**16,250**	16,900	650	**155,600**
Statement of Retained Earnings					
Beginning Balance	300,000	12,000	12,000		300,000
Net Income	**155,600**	**16,250**	16,900	650	155,600
Less: Dividends Declared	(60,000)	(8,500)		8,500	(60,000)
Ending Balance	**395,600**	**19,750**	28,900	9,150	**395,600**
Balance Sheet					
Cash	425,500	15,050			440,550
Dollars Held by German Company		4,200			4,200
Receivables	75,000	14,700			89,700
Inventory	100,000	7,000			107,000
Investment in German Company Stock	81,550			67,750	0
				2,800	
				11,000	
Land	175,000				175,000
Patent			2,800		2,800
Plant & Equipment	800,000	70,000		6,000	864,000
Less: Accumulated Depreciation	(450,000)	(10,500)	6,000		(454,500)
Total Assets	**1,207,050**	**100,450**	8,800	87,550	**1,228,750**

Accounts Payable	100,000	4,200			104,200
Bonds Payable	200,000	17,500			217,500
Common Stock	500,000	48,000	48,000		500,000
Retained Earnings	**395,600**	**19,750**	**28,900**	**9,150**	395,600
Accumulated Other Comprehensive Income	11,450	11,000	**11,000**	**0**	11,450
Total Liabilities & Equity	**1,207,050**	**100,450**	**87,900**	**9,150**	**1,228,750**
Other Comprehensive Income					
Accumulated Other Comprehensive Income, 1/1/X1	0	0			0
Other Comprehensive Income Translation Adjustment	11,450	11,000	**11,000**		11,450
Accumulated Other Comprehensive Income, 12/31/X1	**11,450**	**11,000**	**11,000**	**0**	**11,450**

FIGURE 12–8 Consolidated Statement of Changes in Stockholders' Equity

PEERLESS PRODUCTS AND SUBSIDIARY
Consolidated Statement of Changes in Equity
Year Ended December 31, 20X1

	Total	Comprehensive Income	Retained Earnings	Accumulated Other Comprehensive Income	Capital Stock
Beginning Balance	$800,000		$300,000	$ 0	$500,000
Comprehensive Income:					
Net Income	155,600	$155,600	155,600		
Other Comprehensive Income:					
Foreign Currency Translation Adjustment	11,450	11,450		11,450	
Comprehensive Income		$167,050			
Dividends Declared on Common Stock	(60,000)		(60,000)		
Ending Balance	$907,050		$395,600	$11,450	$500,000

Common stock ($48,000 × 0.20)		$ 9,600
Retained earnings:		
Beginning retained earnings ($12,000 × 0.20)	$2,400	
Add: Net income ($16,250 × 0.20)	3,250	
Less: Dividends ($8,500 × 0.20)	(1,700)	
Total retained earnings		3,950
Accumulated other comprehensive income—translation adjustment ($11,000 × 0.20)		2,200
Total noncontrolling interest		$15,750

REMEASUREMENT OF THE BOOKS OF RECORD INTO THE FUNCTIONAL CURRENCY

FIGURE 12–9
Accounts to Be Remeasured Using Historical Exchange Rates

Examples of Balance Sheet Nonmonetary Items

Marketable securities:
- Equity securities
- Debt securities not intended to be held until maturity

Inventories
Prepaid expenses such as insurance, advertising, and rent
Property, plant, and equipment
Accumulated depreciation on property, plant, and equipment
Patents, trademarks, licenses, and formulas
Goodwill
Other intangible assets
Deferred charges and credits except deferred income taxes and policy acquisition costs for life insurance companies
Deferred income
Common stock
Preferred stock carried at issuance price

Examples of Revenue and Expenses Related to Nonmonetary Items

- Cost of goods sold
- Depreciation of property, plant, and equipment
- Amortization of intangible items such as patents, licenses, etc.
- Amortization of deferred charges or credits, except deferred income taxes and policy acquisition costs for life insurance companies

FIGURE 12–10
December 31, 20X1, Remeasurement of the Foreign Subsidiary's Trial Balance
U.S. Dollar Is the Functional Currency

Item	Balance, €	Exchange Rate	Balance, $
Cash	10,750	1.40	15,050
Foreign Currency Units	3,000	1.40	4,200
Receivables	10,500	1.40	14,700
Inventory	5,000	1.38	6,900
Plant & Equipment	50,000	1.20	60,000
Cost of Goods Sold	22,500	(a)	28,100
Operating Expenses	14,500	(b)	18,600
Foreign Currency Transaction Loss	500	1.30	650
Dividends Paid	6,250	1.36	8,500
Total Debits	123,000		156,700
Accumulated Depreciation	7,500	1.20	9,000
Accounts Payable	3,000	1.40	4,200
Bonds Payable	12,500	1.40	17,500
Common Stock	40,000	1.20	48,000
Retained Earnings	10,000	(c)	12,000
Sales	50,000	1.30	65,000
Total	123,000		155,700
Remeasurement Gain			1,000
Total Credits			156,700

	In Euros	Exchange Rate	In Dollars
(a) Cost of Goods Sold:			
Beginning Inventory	7,500	1.20	9,000
Purchases	20,000	1.30	26,000
Goods Available	27,500		35,000
Less: Ending Inventory	(5,000)	1.38	(6,900)
Cost of Goods Sold	22,500		28,100
(b) Operating Expenses:			
Cash Expenses	12,000	1.30	15,600
Depreciation Expense	2,500	1.20	3,000
	14,500		18,600

(c) Carry forward from January 1, 20X1, worksheet.

FIGURE 12–11
Proof of the Remeasurement Exchange Gain for the Year Ended December 31, 20X1
Functional Currency Is the U.S. Dollar

Schedule 1
Statement of Net Monetary Positions

	End of Year	Beginning of Year
Monetary assets:		
Cash	€10,750	€ 2,500
Foreign currency units	3,000	0
Receivables	10,500	10,000
Total	€24,250	€12,500
Less: Monetary equities:		
Accounts payable	€ 3,000	€ 2,500
Bonds payable	12,500	12,500
Total	€15,500	€15,000
Net monetary liabilities		€ (2,500)
Net monetary assets	€ 8,750	
Increase in net monetary assets during year	€11,250	

Schedule 2
Analysis of Changes in Monetary Accounts

	€	Exchange Rate	U.S. $
Exposed net monetary liability position, 1/1	(2,500)	1.20	(3,000)
Adjustments for changes in net monetary position during year:			
Increases:			
From operations:			
Sales	50,000	1.30	65,000
From other sources	0		0
Decreases:			
From operations:			
Purchases	(20,000)	1.30	(26,000)
Cash expenses	(12,000)	1.30	(15,600)
Foreign currency transaction loss	(500)	1.30	(650)
From dividends	(6,250)	1.36	(8,500)
From other uses	0		0
Net monetary position prior to remeasurement at year-end rates			11,250
Exposed net monetary asset position, 12/31	8,750	1.40	12,250
Remeasurement gain			1,000

FOREIGN INVESTMENTS AND UNCONSOLIDATED SUBSIDIARIES

FIGURE 12–13 Summary of the Translation and Remeasurement Processes

Item	Translation Process	Remeasurement Process
Foreign entity's functional currency	Local currency unit	U.S. dollar
Method used	Current rate method	Monetary-nonmonetary method
Income statement accounts:		
Revenue	Weighted-average exchange rate	Weighted-average exchange rate except revenue related to nonmonetary items (historical exchange rate)
Expenses	Weighted-average exchange rate	Weighted-average exchange rate except costs related to nonmonetary items (historical exchange rate)
Balance sheet accounts:		
Monetary accounts	Current exchange rate	Current exchange rate
Nonmonetary accounts	Current exchange rate	Historical exchange rate
Stockholders' equity capital accounts	Historical exchange rate	Historical exchange rate
Retained earnings	Prior-period balance plus income less dividends	Prior-period balance plus income less dividends
Exchange rate adjustments arising in process	Translation adjustment accumulated in stockholders' equity	Remeasurement gain or loss included in period's income statement

FIGURE 12–14
Two-Statement Approach to Display Comprehensive Income

PEERLESS PRODUCTS AND SUBSIDIARY
Consolidated Income Statement
Year Ended December 31, 20X1

Sales	$465,000
Cost of Goods Sold	(199,250)
Gross Profit	265,750
Operating Expenses	(109,500)
Foreign Currency Transaction Loss	(650)
Consolidated Net Income to Controlling Interest	$155,600

PEERLESS PRODUCTS AND SUBSIDIARY
Consolidated Statement of Comprehensive Income
Year Ended December 31, 20X1

Consolidated Net Income to Controlling Interest	$155,600
Other Comprehensive Income: Foreign Currency Translation Adjustment	$ 11,450
Comprehensive Income to Controlling Interest	$167,050

INVESTMENT IN A FOREIGN SUBSIDIARY

January 1, 20X1

(11)	Cash	60,000	
	Loan Payable (€)		60,000

Borrow a euro-denominated loan to hedge net investment in German subsidiary:
\$60,000 = €50,000 × \$1.20 spot rate.

December 31, 20X1

(12)	Other Comprehensive Income	10,000	
	Loan Payable (€)		10,000

Revalue foreign currency–denominated payable to end-of-period spot rate:
\$10,000 = €50,000 × (\$1.40 − \$1.20).

(13)	Interest Expense	3,250	
	Foreign Currency Transaction Loss	250	
	Interest Payable (€)		3,500

Accrue interest expense and payable on euro loan:
$3,250 = €50,000 × 0.05 interest × $1.30 average exchange rate
$3,500 = €50,000 × 0.05 interest × $1.40 ending spot rate.

(14)	Accumulated OCI—Translation Adjustment	10,000	
	Profit and Loss Summary (or Retained Earnings)	250	
	Foreign Currency Transaction Loss		250
	Other Comprehensive Income		10,000

Close nominal accounts related to hedge of net investment in foreign subsidiary.

Then, when the principal and interest are paid on January 1, 20X2, Peerless makes the following entry:

	January 1, 20X2		
(15)	Interest Payable (€)	3,500	
	Loan Payable (€)	70,000	
	Cash		73,500

Pay principal and interest due on euro-denominated hedge:
$70,000 = $60,000 + $10,000.

DISCLOSURE REQUIREMENTS

PSAK 10- The effect of Changes in Foreign Exchange Rate (PSAK 10) requires the aggregate foreign transaction gain or loss included in income to be separately disclosed in the income statement or in an accompanying note. This includes gains or losses recognized from foreign currency transactions, forward exchange contracts, and any remeasurement gain or loss. If not disclosed as a one-line item on the income statement, this disclosure is usually a one-sentence footnote summarizing the company's foreign operations.

ADDITIONAL CONSIDERATIONS IN ACCOUNTING FOR FOREIGN OPERATIONS AND ENTITIES

1. Remeasurement Case: Subsequent Consolidation Workpaper
2. Proof of Remeasurement of Exchange Gain
3. Statement of cash Flow
4. Lower-of-Cost-or-Net Realizable Value Inventory Valuation under Remeasurement
5. Intercompany Transactions
6. Income Taxes
7. Translation When a Third Currency is the Functional Currency

THANK YOU