

CHAPTER 12

MULTINATIONAL ACCOUNTING: ISSUES IN FINANCIAL REPORTING AND TRANSLATION OF FOREIGN ENTITY STATEMENTS

ANSWERS TO QUESTIONS

Q12-1 Interest is increasing because of the expected benefits of adopting a single set of high-quality accounting standards, which include:

1. Continued expansion of capital markets across national borders.
2. More rapid development of stable, liquid capital markets.
3. Increased economic growth.
4. Improve ability of investors to evaluate opportunities across national borders.
5. Improve the efficient use of global capital.
6. Reduce reporting costs for corporations that wish to access capital in markets outside of their home country.
7. Increase confidence of financial statement users in the quality of financial reporting.

Q12-2 The IASB is an independent privately funded accounting standards-setting body. The mission of the IASB is to develop a single set of high-quality, understandable, and enforceable global accounting standards. The IASB is composed of 15 members who each serve a five-year term subject to one reappointment. Members are required to sever all employment relationships that might compromise their independent judgement in setting accounting standards. The IASB is based in London.

Q12-3 The IASB solicits input from the public when evaluating potential standards and publishes a discussion paper and/or an exposure draft which are subject to comment before issuing a final standard.

Q12-4 IFRS are already mandated or permitted in over 100 countries around the world. Beginning with 2005, the European Union mandated the use of IFRS for companies listing on stock exchanges in the EU, although the EU also continues to accept statements prepared according to US GAAP. Beginning in 2008, foreign private issuers who list their shares on US stock exchanges may use IFRS in their financial statements without reconciliation to US GAAP.

Q12-5 The attitude toward the possible use of IFRS in the United States is cautiously supportive (based on the SEC roundtable panellists).

Q12-6 Potential benefits include:

- Improve global competitive position of US corporations.
- Increase the quality of information available to investors.
- Reduce costs of compliance for companies that are currently using multiple reporting frameworks.
- Enhance global capital markets.
- Companies would have easier access to raising capital in the global markets.
- Because SEC now permits foreign private issuers to file their financial reports using IFRS without reconciliation, not allowing US companies to report under IFRS could result in US companies bearing costs not incurred by foreign private issuers.
- Enhance comparability across companies for users. SEC chairman Cox noted that two-thirds of US investors own securities of foreign companies, a 30 percent increase in the last five years.

Q12-7 a. Local currency unit. The local currency unit (LCU) is the currency used locally; that is, the currency used in the country in which the company is located.

b. Recording currency. The recording currency is the currency used to record the economic activities in the journals and ledger of the business entity. The recording currency is typically the local currency, but may be some other currency.

c. Reporting currency. The reporting currency is the currency used on the financial statements of the business entity. Typically, the reporting currency is the same as the recording currency.

Q12-8 The functional currency is normally the currency in which the foreign entity performs most of its cash functions. However, for entities operating in highly inflationary economies, the functional currency is designated as the U.S. dollar regardless of the actual currency used for cash functions. The definition of a highly inflationary economy is one that has a cumulative inflation of approximately 100 percent or more over a 3-year period. **ASC 830** provides six indicators to be used to determine a foreign entity's functional currency: (1) cash flows, (2) sales prices, (3) sales markets, (4) expenses, (5) financing, and (6) intercompany transactions and arrangements. If most of these indicators take place in the foreign currency unit, then the FCU is the functional currency. If most take place in the U.S. dollar, then the dollar is the functional currency.

Q12-9 Harmonization means to standardize the accounting principles used around the world. For example, the U.S. does not allow a company to revalue its own assets for the effects of inflation. Several countries do, however, allow for this revaluation and subsequent depreciation on the revaluation. Differences in accounting principles from country to country make it difficult to compare business entities doing business in different countries. The harmonization of accounting principles around the world would eliminate many of the problems of combining and consolidating multinational entities. A U.S. company with international investments could then be assured of essentially the same accounting principles being applied; therefore, revenues, profits, and investments in these foreign investments could effectively be compared and contrasted.

Q12-10 When the local currency is the foreign entity's functional currency, the translation method is used to convert the foreign entity's financial statements into U.S. dollars, the parent company's reporting currency. The translation method uses the current exchange rate for converting all assets and liabilities. The appropriate historical exchange rate is used to convert the Canadian entity's stockholders' equity accounts. The weighted average exchange rate is used to convert the Canadian entity's income statement accounts. The change in the translation adjustment during the period is reported as an element of other comprehensive income on the Statement of Comprehensive Income, and is then accumulated with the other elements of comprehensive income and reported within the stockholders' equity section of the consolidated balance sheet. The translation adjustment may have a debit or credit balance, depending on the relative change in the exchange rate since the parent acquired the subsidiary.

Q12-11 Remeasurement is used when the U.S. dollar is the functional currency of the foreign entity. Furthermore, **ASC 830** requires that the financial statements of foreign entities operating in highly inflationary economies be remeasured as if the functional currency were the reporting currency. Remeasurement requires the use of the current exchange rate to convert all monetary assets and liabilities. The historical exchange rate is used to convert nonmonetary assets and the stockholders' equity accounts. The appropriate historical rate is the rate on the later of the two following dates: (1) the day the foreign entity obtained the asset or the day the foreign entity made a transaction affecting the stockholders' equity section such as selling additional stock or declaring dividends, or (2) the day the U.S. parent company purchased the foreign affiliate.

The weighted average exchange rate for the period covered by the income statement is used for revenues or expenses incurred evenly over the period except for those expenses that are allocations of balance sheet items, such as depreciation, cost of goods sold (inventories), or write-offs of goodwill. For cost allocations, the same rate used on the balance sheet to convert the items to U.S. dollars is used on the income statement.

Q12-12 Translation adjustments are the balancing items to make the debit and credit items equal in the translated trial balance measured in U.S. dollars. The parent company records its share of the translation adjustment in its books through an adjusting entry. The change during the period in the translation adjustment is reported as a component of other comprehensive income in the Statement of Comprehensive Income. The accumulated other comprehensive income is reported as a separate item of stockholders' equity in the balance sheet. The cumulative translation adjustment may have a debit balance or credit balance. A debit balance usually means that the current exchange rate is less than the historical rate used to translate the stockholders' equity accounts. This means the dollar is strengthening relative to the foreign currency. A credit balance usually results when the dollar is weakening relative to the foreign currency, and the current exchange rate is higher than the historical exchange rate.

Q12-13 The remeasurement gain or loss first appears as the trial balance balancing item in the income statement section of the foreign affiliate's trial balance. The parent company recognizes its share of the remeasurement gain through an adjusting entry. Typically, the remeasurement gain is shown in the "Other Income" section of the consolidated income statement.

Q12-14 The stockholders' equity accounts are translated at the historical rate in effect the date the parent company acquired the foreign affiliate because this aids in the elimination entry process used to prepare the consolidated statements. The investment account on the parent company's books includes the initial investment measured in terms of the exchange rate on the date the parent purchased the foreign affiliate. Thus, the basic eliminating entry to eliminate the investment account against the capital stock and additional paid-in capital includes accounts with the same currency measurement rate. The retained earnings include the effects of revenue and expense transactions, all measured at different rates over time. The beginning translated retained earnings, as measured in U.S. dollars, is taken from last year's ending retained earnings. Net income is obtained from the income statement and dividends are translated using the exchange rate in effect the date the dividends are declared. The translated balances for net income and dividends are then used to adjust beginning retained earnings and come to the new balance for ending retained earnings.

Q12-15 The current rate method uses the current exchange rate to translate the foreign affiliate's assets and liabilities. The weighted-average exchange rate is used to translate the foreign affiliate's revenues and expenses. This means that the relationships within the assets and liabilities of the foreign affiliate's balance sheet are not changed in the translation process. For example, the current ratio in U.S. dollar statements will be the same as in the foreign currency statements. This results from the use of a constant translation multiplier within the financial statements. However, this relationship does not hold when computing ratios using a balance sheet account and an income statement account: for example, return on equity. These ratios include accounts with different translation exchange rates and will, therefore, produce different results when looking at the foreign currency ratio as compared to the US dollar ratio.

Q12-16 The excess of cost over book value has two effects: (1) the portion amortized for the period is reported in the income statement, and (2) the unamortized balance is reported in the balance sheet. When the local currency unit is the functional currency, the translation method is used to convert the foreign entity's financial statements into U.S. dollars. **ASC 830** requires that the differential be evaluated in terms of the foreign currency unit. Therefore, the period's amortization, measured in the foreign currency, is translated at the weighted average exchange rate. The remaining unamortized differential is translated at the current exchange rate at the end of the period. The different exchange rates used typically result in a difference when measured in U.S. dollars. This difference becomes part of the translation adjustment.

Q12-17 Since the parent company controls the foreign subsidiary, it logically must consolidate the entity. By virtue of the fact that the subsidiary resides in a foreign country, the parent bears the risk of fluctuations in the exchange rate. Thus, parent's share of the translation adjustment should affect the financial statements of the parent. However, the FASB allowed comprehensive income treatment for these transactions so that constant fluctuations in exchange rates would not cause constant variability to the net income of companies with foreign investments. The change during the period in the translation adjustment is reported as a component of other comprehensive income. The translation adjustment is part of the accumulated other comprehensive income that is reported in the stockholders' equity section of the consolidated balance sheet.

Q12-18 Not all foreign subsidiaries are consolidated. The parent must be able to exercise control over the foreign subsidiary's operating and financial policies before consolidation is proper. This may not be the case if the foreign subsidiary is located in a country in which the government places significant restrictions on dividend declarations, input from non-local management, or other operating or financing aspects of the business.

Q12-19 If an investment in a foreign subsidiary is not consolidated, it is reported as a long-term investment on the U.S. company's financial statements, usually under the equity method. The cost method is used to account for the foreign investment, however, if the U.S. investor is not able to exercise significant influence over the foreign investee's operating and financial policies.

Q12-20 The issue with intercompany transactions is with regard to the amount of unrealized profit. The unrealized profit determined at the time of the initial intercompany transaction is a function of the currency exchange rate at that time. As the rate changes, the underlying accounts may be translated at different exchange rates, thus affecting the computation of unrealized intercompany profit. **ASC 830** states that the intercompany profit should be eliminated based on the exchange rate at the date the intercompany transaction occurred. This eliminates any potential problems from subsequent changes in exchange rates.

SOLUTIONS TO CASES

C12-1 Comparison of US GAAP and IFRS

Solutions will vary by student depending on the particular items he or she selects.

C12-2 Structure of the IASB

The International Accounting Standards Committee (IASC) Foundation is the parent entity of the IASB. The IASC Foundation is an independent organization. The IASC Foundation trustees appoint the IASB members, exercise oversight, and raise funds to support the organization. The IASC Foundation also appoints the Standards Advisory Council, which advises the IASB and the International financial Reporting Interpretations Committee. The IASB has the sole responsibility for setting accounting standards. These standards are called International Financial Reporting Standards (IFRS).

C12-3 IASB Deliberations

Solutions will vary by student depending on the particular items he or she selects.

C12-4 Determining a Functional Currency

The choice of a functional currency is based on the currency used for six criteria provided in **ASC 830**, as follows: (1) cash flows, (2) sales prices, (3) sales markets, (4) expenses, (5) financing, and (6) intercompany transactions and arrangements. The choice of a functional currency is made by management after a subjective evaluation of these criteria. However, the U.S. dollar is specified as the functional currency in cases in which the foreign affiliate of a U.S. company is located in a country experiencing high inflation (approximately 100 percent or more over a three-year period).

	<u>Foreign Entity's Recording Currency</u>	<u>Foreign Entity's Functional Currency</u>	<u>Process of Restatement into U.S. Dollars</u>
1.	Argentinean peso	U.S. dollar	Remeasurement
<p>Note: This case shows that the U.S. dollar is the specified functional currency for foreign subsidiaries located in countries with highly inflationary economies.</p>			
2.	Mexican pesos	Either peso or dollar, management may select either.	Either
<p>Note: This case indicates that the criteria are not always absolute. Management probably would select the specific functional currency on the basis of financial effects, such as effect on earnings per share.</p>			
3.	British pound	British pound	Translation
4.	Swiss franc	European euro	Remeasurement from franc to euro; then translation from euro to dollars
<p>Note: This case shows that the local currency of the country in which the foreign affiliate is located may not be the foreign affiliate's functional currency; instead, a third currency presents the functional currency.</p>			

**C12-5 Principles of Consolidating and Translating Foreign Accounts
[AICPA Adapted]**

a. The rules for consolidating a foreign subsidiary are essentially the same as for a domestic subsidiary. The key element is the degree of control Petie Products has over the financial and operating policies of Cream, Ltd. Typically, a 90 percent stock ownership level would assure the parent company's control of the subsidiary. It is possible, however, that the country of Kolay may have severe restrictions on the decision-making abilities of non-Kolay investors, or that Kolay may have restrictive laws regulating commerce within Kolay. Petie Products' management must evaluate their ability to control the foreign subsidiary. If they do possess the necessary level of control, the foreign subsidiary should be consolidated. If not, then the foreign subsidiary is reported as an investment on the parent company's financial statements.

b. Translation means that the local currency unit is functional. The foreign subsidiary's assets and liabilities are translated using the current exchange rate at the end of 20X7. The stockholders' equity accounts are translated at appropriate historical rates. The income statement accounts are translated at the weighted average exchange rate during 20X7.

The appropriate exchange rates for each of the 10 items are presented below:

1. Current exchange rate at December 31, 20X7
2. Current exchange rate at December 31, 20X7
3. Current exchange rate at December 31, 20X7
4. Current exchange rate at December 31, 20X7
5. Current exchange rate at December 31, 20X7
6. Historical exchange rate at January, 20X4
7. Beginning Retained Earnings is carried forward as a composite from prior years' operations. The beginning Retained Earnings is the prior period's ending Retained Earnings.
8. Average exchange rate for 20X7 (assumes revenues earned evenly throughout year)
9. Average exchange rate for 20X7
10. Average exchange rate for 20X7

C12-6 Translating and Remeasuring Financial Statements of Foreign Subsidiaries [AICPA Adapted]

- a. The objectives of translating a foreign subsidiary's financial statements are to:
1. Provide information that is generally compatible with the expected economic effects of a rate change on a subsidiary's cash flows and equity.
 2. Reflect the subsidiary's financial results and relationships in single currency financial statements, as measured in its functional currency and in conformity with generally accepted accounting principles.
- b. Applying different exchange rates to the various financial statement accounts causes the restated financial statements to be unbalanced. 'Unbalanced' means that the debits will not equal the credits in the subsidiary's trial balance prepared in U.S. dollars. The amount required to bring the restated financial statements into balance is termed the gain or loss from the translation or remeasurement. The gain or loss from remeasuring Wahl A's financial statements is reported in the consolidated income statement. The gain or loss arising from translating Wahl F's financial statements (described as a translation adjustment) is reported as a component of comprehensive income and then accumulated with other comprehensive income items and reported under stockholders' equity in the consolidated balance sheet.
- c. The functional currency is the foreign currency or the parent's currency that most closely correlates with the following economic indicators:
1. Cash flow indicators
 2. Sales price indicators
 3. Sales market indicators
 4. Expense indicators
 5. Financing indicators
 6. Intercompany transactions and arrangement indicators
- d. All accounts relating to Wahl A's equipment—the equipment, accumulated depreciation, and depreciation expense accounts—are remeasured by using the exchange rate prevailing between the U.S. and Australian dollars at the later of the two following dates: (1) the date at which Wahl Co. acquired its investment in Wahl A, or (2) the date(s) the equipment was purchased by Wahl A. This exchange rate is referred to as the historical rate.

All accounts relating to Wahl F's equipment are translated by using the current exchange rates prevailing between the U.S. dollar and the European euro. For the equipment cost and the accumulated depreciation, the current exchange rate at December 31, 20X5, should be used for translation. Depreciation expense is translated at an appropriate weighted average exchange rate for 20X5.

C12-7 Translation Adjustment and Comprehensive Income

- a. Statement of income for the year, for the subsidiary

Subsidiary Statement of Income Year Ended December 31, 20XX	
Sales	\$ 560,000
Cost of Sales	<u>(285,000)</u>
Gross Profit	\$ 275,000
Operating Expenses	<u>(140,000)</u>
Income from Operations	<u>\$ 135,000</u>
Consolidated Net Income to Controlling Interest	<u>\$ 135,000</u>

- b. Statement of comprehensive income for the year, for the subsidiary

Subsidiary Statement of Comprehensive Income Year Ended December 31, 20XX	
Consolidated Net Income to Controlling Interest	\$ 135,000
Other Comprehensive Income:	
Translation Adjustment	<u>(12,000)</u>
Comprehensive Income	<u>\$ 123,000</u>

- c. Balance sheet as of December 31, for the subsidiary

Subsidiary Balance Sheet December 31, 20XX	
Assets	
Cash	\$ 50,000
Receivables	24,700
Inventories	60,300
Property, Plant, and Equipment (net)	<u>328,000</u>
Total Assets	<u>\$ 463,000</u>
Liabilities and Stockholders' Equity	
Current Payables	\$ 16,000
Long-Term Payables	181,000
Capital Stock	100,000
Retained Earnings	258,000
Accumulated Other Comprehensive Income:	
Translation Adjustment	<u>(92,000)</u>
Total Liabilities and Stockholders' Equity	<u>\$ 463,000</u>

Note: The end-of-year retained earnings (\$258,000) comprises the January 1 balance of \$135,000, plus net income of \$135,000, less dividends of \$12,000.

C12-7 (continued)

- d. **ASC 220** allows for either the one-statement format for the combined statement of income and comprehensive income, or the two-statement format for a statement of income and a separate statement of comprehensive income. Both formats must include all the elements of comprehensive income. The one-statement format presents the other comprehensive income elements immediately below net income.

The two-statement format presents a separate statement of income as was done prior to **ASC 220**. The statement of income ends with net income. Then, a separate statement of comprehensive income begins with net income, followed with the elements of other comprehensive income, and ends with comprehensive income.

C12-8 Changes in the Cumulative Translation Adjustment Account

Johnson & Johnson Company applied the concepts presented in the chapter for translating the trial balances of its foreign subsidiaries. The resulting cumulative translation adjustment has changed dramatically from a credit balance of \$134 million at the end of 20X1 to a debit balance of \$338 million at the end of 20X3.

The translation adjustment is related to the translated net asset balance (assets minus liabilities) of the foreign subsidiaries. Several factors could account for the decrease in the net assets of Johnson & Johnson’s foreign subsidiaries, as follows:

1. The foreign subsidiaries could be increasing their local liabilities, i.e., taking out more local debt.
2. The foreign subsidiaries could be decreasing their local assets, i.e., not maintaining their physical capital through reinvestment.
3. The direct exchange rate of the dollar versus the local currency units of the countries in which the company has foreign subsidiaries has been decreasing over time (i.e., the dollar had strengthened versus the local currency units).

Question **d.** can be used to demonstrate these factors. Remember that it is assumed that the translated stockholders’ equity, other than the accumulated other comprehensive income (AOCI) from the translation adjustment, remained constant at \$500 million for each of the three years. The following condensed balance sheets can be presented:

20X1 Translated Balance Sheets of All Foreign Subsidiaries			
Net assets	\$634	Stockholders’ equity:	
		Other than AOCI	\$ 500
		AOCI Translation Adjustment	134
20X2 Translated Balance Sheets of All Foreign Subsidiaries			
Net assets	\$354	Stockholders’ equity:	
		Other than AOCI	\$ 500
		AOCI Translation Adjustment	(146)
20X3 Translated Balance Sheets of All Foreign Subsidiaries			
Net assets	\$162	Stockholders’ equity:	
		Other than AOCI	\$ 500
		AOCI Translation Adjustment	(338)

C12-8 (continued)

If the direct exchange rate decreased over the two-year period, the translated net assets would decrease, thus causing a decrease (debit change) in the translation adjustment. The direct exchange rate would decrease if the dollar were strengthening versus the local currency units of the countries in which the company had foreign subsidiaries. Other causes for the decrease in the translated net assets would be a decrease in local assets, or an increase in local liabilities.

Johnson & Johnson Company did make several changes in its foreign investment portfolio during 20X2 and 20X3 that would have resulted in a change in the combined stockholders' equity of the company's foreign investments. During 20X3, the company acquired approximately \$266 million in European companies. In 20X2, the company acquired approximately \$47 million in Japanese companies. The company completed relatively minor sales of foreign subsidiaries and operations during 20X2 and 20X3.

Thus, it appears that the major reasons for the significant debit change in the accumulated other comprehensive income—translation adjustment account over the two-year period was that the foreign subsidiaries were increasing their local debt, and that the U.S. dollar was strengthening versus the local currency units of the foreign countries in which Johnson & Johnson Company had subsidiaries. A more specific analysis would require knowledge of the amount of the foreign investments in each country, the balance of the local assets and local liabilities of each of the foreign subsidiaries, and the knowledge of the exchange rates for the dollar versus the foreign currencies of the countries in which the company has invested.

C12-9 Pros and Cons of Foreign Investment

The focus of this case is to consider the variables involved with the business decision of expanding a company's production and/or marketing investment in a foreign country. Many of the variables would be similar to those considered in the decision to increase a company's physical capital in the U.S. But, some additional variables should be considered for the foreign country such as: home-country laws, the political and economic environment, the accounting and tax laws, the status of labor organization, the cost-of-living and prevailing wages, the supply of trained labor forces (including local management personnel), and the different cultural aspects that might impact on obtaining the factors of production or on the markets for the company's goods. Some companies make investment in foreign production facilities in order to have a production capability closer to a foreign market. Thus transportation costs of the finished goods are decreased, while the company is able to increase overall revenue and income.

Many companies go to non-U.S. production sources because of the lower costs for labor. Thus, if the company produces a labor-intensive product, the economics of the decision may favor foreign production. In addition, as tariffs are reduced, U.S. companies may find it more advantageous to move their production facilities to non-U.S. locations. One possible outcome is that the costs of the finished goods to U.S. consumers would be lower for goods manufactured outside the U.S. However, an argument often raised in the political arena is that unemployed U.S. consumers would not be able to purchase the products.

The U.S. government has proposed retraining programs for dislocated workers who lose their jobs because the company has closed the U.S. production facility. Students should be encouraged to develop some new and novel approaches to solving the problem of the general change in the types of new jobs being created in the U.S. economy.

C12-10 Determining an Entity's Functional Currency

MEMO

To: Garry Parise, CFO, Maxima Corporation

From: _____, CPA, Controller's Department

Re: Functional Currency of Luz Maxima

According to **ASC 830**, the functional currency for a company is the primary currency that is generated by cash inflows and used for cash outflows. Further, it is the currency the country that is primary economic environment of the company's business operations as indicated by items such as sales, and expense, and financing activities.

Because Luz Maxima initially did business exclusively with Maxima Corporation and these transactions were denominated in the U.S. dollar, its functional currency was originally determined to be the U.S. dollar. However, it appears that changes in Luz Maxima's operation over the past five years may result in a change in the functional currency from the U.S. dollar to the Mexican peso.

Appendix A of **ASC 830** provides indicators that should be considered in determining a foreign subsidiary's functional currency. Among the indicators that may be relevant for evaluating the functional currency of Luz Maxima are sales, expense, and financing indicators.

- Sales market indicators – Luz Maxima now sells a significant amount of product in Mexico and South America. These transactions are denominated in the peso.
- Expense indicators – Luz Maxima obtains a significant amount of materials from local suppliers.
- Financing indicators – Luz Maxima obtained long-term debt financing and a line of credit from banks in Mexico.

To the extent indicators are mixed and Luz Maxima also has sales, expenses, and financing transactions denominated in the U.S. dollar, **ASC 830** states that management should make the final determination as to the functional currency. **ASC 830** also indicates that, while it is desirable for the functional currency to be used consistently, if economic facts change, it may be appropriate to change the determination of the functional currency.

Management should assess all aspects of Luz Maxima's operation to determine the most appropriate and relevant functional currency for this subsidiary. If a decision is made to change the functional currency from the U. S. dollar to the Mexican peso, Luz Maxima's current financial statements should be converted to U.S. dollars using the current rate translation method. Any adjustment that occurs as a result of translating nonmonetary assets using the current rate method should be reported as a component of other comprehensive income.

Authoritative support for the above memo can be found in ASC 830.

C12-11 Accounting for the Translation Adjustment

MEMO

To: Renee Voll, Controller

From: _____, CPA

Re: Translation Adjustment for Valencia subsidiary

Since Sonoma has sold 30% of the investment in our Spanish subsidiary, the balance of the cumulative translation adjustment, included in consolidated stockholders' equity, should be reduced proportionately.

ASC 830 normally does not require that changes in the translation adjustment be included in earnings. Prior to the liquidation of an investment in a subsidiary, the FASB believes that the effects of such translation adjustments are uncertain and should not be included in income. However, when there is a sale or liquidation of a subsidiary, the amount of the translation adjustment that is included in equity should be removed from equity and should be reported as part of the gain or loss in the period in which the transaction occurs.

Although Sonoma has not completely liquidated the investment in Valencia, the company is still required to recognize a portion of the translation adjustment in computing the gain or loss. According to **ASC 830**, a pro rata portion of the accumulated translation adjustment that is attributable to the subsidiary must be included in the calculation of the gain or loss on the sale of a portion of the subsidiary.

Therefore, the gain on the sale of the Valencia investment should be reduced by 30% of the (debit balance) cumulative translation adjustment related to this investment. Sonoma should disclose the amount by which the gain is decreased because of the adjustment for the cumulative translation adjustment.

In the presentation of comprehensive income, the adjustment to the translation adjustment should be identified as a reclassification adjustment so that the same amount is not included in both net income and in comprehensive income.

Authoritative support for the above memo can be found in the following references:

ASC 830
ASC 220
ASC 830

SOLUTIONS TO EXERCISES

E12-1 Multiple-Choice Translation and Remeasurement [AICPA Adapted]

Foreign Currency is Functional Currency	U.S. Dollar is Functional Currency
1. a – <u>\$215,000</u>	b – <u>\$225,000</u> (\$100,000 + \$50,000 + \$30,000 + \$45,000)
2. c – 400,000 LCU x \$0.44 = <u>\$176,000</u>	d – 120,000 LCU x = \$ 60,000 \$0.50 80,000 LCU x = 35,200 \$0.44 200,000 LCU x = <u>88,000</u> \$0.44 <u>\$183,200</u>
3. a – Indirect rates used 260,000 LCU / 1.8 LCU = <u>\$144,444</u>	c – 170,000 LCU / 1.5 LCU = \$113,333 90,000 LCU / 1.6 LCU = <u>56,250</u> <u>\$169,583</u>
4. d – 25,000 LCU / 2 LCU = <u>\$12,500</u>	b – 25,000 LCU / 2.2 LCU = <u>\$ 11,364</u>
5. a	d
6. a	c
7. a – <u>\$755,000</u> (All assets are translated at current rate)	c – <u>\$870,000</u> (\$75,000 + \$700,000 + \$25,000 + \$70,000)

E12-2 Multiple-Choice Questions on Translation and Foreign Currency Transactions [AICPA Adapted]

- | Foreign Currency
is Functional Currency | U.S. Dollar
is Functional Currency |
|---|--|
| <p>1. b – <u>\$10,000</u></p> <p style="padding-left: 20px;">\$120,000 = 2/15/X2 \$ value</p> <p style="padding-left: 20px;"><u>(110,000)</u> = 12/31/X1 \$ value</p> <p style="padding-left: 40px;">\$ = Foreign exchange</p> <p style="padding-left: 20px;"><u>10,000</u></p> <p style="padding-left: 40px;">gain</p> | <p>d – <u>\$40,000</u></p> <p style="padding-left: 20px;">\$10,000 = Foreign currency</p> <p style="padding-left: 40px;">transaction gain</p> <p style="padding-left: 20px;"><u>30,000</u> = Remeasurement gain</p> <p style="padding-left: 20px;"><u>\$40,000</u> = Foreign exchange gain</p> |
| <p>2. d – <u>\$17,000</u></p> <p style="padding-left: 20px;">\$13,000 = Preadjusted foreign exchange loss</p> <p style="padding-left: 20px;">4,000 = Foreign currency transaction loss</p> <p style="padding-left: 40px;">(\$60,000 - \$64,000)</p> <p style="padding-left: 20px;"><u>\$17,000</u> = Foreign exchange loss</p> | <p>b – <u>\$10,000</u></p> <p style="padding-left: 20px;">\$13,000 = Preadjusted foreign exchange loss</p> <p style="padding-left: 20px;">4,000 = Foreign currency transaction loss</p> <p style="padding-left: 40px;"><u>(7,000)</u> = Remeasurement gain</p> <p style="padding-left: 20px;"><u>\$10,000</u> = Net foreign exchange loss</p> |
| <p>3. c – <u>\$21,000</u></p> <p style="padding-left: 20px;">\$15,000 = Preadjusted foreign exchange loss</p> <p style="padding-left: 20px;">6,000 = Foreign currency transaction loss</p> <p style="padding-left: 40px;">(\$100,000 - \$106,000)</p> <p style="padding-left: 20px;"><u>\$21,000</u> = Foreign exchange loss</p> | <p>a – <u>\$41,000</u></p> <p style="padding-left: 20px;">\$15,000 = Preadjusted foreign exchange loss</p> <p style="padding-left: 20px;">6,000 = Foreign currency transaction loss</p> <p style="padding-left: 40px;"><u>20,000</u> = Remeasurement gain</p> <p style="padding-left: 20px;"><u>\$41,000</u> = Net foreign exchange loss</p> |
| <p>4. a – When the remeasurement method is used, monetary accounts are restated at the exchange rate at the balance sheet date, while nonmonetary accounts are restated using the exchange rate(s) at the date(s) the transaction(s) occurred which are reflected in the account balance. In this question, bonds payable and accrued liabilities are both monetary accounts and would be restated using the current exchange rate. Trading securities represent a nonmonetary account, however, Trading securities would be restated using the current rate because the account balance is stated at the market values at the balance sheet date. Inventories are also a nonmonetary asset. Since they are stated at cost, a historical exchange rate would be used to restate inventories.</p> | |

E12-2 (continued)

5. **b** – The current rate method of translation allows the use of a weighted average exchange rate for revenues and expenses that occur throughout the year. Since both sales and wages expense occur throughout the year, a weighted average exchange rate can be used for translation.

6. **a** – For hedges of net investments in a foreign entity, the amount of the change in fair value of the hedging instrument is recorded to other comprehensive income that then becomes part of the accumulated other comprehensive income. The change in the translation adjustment during the period is reported as a component of other comprehensive income and then carried forward to be accumulated in the stockholders' equity section of the balance sheet with the other components of other comprehensive income. Therefore, in this case in which a hedge of a net investment in a foreign entity is used, the exchange gain on the hedge is reported along with the change in the translation adjustment.

E12-3 Matching Key Terms

1. H
2. G
3. F
4. D
5. E
6. B
7. C
8. B
9. D
10. E
11. J
12. C

E12-4 Multiple-Choice Questions on Translation and Remeasurement

1. b –	Investment cost	\$160,000
	Less:	
	Book and fair values of sub's net assets	
	680,000 ringitts x \$0.21 x 0.90 =	<u>128,520</u>
	Goodwill	<u>\$ 31,480</u>

2. c –		<u>Dollars</u>		<u>Ringitts</u>
	Goodwill	\$10,500		RM 50,000 (\$10,500 / \$.21)
	Impairment	1,100 (RM 5,000 x \$0.22)		5,000 (RM 50,000 / 10)

3. **a** – Impairment loss = \$10,500 / 10 = \$1,050

4. b –	Sub's Net Income (€25,000 x \$1.24)	\$31,000
	Less:	
	Goodwill Impairment Loss	
	(€35,000 x 1.24 x 0.1)	<u>4,340</u>
	Income from Sub	<u>\$ 26,660</u>

Goodwill of €35,000 calculated as follows:

Amount paid for Common Stock	\$402,000 / \$1.2)	€335,000
Less: Fair value of identifiable assets		<u>€300,000</u>
Goodwill		<u>€ 35,000</u>

5. **d** – €5,000 x \$1.30 = \$6,500

6. d –	Investment cost on January 1, 20X5	\$402,000
	Less:	
	Book and fair values of sub's net assets:	
	€300,000 x \$1.20	<u>360,000</u>
	Goodwill	<u>\$ 42,000</u>

		<u>Dollars</u>		<u>Euros</u>
	Goodwill	\$42,000		€35,000 (\$ 42,000 / \$1.20)
	Impairment	<u>4,340</u> (€3,500 x \$1.24)		<u>3,500</u> (€35,000 / 10)
	Balance	<u>\$37,660</u>		<u>€31,500</u>

Translated balance \$41,580 (€31,500 x \$1.32)

Translation adjustment: \$41,580 minus \$37,660 = \$3,920 – use for question 7.

7. b –	Translation adjustment from translating the trial balance	\$12,000cr
	Translation adjustment from translating goodwill	<u>3,920cr</u>
	Total translation adjustment	<u>\$15,920cr</u>

E12-5 Translation

RoadTime Company
Trial Balance Translation
December 31, 20X1

	<u>Swiss Francs</u>	<u>Translation Rate</u>	<u>U.S. Dollars</u>
Cash	SFr 7,000	0.80	\$ 5,600
Accounts Receivable (net)	20,000	0.80	16,000
Receivable from Popular Creek	5,000	0.80	4,000
Inventory	25,000	0.80	20,000
Plant and Equipment	100,000	0.80	80,000
Cost of Goods Sold	70,000	0.75	52,500
Depreciation Expense	10,000	0.75	7,500
Operating Expense	30,000	0.75	22,500
Dividends Paid	15,000	0.77	11,550
Total Debits	<u>SFr 282,000</u>		<u>\$219,650</u>
Accumulated Depreciation	SFr 10,000	0.80	\$ 8,000
Accounts Payable	12,000	0.80	9,600
Bonds Payable	50,000	0.80	40,000
Common Stock	60,000	0.73	43,800
Sales	150,000	0.75	112,500
Total	<u>SFr 282,000</u>		<u>\$213,900</u>
Accumulated Other Comprehensive Income — Translation Adjustment (credit)			<u>5,750</u>
Total Credits			<u>\$219,650</u>

E12-6 Proof of Translation Adjustment

a. Popular Creek Corporation and Subsidiary
 Proof of Translation Adjustment
 Year Ended December 31, 20X1

	<u>SFr</u>	<u>Translation Rate</u>	<u>U.S. Dollars</u>
Net assets at beginning of year	SFr 60,000	0.73	\$ 43,800
Adjustment for changes in net asset position during year:			
Net income for year	40,000	0.75	30,000
Dividends paid	<u>(15,000)</u>	0.77	<u>(11,550)</u>
Net assets translated at:			
Rates during year			\$ 62,250
Rates at end of year	<u>SFr 85,000</u>	0.80	<u>68,000</u>
Change in other comprehensive income - translation adjustment during year - net increase			\$ 5,750
Accumulated other comprehensive income — translation adjustment — January 1			<u>-0-</u>
Change in other comprehensive income — translation adjustment December 31 (credit)			<u>\$ 5,750</u>

b. The change in the translation adjustment of \$5,750 is included as a credit in the other comprehensive income on the Statement of Comprehensive Income. The other comprehensive income is then accumulated and reported in the stockholders' equity section of the consolidated balance sheet.

Supporting computations:

Net income:

		<u>Balance Sheet, 12/31/X1</u>			
Sales	SFr 150,000	Net Assets	\$68,000	Common Stock	\$ 43,800
CGS	(70,000)			Ret. Earn.*	18,450
Depreciation	(10,000)			AOCI	5,750
Oper. Expenses	<u>(30,000)</u>	Total	<u>\$68,000</u>	Total	<u>\$ 68,000</u>
Net Income	<u>SFr 40,000</u>				
		Retained earnings, 1/1/X1		\$	-0-
		Net income			30,000
		Dividends			<u>(11,550)</u>
		*Retained earnings, 12/31/X1			<u>\$ 18,450</u>

E12-7 Remeasurement

RoadTime Company
Trial Balance Remeasurement
December 31, 20X1

	<u>Swiss Francs</u>	<u>Rate</u>	<u>U.S. Dollars</u>
Cash	SFr 7,000	0.80	\$ 5,600
Accounts Receivable (net)	20,000	0.80	16,000
Receivables from Popular Creek	5,000	0.80	4,000
Inventory	25,000	0.77	19,250
Plant and Equipment	100,000	0.74	74,000
Cost of Goods Sold	70,000	(a)	52,000
Depreciation Expense	10,000	0.74	7,400
Operating Expense	30,000	0.75	22,500
Dividends Paid	<u>15,000</u>	0.77	<u>11,550</u>
Total	<u>SFr 282,000</u>		<u>\$212,300</u>
Remeasurement Loss			<u>1,000</u>
Total Debits			<u>\$213,300</u>
Accumulated Depreciation	SFr 10,000	0.74	\$ 7,400
Accounts Payable	12,000	0.80	9,600
Bonds Payable	50,000	0.80	40,000
Common Stock	60,000	0.73	43,800
Sales	<u>150,000</u>	0.75	<u>112,500</u>
Total Credits	<u>SFr 282,000</u>		<u>\$213,300</u>

	<u>Swiss Francs</u>	<u>Rate</u>	<u>U.S. Dollars</u>
(a) Cost of Goods Sold:			
Beginning Inventory	SFr -0-	0.75	\$ -0-
Purchases	<u>95,000</u>	0.75	<u>71,250</u>
Goods Available for Sale	SFr 95,000		\$ 71,250
Less: Ending Inventory	<u>(25,000)</u>	0.77	<u>(19,250)</u>
Cost of Goods Sold	<u>SFr 70,000</u>		<u>\$ 52,000</u>

E12-8 Proof of Remeasurement Gain (Loss)

a. Popular Creek Corporation and Subsidiary
 Proof of Remeasurement Loss
 Year Ended Dec. 31, 20X1

Schedule 1
 Statement of Net Monetary Position

	<u>End of Year</u>	<u>Beginning of Year</u>
Monetary Assets:		
Cash	SFr 7,000	SFr 60,000
Accounts Receivable (net)	20,000	
Receivables from Popular Creek	<u>5,000</u>	
Total	<u>SFr 32,000</u>	<u>SFr 60,000</u>
Less Monetary Liabilities:		
Accounts Payable	SFr 12,000	SFr -0-
Bonds Payable	<u>50,000</u>	<u>-0-</u>
Total	<u>SFr(62,000)</u>	<u>SFr -0-</u>
Net Monetary Assets		<u>SFr 60,000</u>
Net Monetary Liabilities	<u>SFr 30,000</u>	
Change in net monetary investment during 20X1		<u>SFr (90,000)</u>

Schedule 2
 Analysis of Changes in Monetary Accounts

	<u>SFr</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Exposed net monetary asset Position – January 1	SFr 60,000	0.73	\$ 43,800
Adjustments for changes in the net monetary position during the year:			
Increases:			
From operations:			
Sales	150,000	0.75	112,500
From other sources	-0-		-0-
Decreases:			
From operations:			
Purchases	(95,000)	0.75	(71,250)
Cash expenses	(30,000)	0.75	(22,500)
From dividends	(15,000)	0.77	(11,550)
From purchase of plant and equipment	<u>(100,000)</u>	0.74	<u>(74,000)</u>
Net monetary position prior to remeasurement at year-end rates			\$(23,000)
Exposed net monetary liability Position – December 31	<u>SFr(30,000)</u>	0.80	<u>(24,000)</u>
Remeasurement loss			<u>\$ (1,000)</u>

E12-8 (continued)

Note: The issuance of the bonds payable has no effect on net monetary assets. Cash, a monetary asset, is increased and bonds payable, a monetary liability, is increased.

The Remeasurement Loss results from the decrease in the net monetary asset position during a period in which the exchange rate has increased. The end-of-period remeasured net liability position of \$24,000 is more than the net monetary liability position of \$23,000 remeasured using the rates in effect at the times of the transactions.

- b. The remeasurement loss is included in the period's consolidated statement of income.

E12-9 Translation with Strengthening U.S. Dollar

a.

RoadTime Company
Trial Balance Translation
December 31, 20X1

	<u>Swiss Francs</u>	<u>Rate</u>	<u>U.S. Dollars</u>
Cash	SFr 7,000	0.73	\$ 5,110
Accounts Receivable (net)	20,000	0.73	14,600
Receivable from Popular Creek	5,000	0.73	3,650
Inventory	25,000	0.73	18,250
Plant and Equipment	100,000	0.73	73,000
Cost of Goods Sold	70,000	0.75	52,500
Depreciation Expense	10,000	0.75	7,500
Operating Expense	30,000	0.75	22,500
Dividends Paid	<u>15,000</u>	0.74	<u>11,100</u>
Total	SFr 282,000		\$208,210
Accumulated Other Comprehensive Income — Translation Adjustment (debit)			4,850
Total Debits	<u>SFr 282,000</u>		<u>\$213,060</u>
Accumulated Depreciation	SFr 10,000	0.73	\$ 7,300
Accounts Payable	12,000	0.73	8,760
Bonds Payable	50,000	0.73	36,500
Common Stock	60,000	0.80	48,000
Sales	<u>150,000</u>	0.75	<u>112,500</u>
Total Credits	<u>SFr 282,000</u>		<u>\$213,060</u>

NOT REQUIRED: Proof of Translation Adjustment

	<u>SFr</u>	<u>Translation Rate</u>	<u>U.S. Dollars</u>
Net assets at beginning of year	SFr 60,000	0.80	\$ 48,000
Adjustment for changes in net asset position during year:			
Net income for year	40,000	0.75	30,000
Dividends paid	<u>(15,000)</u>	0.74	<u>(11,100)</u>
Net assets translated at:			
Rates during year			\$ 66,900
Rates at end of year	<u>SFr 85,000</u>	0.73	<u>(62,050)</u>
Change in other comprehensive Income — translation adjustment during year — net decrease			\$ 4,850
Accumulated other comprehensive income — translation adjustment — January 1			<u>-0-</u>
Accumulated other comprehensive income — translation adjustment — December 31 (debit)			<u>\$ 4,850</u>

E12-9 (continued)

- b. In Exercise 12-5, the U.S. dollar weakened against the Swiss franc; i.e., the direct exchange rate increased during the 20X1 year. Thus, the \$11,000 credit translation adjustment was the balancing item because the translated net assets of the foreign subsidiary were higher at the end of the year than the net assets at the beginning of the year adjusted for changes in the net assets that occurred during the year (income less dividends).

In Exercise 12-9, the U.S. dollar strengthened against the Swiss franc during the year; i.e., the direct exchange rate decreased during the year. Thus, the \$4,850 debit translation adjustment was the balancing item in Exercise 12-9 because the translated net assets at the end of the year were lower than the translated net assets at the beginning of the year as adjusted for changes during the year. The periodic change in the translation adjustment of \$4,850 is reported as a component of other comprehensive income on the Statement of Comprehensive Income, and is then accumulated with other comprehensive income items and reported in the stockholders' equity section of the consolidated balance sheet.

E12-10 Remeasurement with Strengthening U.S. Dollar

a.

RoadTime Company
 Trial Balance Remeasurement
 December 31, 20X1

	<u>Swiss Francs</u>	<u>Rate</u>	<u>U.S. Dollars</u>
Cash	SFr 7,000	0.73	\$ 5,110
Accounts Receivable (net)	20,000	0.73	14,600
Receivable from Popular Creek	5,000	0.73	3,650
Inventory	25,000	0.74	18,500
Plant and Equipment	100,000	0.77	77,000
Cost of Goods Sold	70,000	(a)	52,750
Depreciation Expense	10,000	0.77	7,700
Operating Expense	30,000	0.75	22,500
Dividends Paid	15,000	0.74	11,100
Total	<u>SFr 282,000</u>		<u>\$212,910</u>
Remeasurement Loss			<u>550</u>
Total Debits			<u>\$213,460</u>
Accumulated Depreciation	SFr 10,000	0.77	\$ 7,700
Accounts Payable	12,000	0.73	8,760
Bonds Payable	50,000	0.73	36,500
Common Stock	60,000	0.80	48,000
Sales	150,000	0.75	112,500
Total Credits	<u>SFr 282,000</u>		<u>\$213,460</u>

(a)	Cost of Goods Sold:	<u>Swiss Francs</u>	<u>Rate</u>	<u>U.S. Dollars</u>
	Beginning Inventory	SFr -0-	0.80	\$ -0-
	Purchases	<u>95,000</u>	0.75	<u>71,250</u>
	Goods Available for Sale	SFr 95,000		\$ 71,250
	Less: Ending Inventory	<u>(25,000)</u>	0.74	<u>(18,500)</u>
	Cost of Goods Sold	<u>SFr 70,000</u>		<u>\$ 52,750</u>

E12-10 (continued)

- b. In Exercise 12-5, the U.S. dollar weakened against the Swiss franc; i.e., the direct exchange rate increased during the 20X1 year. The \$1,000 remeasurement loss resulted from the decrease in the net monetary items during a period in which the exchange rate increased.

In Exercise 12-10, the U.S. dollar strengthened against the Swiss franc during the year. Note that the remeasurement gain or loss is computed only on monetary items. In E12-10, the net monetary items decreased during the year. Thus, the \$550 remeasurement loss in E12-10 results from the fact that the remeasured net monetary liability position at the end of the year is greater than the net monetary position prior to remeasurement at year-end rates. This is shown in the proof below which was not required for the exercise.

NOT REQUIRED: Proof of Remeasurement Loss

Schedule 1
Statement of Net Monetary Position

	<u>End of Year</u>	<u>Beginning of Year</u>
Monetary Assets:		
Cash	SFr 7,000	SFr 60,000
Accounts Receivable (net)	20,000	
Receivables from Popular Creek	5,000	
Total	<u>SFr 32,000</u>	<u>SFr 60,000</u>
Less Monetary Liabilities:		
Accounts Payable	SFr 12,000	SFr -0-
Bonds Payable	50,000	-0-
Total	<u>SFr(62,000)</u>	<u>SFr -0-</u>
Net Monetary Assets 1/1/X1		<u>SFr 60,000</u>
Net Monetary Liabilities 12/31/X1	<u>SFr 30,000</u>	
Change in net monetary investment during 20X1		<u>SFr(90,000)</u>

E12-10 (continued)

NOT REQUIRED: Proof of Remeasurement Loss (continued)

Schedule 2
Analysis of Changes in Monetary Accounts

	<u>SFr</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Exposed net monetary asset			
Position — January 1	SFr 60,000	0.80	\$ 48,000
Adjustments for changes in the net monetary position during the year:			
Increases:			
From operations:			
Sales	150,000	0.75	112,500
From other sources	-0-		-0-
Decreases:			
From operations:			
Purchases	(95,000)	0.75	(71,250)
Cash expenses	(30,000)	0.75	(22,500)
From dividends	(15,000)	0.74	(11,100)
From purchase of plant and equipment	<u>(100,000)</u>	0.77	<u>(77,000)</u>
Net monetary position prior to remeasurement at year-end rates			\$(21,350)
Exposed net monetary liability			
Position--December 31	<u>SFr (30,000)</u>	0.73	<u>(21,900)</u>
Remeasurement loss			<u>\$ (550)</u>

E12-11 Remeasurement and Translation of Cost of Goods Sold

a. Remeasurement:

	<u>Euros</u>	<u>Rate</u>	<u>U.S. Dollars</u>
Beginning Inventory	€ 220,000	1.29015	\$283,833
Purchases	<u>846,000</u>	1.39655	<u>1,181,481</u>
Goods Available	1,066,000		1,465,314
Less Ending Inventory	<u>(180,000)</u>	1.45000	<u>(261,000)</u>
Cost of Goods Sold	€ 886,000		\$1,204,314

b. Translation:

	<u>Euros</u>	<u>Rate</u>	<u>U.S. Dollars</u>
Cost of Goods Sold	€ 886,000	1.39655	\$1,237,343

E12-12 Equity-Method Entries for a Foreign Subsidiary

a.

Cash	19,680	
Investment in Thames Company		19,680
Receive dividend: \$19,680 = £15,000 x \$1.64 x 0.80		

b.

Investment in Thames Company	48,000	
Income from Subsidiary		48,000
Record equity accrual: \$48,000 = \$60,000 x 0.80		

Other Comprehensive Income — Translation Adjustment	5,120	
Investment in Thames Company		5,120
Parent's share of subsidiary's translation adjustment: \$5,120 = \$6,400 x 0.80		

c.

	<u>British Pounds</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Income Statement:			
Differential Jan. 1, 20X8 (10-year life)	£30,000	1.60	\$48,000
Amortization for 20X8	<u>(3,000)</u>	1.63	<u>(4,890)</u>
Remaining balance	<u>£27,000</u>		<u>\$43,110</u>

Balance Sheet:

Remaining balance on Dec. 31 translated at year-end rate	<u>£27,000</u>	1.65	<u>44,550</u>
Difference to translation adjustment			<u>\$ 1,440</u>

Note that the amount of the differential necessary for the balance sheet is \$44,550, while the amount, without any adjustment, would be \$43,110. Therefore, the differential portion of the parent company's investment must be increased by \$1,152 (\$1,440 x 0.80) through a debit to the Investment in Thames Company account and a corresponding credit to the Other Comprehensive Income—Translation Adjustment account. The differential adjustment adjusts to the amount needed for the balance sheet.

Investment in Thames Company	1,152	
Other Comprehensive Income — Translation Adjustment		1,152
Recognize translation adjustment for increase in differential.		

d.

Income from Subsidiary	3,912	
Investment in Thames Company		3,912
Amortization of trademark for 20X1: \$3,912 = £3,000 x \$1.63 x 0.80		

e. Other comprehensive income reports the periodic change in the translation adjustment. For 20X8, this would be the sum of a debit of \$5,120 which is the parent company's portion of the translation adjustment resulting from translating the subsidiary's trial balance, less the \$1,152 translation adjustment that is made only by the parent company due to the adjustment of the differential. Therefore, other comprehensive income would report \$3,968 (\$5,120 - \$1,152) due to foreign translations.

E12-13 Effects of a Change in the Exchange Rate — Translation and Other Comprehensive Income

a. Direct and indirect exchange rates:

	<u>Direct (\$/R 1)</u>	<u>Indirect (R/\$1)</u>
January 1, 20X6	\$0.03333 = R 1	R 30 = \$1
December 31, 20X6	\$0.02857 = R 1	R 35 = \$1
December 31, 20X7	\$ 0.025 = R 1	R 40 = \$1

The dollar strengthened during 20X6 because the number of rupees one U.S. dollar could acquire at the end of the year (35) is greater than the number of rupees that could be acquired at the beginning of the year (30); therefore, the value of the dollar has increased relative to the rupee during 20X6. The dollar continued to strengthen during 20X7.

b. Translated December 31, 20X6, balance sheet:

	<u>Subsidiary's Trial Balance (in rupees)</u>	<u>Direct Exchange Rate</u>	<u>Translated Trial Balance (in \$)</u>
Cash	R 100,000	\$0.02857	\$ 2,857
Receivables	450,000	\$0.02857	12,857
Inventory	680,000	\$0.02857	19,428
Fixed assets	1,000,000	\$0.02857	28,570
Total	<u>R 2,230,000</u>		<u>\$63,712</u>
Accumulated other comprehensive income — translation adjustment (debit)			<u>2,903</u>
Total debits			<u>\$66,615</u>
Current payables	R 260,000	\$0.02857	\$ 7,428
Long-term debt	1,250,000	\$0.02857	35,713
Common stock	500,000	\$0.03333	16,665
Retained earnings	220,000	\$0.03095*	6,809
Total credits	<u>R 2,230,000</u>		<u>\$66,615</u>

*\$.03095 = average of beginning and ending exchange rates, rounded to 4 decimal points: $$.030945 = [($.03333 + $.02857) / 2]$

(Not required: Proof of translation adjustment (debit) of \$2,903)

	<u>Rupees</u>	<u>Translation Rate</u>	<u>Dollars</u>
Net assets, 1/1/X6	R 500,000	\$0.03333	\$16,665
Adjustment for changes in net assets during year:			
Net income	<u>220,000</u>	\$0.03095	<u>6,809</u>
Net assets translated at:			
Rates during year			\$23,474
Rate at end of year	<u>R 720,000</u>	\$0.02857	<u>(20,570)</u>
Change in translation adjustment during year (debit)			<u>\$ 2,904*</u>

*Difference of \$1 (\$2,904 - \$2,903) due to rounding of exchange rates.

E12-13 (continued)

c. Translated December 31, 20X7, balance sheet:

	Subsidiary's Trial Balance (in rupees)	Direct Exchange Rate	Translated Trial Balance (in \$)
Cash	R 80,000	\$0.025	\$ 2,000
Receivables	550,000	\$0.025	13,750
Inventory	720,000	\$0.025	18,000
Fixed assets	900,000	\$0.025	22,500
Total	<u>R 2,250,000</u>		<u>\$56,250</u>
AOCI translation adjustment (debit)			<u>5,635</u>
Total debits			<u>\$61,885</u>
Current payables	R 340,000	\$0.025	\$ 8,500
Long-term debt	1,100,000	\$0.025	27,500
Common stock	500,000	\$0.03333	16,665
Retained earnings	310,000	(a)	9,220
Total credits	<u>R 2,250,000</u>		<u>\$61,885</u>

(a) The retained earnings in dollars would begin with the December 31, 20X6's, dollar balance (\$6,809) that would be carried forward. To this would be added 20X7's net income of R 90,000, which is the change in retained earnings in rupees multiplied by the average 20X7 exchange rate of \$.02679 [(\$.02857 + \$.025)/2] which equals \$2,411. Therefore, translated retained earnings on December 31, 20X7, is \$9,220 (\$9,220 = \$6,809 + \$2,411).

(Not required: Proof of translation adjustment (debit) of \$5,635)

	Rupees	Translation Rate	Dollars
Net assets, 1/1/X7	R 720,000	\$0.02857	\$20,570
Adjustment for changes in net assets during year:			
Net income	<u>90,000</u>	\$0.02679	<u>2,411</u>
Net assets translated at:			
Rates during year			\$22,981
Other comprehensive income — Rate at end of year	<u>R 810,000</u>	\$0.025	<u>(20,250)</u>
Change in other comprehensive Income — translation adjustment during year (debit)			\$ 2,731
Accumulated other comprehensive Income — translation adjustment, 1/1/X7			<u>2,904</u>
Accumulated other comprehensive Income — translation adjustment, 12/31/X7 (debit)			<u>\$ 5,635</u>

- d. The \$2,731 change in the accumulated other comprehensive income — translation adjustment during 20X7 would be reported as a component of other comprehensive income on 20X7's statement of other comprehensive income.

E12-14 Computation of Gain or Loss on Sale of Asset by Foreign Subsidiary

- a. Journal entries, in pesos, regarding the land:

1/1/X1	Land	P 2,000,000	
	Cash		P 2,000,000
12/31/X2	Cash	P 3,000,000	
	Land		P 2,000,000
	Gain on Sale of Land		P 1,000,000

- b. Amount of transaction gain (\$83,333), and remeasurement loss (\$33,333):

Note that under remeasurement the nonmonetary items are not adjusted for changes in the exchange rate. Therefore, land will be based on its historical cost of P 2,000,000 x \$0.10, the direct exchange rate on 1/1/X1, which equals a remeasured basis for the land of \$200,000.

The direct exchange rate on 1/1/X1 is \$.10 (\$1 = P 10); on 12/31/X1 is \$0.090909 (\$1 = P 11); and on 12/31/X2 is \$0.083333 (\$1 = P 12). The appropriate exchange rate to use to remeasure the gain on the sale of the land is \$0.83333 because the transaction is significant to the subsidiary, solitary to the operations, and occurred on a specific date, the last day of the year.

Remeasured December 31, 20X2 balance sheet:

	Subsidiary's Trial Balance (in pesos)	Direct Exchange Rate	Remeasured Trial Balance (in \$)
Cash	<u>P 3,000,000</u>	\$0.083333	<u>\$250,000</u>
Total	<u>P 3,000,000</u>		<u>\$250,000</u>
Remeasurement loss			<u>33,333</u>
Total debits			<u>\$283,333</u>
Common stock	P 2,000,000	\$0.10	\$200,000
Gain on sale of land	<u>P 1,000,000</u>	\$0.083333	<u>83,333</u>
Total credits	<u>P 3,000,000</u>		<u>\$283,333</u>

The effect on the parent company's net income (\$50,000 = \$83,333 – \$33,333) is the same as if the transactions had been transacted in U.S. dollars, which is an objective of the remeasurement method. The equivalent journal entries to those in part a. of the problem, if transacted in U.S. dollars, would be:

1/1/X1	Land (P 2,000,000 x \$0.10) Cash	\$200,000	\$200,000
12/31/X2	Cash (P 3,000,000 x \$0.08333) Land Gain on Sale of Land	\$250,000	\$200,000 \$ 50,000

E12-14 (continued)

- c. Amount of transaction gain (\$83,333), and other comprehensive income effect in 20X2 (\$15,151):

To compute the change in the translation adjustment for 20X2, which is an element of other comprehensive income for 20X2, it is necessary to prepare the translated trial balance as of the end of 20X1, as follows:

Translated December 31, 20X1, balance sheet:

	Subsidiary's Trial Balance (in pesos)	Direct Exchange Rate	Translated Trial Balance (in \$)
Land	<u>P 2,000,000</u>	\$0.090909	<u>\$181,818</u>
Total	<u>P 2,000,000</u>		<u>\$181,818</u>
Accumulated other comprehensive income — translation adjustment (debit)			<u>18,182</u>
Total debits			<u>\$200,000</u>
Common stock	<u>P 2,000,000</u>	\$0.10	<u>\$200,000</u>
Total credits	<u>P 2,000,000</u>		<u>\$200,000</u>

Note that the translation adjustment account has a debit balance of \$18,182 as of the end of 20X1. The next step is to translate the subsidiary's 12/31/X2 trial balance.

Translated December 31, 20X2, balance sheet:

	Subsidiary's Trial Balance (in pesos)	Direct Exchange Rate	Translated Trial Balance (in \$)
Cash	<u>P 3,000,000</u>	\$0.083333	<u>\$250,000</u>
Total	<u>P 3,000,000</u>		<u>\$250,000</u>
Accumulated other comprehensive income— translation adjustment (debit)			<u>33,333</u>
Total debits			<u>\$283,333</u>
Common stock	<u>P 2,000,000</u>	\$0.10	<u>\$200,000</u>
Gain on sale of land	<u>P 1,000,000</u>	\$0.083333	<u>83,333</u>
Total credits	<u>P 3,000,000</u>		<u>\$283,333</u>

The change in the translation adjustment during 20X2 is \$15,151 ($\$15,151 = \$33,333 - \$18,182$), which is reported on 20X2's statement of comprehensive income. The stockholders' equity section of the 12/31/X2 consolidated balance sheet would report the accumulated other comprehensive income which includes the accumulated translation adjustment, as of 12/31/X2, in the amount of \$33,333

E12-15* Intercompany Transactions

	<u>Measured in U.S. Dollars</u>	<u>Measured in British Pounds</u>
Initial inventory transfer date ($\$1.60 = \text{£}1$):		
Selling price ($\text{£}7,500 = \$12,000 / \1.60)	\$12,000	£7,500
Cost to parent	<u>(8,000)</u>	
Intercompany profit	<u>\$ 4,000</u>	
Balance sheet date ($\$1.70 = \text{£}1$):		
Inventory translation ($\$12,750 = \text{£}7,500 \times \1.70)	<u>\$12,750</u>	<u>£7,500</u>

- a. \$12,750 Inventory of United, Ltd., reported in U.S. dollar trial balance of consolidation worksheet.
 ($\$12,750 = \text{£}7,500 \times \1.70)
- b. \$ 8,750 ($\$8,750 = \$12,750 - \$4,000$ intercompany profit)

SOLUTIONS TO PROBLEMS

P12-16 Parent Company Journal Entries and Translation

a.	P ↓ NB	Investment cost Book value of investment on January 1, 20X1 Differential	<table border="0"> <tr> <td style="text-align: center;"><u>Canadian Dollars</u></td> <td style="text-align: center;"><u>Exchange Rate</u></td> <td style="text-align: center;"><u>U.S. Dollars</u></td> </tr> <tr> <td>C\$150,000</td> <td>0.80</td> <td>\$120,000</td> </tr> <tr> <td style="text-align: right;"><u>90,000</u></td> <td>0.80</td> <td style="text-align: right;"><u>72,000</u></td> </tr> <tr> <td style="text-align: right;"><u>C\$ 60,000</u></td> <td></td> <td style="text-align: right;"><u>\$ 48,000</u></td> </tr> </table>	<u>Canadian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>	C\$150,000	0.80	\$120,000	<u>90,000</u>	0.80	<u>72,000</u>	<u>C\$ 60,000</u>		<u>\$ 48,000</u>
<u>Canadian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>													
C\$150,000	0.80	\$120,000													
<u>90,000</u>	0.80	<u>72,000</u>													
<u>C\$ 60,000</u>		<u>\$ 48,000</u>													

	<u>Canadian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
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Income Statement:

Differential at date of acquisition:

Plant and equipment	C\$10,000		0.80	\$8,000	
Trademark		C\$50,000	0.80		\$40,000
Amortization this period:					
Plant and equipment (10 years)	(1,000)		0.75	(750)	
Trademark (10 years)		<u>(5,000)</u>	0.75		<u>(3,750)</u>

Remaining balance:

Plant and equipment	<u>C\$ 9,000</u>			\$7,250	
Trademark		<u>C\$45,000</u>			\$36,250

Balance Sheet:

Remaining balance on 12/31/X1 translated at year-end exchange rates:

Plant and equipment	<u>C\$ 9,000</u>		0.70	\$6,300	
Trademark		<u>C\$45,000</u>	0.70		<u>\$31,500</u>

Difference to OCI—translation adjustment:

Plant and equipment				<u>\$ 950</u>	
Trademark					<u>\$ 4,750</u>

Note that the differential adjustment is from the amounts of \$7,250 for plant and equipment and from \$36,250 for trademark. The required amounts for the consolidated balance sheet are \$6,300 for plant and equipment, and \$31,500 for trademark. Therefore, in each of these cases, the differential adjustment will reduce the amount of the differential component in the investment account, requiring a credit to the Investment in North Bay Company account with a corresponding debit to the Other Comprehensive Income—Translation Adjustment account. The differential adjustment adjusts to the correct amount necessary to prepare the consolidated balance sheet.

P12-16 (continued)

b. Entries on Par Company's books during 20X1:

(1)	Investment in North Bay Company	120,000	
	Cash		120,000
	Acquire North Bay Company.		
(2)	Investment in North Bay Company	15,000	
	Income from Subsidiary		15,000
	Equity in income of subsidiary: \$15,000 = C\$20,000 x 0.75 average exchange rate		
(3)	Foreign Currency Units (C\$)	6,000	
	Investment in North Bay Company		6,000
	Dividend from foreign subsidiary: \$6,000 = C\$8,000 x 0.75		
(4)	Income from Subsidiary	4,500	
	Investment in North Bay Company		4,500
	Amortization of differential:		
	Plant and equipment	\$ 750	
	Trademark	<u>3,750</u>	
	Total	<u>\$4,500</u>	
(5)	Other Comprehensive Income – Translation Adjustment	5,700	
	Investment in North Bay Company		5,700
	Recognize translation adjustment on differential:		
	Plant and equipment	\$ 950	
	Trademark	<u>4,750</u>	
	Total	<u>\$5,700</u>	

Note: The amount of the differential is being decreased as a result of the translation adjustment. Therefore, the investment account must be credited to reflect this decrease in the portion allocated to the differential.

P12-16 (continued)

c.

Par Company and North Bay Company
Proof of Translation Adjustment
Year Ended December 31, 20X1

	<u>Canadian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Net assets at beginning of year, 1/1/X1	C\$ 90,000	0.80	\$72,000
Adjustment for changes in assets position during year:			
Net income for year	20,000	0.75	15,000
Dividends paid	<u>(8,000)</u>	0.75	<u>(6,000)</u>
Net assets translated at rates in effect for those items			\$81,000
Net assets at end of year	<u>C\$102,000</u>	0.70	<u>71,400</u>
Change in other comprehensive income — translation adjustment during year — net decrease (debit)			<u>\$ 9,600</u>

December 31, 20X1

Other Comprehensive Income — Translation Adjustment	9,600	
Investment in North Bay Company		9,600
Parent's share (100%) of translation adjustment from translation of subsidiary's accounts.		

d.

Equivalent U.S. dollar value of C\$8,000 on December 31, 20X1:		
C\$8,000 x \$.70		\$5,600
Equivalent U.S. dollar value of C\$8,000 at date of receipt:		
C\$8,000 x \$.75		<u>6,000</u>
Foreign Currency Transaction Loss		<u>\$ 400</u>

December 31, 20X1

(7) Foreign Currency Transaction Loss	400	
Foreign Currency Units (C\$)		400
Recognize exchange loss on foreign currency units held.		

P12-17 Translation, Journal Entries, Consolidated Comprehensive Income, and Stockholders' Equity

a.

Vikix Inc.
 Trial Balance Translation
 December 31, 20X5

Item	Balance Kroner	Exchange Rate	Balance Dollars
Cash	NKr 150,000	0.21	\$ 31,500
Accounts Receivable (net)	200,000	0.21	42,000
Inventory	270,000	0.21	56,700
Property, Plant, and Equipment	600,000	0.21	126,000
Cost of Goods Sold	410,000	0.20	82,000
Operating Expenses	100,000	0.20	20,000
Depreciation Expense	50,000	0.20	10,000
Dividends Paid	40,000	0.19	7,600
Total Debits	<u>NKr 1,820,000</u>		<u>\$375,800</u>
Accumulated Depreciation	NKr 150,000	0.21	\$ 31,500
Accounts Payable	90,000	0.21	18,900
Notes Payable	190,000	0.21	39,900
Common Stock	450,000	0.18	81,000
Retained Earnings	250,000	0.18	45,000
Sales	690,000	0.20	138,000
Total	<u>NKr 1,820,000</u>		<u>\$354,300</u>
Accumulated Other Comprehensive Income — Translation Adjustment (credit)			<u>21,500</u>
Total Credits			<u>\$375,800</u>

P12-17 (continued)

b. Entries for 20X5:

January 1

Investment in Vikix Company Common	151,200	
Cash		151,200
Purchase of Vikix Inc.		

July 1

Cash	7,600	
Investment in Vikix Company		7,600
Dividend received from foreign subsidiary: \$7,600 = NKr40,000 x \$.19		

December 31

Investment in Vikix Company Common	26,000	
Income from Subsidiary		26,000
Equity in net income of foreign subsidiary: \$26,000 = Income of NKr130,000 x \$.20		

Investment in Vikix Company Common	21,500	
Other Comprehensive Income — Translation Adjustment		21,500

Parent's share of translation adjustment from translation of subsidiary's accounts:
\$21,500 x 1.00

Income from Subsidiary	3,600	
Investment in Vikix Company		3,600
Amortization of differential:		
Property, plant, and equipment	\$2,000	
Patent	1,600	
Total — see supporting schedule 2	<u>\$3,600</u>	

Investment in Vikix Company Common	4,020	
Other Comprehensive Income — Translation Adjustment		4,020
Translation adjustment applicable to the differential:		
Property, plant, and equipment	\$2,900	
Patent	1,120	
Total — see supporting schedule 2	<u>\$4,020</u>	

P12-17 (continued)

Schedule 1: Determining the differential for 20X5:

Investment cost at January 1, 20X5	\$ 151,200
Less: Book value of net assets acquired on January 1, 20X5 (Nkr700,000 x \$.18)	<u>(126,000)</u>
Differential	<u>\$ 25,200</u>
Differential allocated to:	
Property, plant, and equipment	\$ 18,000
Patent	<u>7,200</u>
Total	<u>\$ 25,200</u>

Schedule 2: Determining the differential amortization for 20X5:

	<u>Norwegian Kroner</u>	<u>Translation Rate</u>	<u>U.S. Dollars</u>
Property, plant, and equipment:			
Income statement:			
Difference at beginning of year	Nkr 100,000	0.18	\$18,000
Amortization for 20X5 (Nkr100,000 / 10 years)	<u>(10,000)</u>	0.20	<u>(2,000)</u>
Remaining balances	<u>Nkr 90,000</u>		\$16,000
Balance sheet:			
Remaining balance on December 31, 20X5, translated at year-end exchange rate	<u>Nkr 90,000</u>	0.21	<u>18,900</u>
Difference to other comprehensive income — translation adjustment			<u>\$ 2,900</u>
Patent:			
Income statement:			
Difference at beginning of year	Nkr 40,000	0.18	\$ 7,200
Amortization for 20X5 (Nkr40,000 / 5 years)	<u>(8,000)</u>	0.20	<u>(1,600)</u>
Remaining balances	<u>Nkr 32,000</u>		<u>\$ 5,600</u>
Balance sheet:			
Remaining balance on December 31, 20X5, translated at year-end exchange rate	<u>Nkr 32,000</u>	0.21	<u>6,720</u>
Difference to other comprehensive income — translation adjustment			<u>\$ 1,120</u>

Note that the property, plant, and equipment portion of the differential must be increased from \$16,000 to \$19,000, requiring a debit of \$2,900 to the investment account. The portion of the differential attributable to patent must be increased from \$5,600 to \$6,720, requiring a debit of \$1,120 to the investment account. The corresponding credit is to the Other Comprehensive Income – Translation Adjustment account (\$4,020 = \$2,900 + \$1,120).

P12-17 (continued)

c. Taft's consolidated comprehensive income for 20X5:

1. Income from Taft's operations for 20X5, exclusive of income from the Norwegian subsidiary	\$ 275,000
2. Add: Income from the Norwegian subsidiary for 20X5	26,000
3. Deduct: Amortization of differential for 20X5	<u>(3,600)</u>
Taft's Net Income	\$ 297,400
4. Add: Translation Adjustment (\$21,500 + \$4,020)	<u>25,520</u>
Taft's Consolidated Comprehensive Income	<u><u>\$ 322,920</u></u>

d. Taft's consolidated stockholders' equity at December 31, 20X5:

1. Taft's stockholders' equity at Jan. 1, 20X5	\$3,500,000
2. Add: Net income for 20X5	297,400
3. Deduct: Dividends declared by Taft during 20X5	(100,000)
4. Add: Accumulated other comprehensive income:	
Foreign currency translation adjustment	<u>25,520</u>
Consolidated Stockholders' Equity at Dec. 31, 20X5	<u><u>\$3,722,920</u></u>

P12-18 Remeasurement, Journal Entries, Consolidated Net Income, and Stockholders' Equity

a. Schedule remeasuring the trial balance into U.S. dollars:

<u>Item</u>	<u>Balance Kroner</u>	<u>Exchange Rate</u>	<u>Balance Dollars</u>
Cash	NKr 150,000	0.21	\$ 31,500
Accounts Receivable (net)	200,000	0.21	42,000
Inventory	270,000	0.205	55,350
Property, Plant, and Equipment	600,000	0.18*	108,000
Cost of Goods Sold	410,000	(a)	75,450
Operating Expenses	100,000	0.20	20,000
Depreciation Expense	50,000	0.18*	9,000
Dividends Paid	40,000	0.19	7,600
Total	<u>NKr 1,820,000</u>		<u>\$348,900</u>
Remeasurement Loss			900
Total Debits			<u>\$349,800</u>
Accumulated Depreciation	NKr 150,000	0.18*	\$ 27,000
Accounts Payable	90,000	0.21	18,900
Notes Payable	190,000	0.21	39,900
Common Stock	450,000	0.18*	81,000
Retained Earnings	250,000	0.18*	45,000
Sales	690,000	0.20	138,000
Total Credits	<u>NKr 1,820,000</u>		<u>\$349,800</u>

* 0.18 = exchange rate at January 1, 20X5, the date the subsidiary was acquired by Taft Company

(a)	<u>Norwegian Kroner</u>	<u>Exchange Rate</u>	<u>U.S. Dollar</u>
Cost of goods sold:			
Beginning inventory			
(CGS of NKr410,000 + ending			
inventory of NKr270,000			
minus purchases of			
NKr420,000 = Beg. Inv.)	NKr 260,000	0.18	\$ 46,800
Purchases	<u>420,000</u>	0.20	<u>84,000</u>
Cost of goods available	NKr 680,000		\$130,800
Less ending inventory	<u>(270,000)</u>	0.205	<u>(55,350)</u>
Cost of goods sold	<u>NKr 410,000</u>		<u>\$ 75,450</u>

P12-18 (continued)

b. Journal entries for 20X5:

January 1

Investment in Vikix Company Common	151,200	
Cash		151,200
Purchase of Vikix, Inc.		

July 1

Cash	7,600	
Investment in Vikix Company Common		7,600
Dividend received from foreign subsidiary: \$7,600 = NKr40,000 x \$.19		

December 31

Investment in Vikix Company Common	32,650	
Income from Subsidiary		32,650

Equity in net income of foreign subsidiary:

Income from the Norwegian sub:

Sales	\$138,000
Less:	
Cost of goods sold	(75,450)
Operating expenses	(20,000)
Depreciation expense	<u>(9,000)</u>
Income	\$ 33,550
Less: Remeasurement loss	<u>(900)</u>
Income recorded by Taft	<u>\$ 32,650</u>

Income from Subsidiary	3,240	
Investment in Vikix Company Common		3,240

Amortization of the differential
(See Schedule 1 below).

Schedule 1: Determining and amortizing the differential for 20X5:

Investment cost at January 1, 20X5	\$151,200
Book value of net assets acquired on January 1, 20X5 (NKr700,000 x \$.18)	<u>(126,000)</u>
Differential	<u>\$ 25,200</u>

Differential allocated to:

Property, plant, and equipment	\$ 18,000
Patent	<u>7,200</u>
Total	<u>\$ 25,200</u>

Amortization for 20X5:

Property, plant, and equipment (\$18,000 / 10 years)	\$ 1,800
Patent (\$7,200 / 5 years)	<u>1,440</u>
Total	<u>\$ 3,240</u>

P12-18 (continued)

c. Consolidated net income for 20X5:

1. Income from Taft's operations for 20X5, exclusive of income from the Norwegian subsidiary	\$275,000
2. Add: Income from the Norwegian subsidiary	32,650
3. Deduct: Amortization of differential for 20X5	<u>(3,240)</u>
Consolidated net income for 20X5	<u>\$304,410</u>

d. Consolidated stockholders' equity at December 31, 20X5:

1. Taft's stockholders' equity at January 1, 20X5	\$3,500,000
2. Add: Consolidated net income for 20X5	304,410
3. Deduct: Dividends declared by Taft during 20X5	<u>(100,000)</u>
Consolidated stockholders' equity at December 31, 20X5	<u>\$3,704,410</u>

P12-19 Proof of Translation Adjustment

	<u>Norwegian Kroner</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Net assets at beginning of year	NKr 700,000	0.18	\$126,000
Adjustments for changes in net assets position during 20X5:			
Net income	130,000	0.20	26,000
Dividends paid	<u>(40,000)</u>	0.19	<u>(7,600)</u>
Net assets translated at:			
Rates during year			\$144,400
Rates at end of year	<u>NKr 790,000</u>	0.21	<u>165,900</u>
Change in other comprehensive income — translation adjustment during year			\$ 21,500
Accumulated other comprehensive income — translation adjustment — January 1			<u>-0-</u>
Accumulated other comprehensive income — translation adjustment — December 31 (credit)			<u>\$ 21,500</u>

P12-20 Remeasurement Gain or Loss

Proof of remeasurement loss for 20X5:

	<u>Norwegian Kroner</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Exposed net monetary liability position at January 1	NKr (60,000)	0.18	\$(10,800)
Adjustments for changes in net monetary position during 20X5:			
Increases:			
From operations:			
Sales	NKr 690,000	0.20	138,000
Decreases:			
From operations:			
Purchases	(420,000)	0.20	(84,000)
Operating expenses	(100,000)	0.20	(20,000)
From dividends	<u>(40,000)</u>	0.19	<u>(7,600)</u>
Net monetary asset position prior to remeasurement at year-end rates			\$ 15,600
Exposed net monetary asset position at December 31	<u>NKr 70,000</u>	0.21	<u>(14,700)</u>
Remeasurement loss			<u>\$ 900</u>

P12-21 Translation and Calculation of Translation Adjustment

a.

DaSilva Company
Trial Balance Translation
December 31, 20X4

		<u>Reals</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Cash	BRL	57,700	0.20	\$ 11,540
Accounts Receivable (net)		82,000	0.20	16,400
Inventory		95,000	0.20	19,000
Prepaid Insurance		2,400	0.20	480
Plant and Equipment		350,000	0.20	70,000
Intangible Assets		30,000	0.20	6,000
Cost of Goods Sold		230,000	0.25	57,500
Insurance Expense		3,200	0.25	800
Depreciation Expense		32,500	0.25	8,125
Amortization Expense		12,000	0.25	3,000
Operating Expense		152,300	0.25	38,075
Dividends Paid		25,000	Sch. A	6,250
Total		<u>BRL 1,072,100</u>		<u>\$237,170</u>
Accumulated Other				
Comprehensive Income —				
Translation Adjustment (debit)				30,250
Total Debits				<u>\$ 267,420</u>
Accumulated Depreciation	BRL	100,000	0.20	\$ 20,000
Accounts Payable		24,000	0.20	4,800
Income Tax Payable		27,000	0.20	5,400
Interest Payable		1,100	0.20	220
Notes Payable		20,000	0.20	4,000
Bonds Payable		120,000	0.20	24,000
Common Stock		80,000	0.30	24,000
Additional Paid-In Capital		150,000	0.30	45,000
Retained Earnings		50,000	0.30	15,000
Sales		500,000	0.25	125,000
Total Credits		<u>BRL 1,072,100</u>		<u>\$267,420</u>
<u>Schedule A</u>				
Dividends April 7	BRL	10,000	0.28	\$ 2,800
Dividends October 9		15,000	0.23	3,450
		<u>BRL 25,000</u>		<u>\$ 6,250</u>

P12-21 (continued)

- b. Schedule to compute the accumulated other comprehensive income – translation adjustment as of December 31, 20X4.

	<u>Reals</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Net assets at beginning of year	BRL 280,000	0.30	\$84,000
Adjustment for changes:			
Net income for year	70,000	0.25	17,500
Dividends paid: April 7	(10,000)	0.28	(2,800)
October 9	<u>(15,000)</u>	0.23	<u>(3,450)</u>
Net assets translated at:			
Rates during year			\$95,250
Rates at end of year	<u>BRL 325,000</u>	0.20	<u>65,000</u>
Accumulated other comprehensive Income — translation adjustment (debit)			<u>\$30,250</u>

Another way of interpreting the direction (debit or credit) of the translation adjustment is to consider the translated balance sheets, as follows:

Translated balance sheet, 1/1/X4

<table border="0" style="width: 100%;"> <tr> <td style="width: 60%;">Net assets</td> <td style="text-align: right; width: 20%;"><u>\$84,000</u></td> </tr> </table>	Net assets	<u>\$84,000</u>	<table border="0" style="width: 100%;"> <tr> <td style="width: 60%;">Stockholders' equity</td> <td style="text-align: right; width: 20%;"><u>\$84,000</u></td> </tr> </table>	Stockholders' equity	<u>\$84,000</u>
Net assets	<u>\$84,000</u>				
Stockholders' equity	<u>\$84,000</u>				

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

Translated balance sheet, 12/31/X4

<table border="0" style="width: 100%;"> <tr> <td style="width: 60%;">Net assets</td> <td style="text-align: right; width: 20%;">\$65,000</td> </tr> </table>	Net assets	\$65,000	<table border="0" style="width: 100%;"> <tr> <td style="width: 60%;">Stockholders' equity (from 1/1/X4)</td> <td style="text-align: right; width: 20%;">\$84,000</td> </tr> <tr> <td>20X4 Income</td> <td style="text-align: right;">\$17,500</td> </tr> <tr> <td>Less dividends</td> <td style="text-align: right;">(6,250)</td> </tr> <tr> <td></td> <td style="text-align: right;">11,250</td> </tr> <tr> <td>Accumulated other comprehensive income — translation adjustment</td> <td style="text-align: right;">(30,250)</td> </tr> <tr> <td>Total</td> <td style="text-align: right;"><u>\$65,000</u></td> </tr> </table>	Stockholders' equity (from 1/1/X4)	\$84,000	20X4 Income	\$17,500	Less dividends	(6,250)		11,250	Accumulated other comprehensive income — translation adjustment	(30,250)	Total	<u>\$65,000</u>
Net assets	\$65,000														
Stockholders' equity (from 1/1/X4)	\$84,000														
20X4 Income	\$17,500														
Less dividends	(6,250)														
	11,250														
Accumulated other comprehensive income — translation adjustment	(30,250)														
Total	<u>\$65,000</u>														

The debit balance of \$30,250 in the accumulated other comprehensive income – translation adjustment, is necessary to “balance” the translated balance sheet.

P12-22 Remeasurement and Proof of Remeasurement Gain or Loss

a.

DaSilva Company
 Trial Balance Remeasurement
 December 31, 20X4

	<u>Reals</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Cash	BRL 57,700	0.20	\$ 11,540
Accounts Receivable (net)	82,000	0.20	16,400
Inventory	95,000	0.25	23,750
Prepaid Insurance	2,400	0.30	720
Plant and Equipment	350,000	Sch. A	103,000
Intangible Assets	30,000	0.30	9,000
Cost of Goods Sold	230,000	Sch. B	62,250
Insurance Expense	3,200	0.30	960
Depreciation Expense	32,500	Sch. C	9,600
Amortization Expense	12,000	0.30	3,600
Operating Expense	152,300	0.25	38,075
Dividends Paid	25,000	Sch. D	6,250
Total Debits	<u>BRL 1,072,100</u>		<u>\$285,145</u>
Accumulated Depreciation	BRL 100,000	Sch. E	\$ 29,850
Accounts Payable	24,000	0.20	4,800
Income Tax Payable	27,000	0.20	5,400
Interest Payable	1,100	0.20	220
Notes Payable	20,000	0.20	4,000
Bonds Payable	120,000	0.20	24,000
Common Stock	80,000	0.30	24,000
Additional Paid-In Capital	150,000	0.30	45,000
Retained Earnings	50,000	0.30	15,000
Sales	500,000	0.25	125,000
Total	<u>BRL 1,072,100</u>		<u>\$277,270</u>
Remeasurement Gain			<u>7,875</u>
Total Credits			<u>\$285,145</u>

P12-22 (continued)

	<u>Reals</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
<u>Schedule A</u>			
Plant and Equipment			
Before January 1, 20X4	BRL 250,000	0.30	\$ 75,000
April 7, 20X4	<u>100,000</u>	0.28	<u>28,000</u>
	<u>BRL 350,000</u>		<u>\$103,000</u>

<u>Schedule B</u>			
Cost of Goods Sold			
Beginning Inventory*	BRL 95,000	0.30	\$ 28,500
Purchases	<u>230,000</u>	0.25	<u>57,500</u>
Goods Available	BRL 325,000		\$ 86,000
Less Ending Inventory	<u>(95,000)</u>	0.25	<u>(23,750)</u>
	<u>BRL 230,000</u>		<u>\$ 62,250</u>

*Acquired before January 1, 20X4; use the exchange rate at date parent acquired subsidiary.

<u>Schedule C</u>			
Depreciation Expense			
Before January 1, 20X4	BRL 25,000	0.30	\$ 7,500
April 7, 20X4	<u>7,500</u>	0.28	<u>2,100</u>
	<u>BRL 32,500</u>		<u>\$ 9,600</u>

<u>Schedule D</u>			
Dividends			
April 7, 20X4	BRL 10,000	0.28	\$ 2,800
Oct. 9, 20X4	<u>15,000</u>	0.23	<u>3,450</u>
	<u>BRL 25,000</u>		<u>\$ 6,250</u>

<u>Schedule E</u>			
Accumulated Depreciation			
Before January 1, 20X4:			
January 1, 20X1	BRL 80,000	0.30	\$ 24,000
July 10, 20X2	12,500	0.30	3,750
April 7, 20X4	<u>7,500</u>	0.28	<u>2,100</u>
	<u>BRL 100,000</u>		<u>\$ 29,850</u>

P12-22 (continued)

b. Proof of Remeasurement Gain

Schedule 1: Statement of Net Monetary Position:

	<u>End of Year</u>	<u>Beginning of Year</u>
Monetary Assets:		
Cash	BRL 57,700	BRL 62,000
Accounts Receivable (net)	<u>82,000</u>	<u>83,900</u>
Total	<u>BRL 139,700</u>	<u>BRL 145,900</u>
Monetary Liabilities:		
Accounts Payable	BRL 24,000	BRL 20,000
Income Taxes Payable	27,000	30,000
Interest Payable	1,100	1,000
Notes Payable	20,000	20,000
Bonds Payable	<u>120,000</u>	<u>120,000</u>
Total	<u>BRL (192,100)</u>	<u>BRL (191,000)</u>
Net Monetary Liabilities	<u>BRL (52,400)</u>	<u>BRL (45,100)</u>
Increase in net monetary liabilities during 20X4		<u>BRL (7,300)</u>

Schedule 2: Analysis of Changes in Monetary Accounts:

	<u>Reals</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Exposed net monetary liability position-January 1, 20X4	BRL (45,100)	0.30	\$(13,530)
Increases			
From operations:			
Sales	500,000	0.25	125,000
Decreases			
From operations:			
Purchases	(230,000)	0.25	(57,500)
Operating expenses	(152,300)	10,000 x 0.28	(38,075)
From dividends	(25,000)	15,000 x 0.23	(6,250)
From purchases of plant and equipment	<u>(100,000)</u>	0.28	<u>(28,000)</u>
Net monetary position prior to remeasurement at year- end rates			\$(18,355)
Exposed net monetary liability Position-December 31, 20X4	<u>BRL (52,400)</u>	0.20	<u>(10,480)</u>
Remeasurement gain			<u>\$ 7,875</u>

P12-23 Translation

a.	Western Ranching Company Trial Balance Translation December 31, 20X3		
	<u>Australian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Cash	A\$ 44,100	0.60	\$ 26,460
Accounts Receivable (net)	72,000	0.60	43,200
Inventory	86,000	0.60	51,600
Plant and Equipment	240,000	0.60	144,000
Cost of Goods Sold	330,000	0.65	214,500
Depreciation Expense	24,000	0.65	15,600
Operating Expense	131,500	0.65	85,475
Interest Expense	5,700	0.65	3,705
Dividends Declared	<u>9,000</u>	0.67	<u>6,030</u>
Total			\$590,570
Accumulated Other Comprehensive Income — Translation Adjustment(debit)			<u>16,760</u>
Total Debits	<u>A\$942,300</u>		<u>\$607,330</u>
Accumulated Depreciation	A\$ 60,000	0.60	\$ 36,000
Accounts Payable	53,800	0.60	32,280
Payable to Alamo, Inc.	10,800	0.60	6,480
Interest Payable	3,000	0.60	1,800
12% Bonds Payable	100,000	0.60	60,000
Premium on Bonds	5,700	0.60	3,420
Common Stock	90,000	0.70	63,000
Retained Earnings	40,000	0.70	28,000
Sales	<u>579,000</u>	0.65	<u>376,350</u>
Total Credits	<u>A\$942,300</u>		<u>\$607,330</u>

b. Schedule to prove translation adjustment:

	<u>Australian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Net assets at beginning of year	A\$130,000	0.70	\$ 91,000
Adjustments for changes:			
Net income for year	87,800	0.65	57,070
Dividends paid	<u>(9,000)</u>	0.67	<u>(6,030)</u>
Net assets translated:			
Rates during year			\$142,040
Rates at end of year	<u>A\$208,800</u>	0.60	<u>(125,280)</u>
Change in other comprehensive Income — translation adjustment (debit)			\$ 16,760
Accumulated other comprehensive Income — translation adjustment, 1/1			<u>-0-</u>
Accumulated other comprehensive Income — translation adjustment, 12/31			<u>\$ 16,760</u>

P12-24 Parent Company Journal Entries and Translation

	Australian Dollar	Rate	US Dollar
Total Purchase Price	A\$ 200,000	0.70	\$ 140,000
Total Fair Value	A\$ 250,000	0.70	\$ 175,000
Less:			
Common Stock	A\$ 90,000	0.70	\$ 63,000
Retained Earnings	A\$ 40,000	0.70	\$ 28,000
Building & Equipment Differential	<u>A\$ 40,000</u>	0.70	<u>\$ 28,000</u>
Patent Value	<u>A\$ 80,000</u>		<u>\$ 56,000</u>

	<u>Australian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>	
Balance Jan. 1, 20X3				
Differential:				
Buildings and Equipment	A\$40,000	0.70	\$28,000	
Patent	80,000	0.70		\$56,000
Amortization:				
Buildings and Equipment (10 years)	(4,000)	0.65	(2,600)	
Patent (10 years)	<u>(8,000)</u>	0.65	<u>(5,200)</u>	
Remaining Balance	<u>A\$108,000</u>		\$25,400	\$50,800
Adjusted balance Dec. 31, 20X3				
Buildings and Equipment	<u>A\$36,000</u>	0.60	(21,600)	
Patent	<u>A\$72,000</u>	0.60	<u>(43,200)</u>	
Differential Translation Adjustment:				
Patent				\$ 7,600
Buildings and Equipment				<u>3,800</u>
Total Differential Translation Adjustment				<u>\$ 11,400</u>

Note: The differential translation adjustment is necessary to decrease the buildings and equipment component of the parent company's differential from \$20,320 to \$17,280, and to decrease the patent component from \$40,640 to \$34,560. Thus, a credit will be made to the parent company's investment account for the total of \$9,120 (\$3,040 + \$6,080) with a corresponding debit to the parent company's Other Comprehensive Income – Translation Adjustment account.

P12-24 (continued)Parent company journal entries 20X3:

- | | | | | | | | |
|--------------------------------|--|--------------------------------|---------|--|--------------------------------|--|---------|
| (1) | <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Investment in Western Ranching</td> <td style="width: 20%; text-align: right;">140,000</td> <td style="width: 20%;"></td> </tr> <tr> <td style="padding-left: 20px;">Cash</td> <td></td> <td style="text-align: right;">140,000</td> </tr> </table> | Investment in Western Ranching | 140,000 | | Cash | | 140,000 |
| Investment in Western Ranching | 140,000 | | | | | | |
| Cash | | 140,000 | | | | | |
| | Acquire foreign investment. | | | | | | |
| (2) | <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Cash</td> <td style="width: 20%; text-align: right;">4,824</td> <td style="width: 20%;"></td> </tr> <tr> <td style="padding-left: 20px;">Investment in Western Ranching</td> <td></td> <td style="text-align: right;">4,824</td> </tr> </table> | Cash | 4,824 | | Investment in Western Ranching | | 4,824 |
| Cash | 4,824 | | | | | | |
| Investment in Western Ranching | | 4,824 | | | | | |
| | Receive dividend:
A\$9,000 x 0.80 x \$.67 | | | | | | |
| (3) | <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Investment in Western Ranching</td> <td style="width: 20%; text-align: right;">45,656</td> <td style="width: 20%;"></td> </tr> <tr> <td style="padding-left: 20px;">Income from Western Ranching</td> <td></td> <td style="text-align: right;">45,656</td> </tr> </table> | Investment in Western Ranching | 45,656 | | Income from Western Ranching | | 45,656 |
| Investment in Western Ranching | 45,656 | | | | | | |
| Income from Western Ranching | | 45,656 | | | | | |
| | Equity accrual for percentage of subsidiary's income: | | | | | | |
| | A\$ | U.S.\$ | | | | | |
| | Sales | \$376,350 | | | | | |
| | Cost of goods sold | (214,500) | | | | | |
| | Depreciation expense | (15,600) | | | | | |
| | Operating expense | (85,475) | | | | | |
| | Interest expense | (3,705) | | | | | |
| | Income | \$ 57,070 | | | | | |
| | Average exchange rate | x 0.65 | | | | | |
| | U.S. dollar equivalent | \$ 57,070 | | | | | |
| | Parent's percent | x 0.80 | | | | | |
| | Equity accrual | \$ 45,656 | | | | | |
- | | | | | | | | |
|--------------------------------|--|------------------------------|-------|--|--------------------------------|--|-------|
| (4) | <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Income from Western Ranching</td> <td style="width: 20%; text-align: right;">6,240</td> <td style="width: 20%;"></td> </tr> <tr> <td style="padding-left: 20px;">Investment in Western Ranching</td> <td></td> <td style="text-align: right;">6,240</td> </tr> </table> | Income from Western Ranching | 6,240 | | Investment in Western Ranching | | 6,240 |
| Income from Western Ranching | 6,240 | | | | | | |
| Investment in Western Ranching | | 6,240 | | | | | |
| | Amortization of differential: | | | | | | |
| | Buildings and equipment | = \$2,600 | | | | | |
| | Patent | = 5,200 | | | | | |
| | <u>\$7,800</u> | x 0.80 = 6,240 | | | | | |
- | | | | | | | | | | | |
|--------------------------------|---|------------------------------|--|--|------------------------|-------|--|--------------------------------|--|-------|
| (5) | <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Other Comprehensive Income —</td> <td style="width: 20%;"></td> <td style="width: 20%;"></td> </tr> <tr> <td style="padding-left: 20px;">Translation Adjustment</td> <td style="text-align: right;">9,120</td> <td></td> </tr> <tr> <td style="padding-left: 20px;">Investment in Western Ranching</td> <td></td> <td style="text-align: right;">9,120</td> </tr> </table> | Other Comprehensive Income — | | | Translation Adjustment | 9,120 | | Investment in Western Ranching | | 9,120 |
| Other Comprehensive Income — | | | | | | | | | | |
| Translation Adjustment | 9,120 | | | | | | | | | |
| Investment in Western Ranching | | 9,120 | | | | | | | | |
| | Translation adjustment related to decrease in differential: | | | | | | | | | |
| | Buildings and equipment | = \$3,800 | | | | | | | | |
| | Patent | = 7,600 | | | | | | | | |
| | <u>\$11,400</u> | x 0.80 = 9,120 | | | | | | | | |
- | | | | | | | | | | | |
|--------------------------------|---|------------------------------|--|--|------------------------|--------|--|--------------------------------|--|--------|
| (6) | <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Other Comprehensive Income —</td> <td style="width: 20%;"></td> <td style="width: 20%;"></td> </tr> <tr> <td style="padding-left: 20px;">Translation Adjustment</td> <td style="text-align: right;">13,408</td> <td></td> </tr> <tr> <td style="padding-left: 20px;">Investment in Western Ranching</td> <td></td> <td style="text-align: right;">13,408</td> </tr> </table> | Other Comprehensive Income — | | | Translation Adjustment | 13,408 | | Investment in Western Ranching | | 13,408 |
| Other Comprehensive Income — | | | | | | | | | | |
| Translation Adjustment | 13,408 | | | | | | | | | |
| Investment in Western Ranching | | 13,408 | | | | | | | | |
| | Parent company's share of translation adjustment from subsidiary:
\$13,408 = \$16,760 x 0.80 | | | | | | | | | |

P12-24 (continued)

Entries posted to T-accounts (not required):

	Investment in Western Ranching			Income from Western Ranching	
Acquisition Price	140,000				
80% Net Income	45,656			45,656	80% Net Income
		4,824	80% Dividends		
		6,240	80% Amort. of Diff.	6,240	
		9,120	Diff. Translation		
		13,408	80% of WR Trans. Adj.		
Ending Balance	152,064			39,416	Ending Balance

P12-25 Consolidation Worksheet after Translation

Book Value Calculations:

	NCI 20%	+	Alamo 80%	=	Common Stock	+	Retained Earnings
Beginning book value	18,200		72,800		63,000		28,000
+ Net Income	11,414		45,656				57,070
- Dividends	(1,206)		(4,824)				(6,030)
Ending book value	28,408		113,632		63,000		79,040

Basic elimination entry

Common stock	63,000
Retained earnings	28,000
Income from Western Ranching	45,656
NCI in NI of Western Ranching	11,414
Dividends declared	6,030
Investment in Western Ranching	113,632
NCI in NA of Western Ranching	28,408

Book Value Other Comprehensive Income Entry:

Investment in Western Ranching	13,408
NCI in NA of Western Ranching	3,352
OCI from Western Ranching	13,408
OCI to NCI in Western Ranching	3,352

Excess Value (Differential) Calculations:

	NCI 20%	+	Alamo 80%	=	Plant and Equipment	+	Patent	+	Acc. Depr.
Beginning balance	16,800		67,200		28,000		56,000		0
-Amortization of differential	(1,560)		(6,240)				(5,200)		(2,600)
-Differential translation adj.	(2,280)		(9,120)				(7,600)		(3,800)
Ending balance	12,960		51,840		28,000		43,200		(6,400)

Amortized excess value reclassification entry:

Amortization Expense	5,200
Depreciation expense	2,600
Income from Western Ranching	6,240
NCI in NI of Western Ranching	1,560

Excess value (differential) reclassification entry:

Plant and Equipment	28,000
Patent	43,200
Accumulated Depreciation	6,400
Investment in Western Ranching	51,840
NCI in NA of Western Ranching	12,960

Eliminate intercompany accounts:

Payable to Alamo	6,480
Receivable from Western Ranching	6,480

P12-25 (continued)

	Alamo	Western Ranching	Elimination Entries		Consolidated
			DR	CR	
Income Statement					
Sales	1,000,000	376,350			1,376,350
Less: COGS	(600,000)	(214,500)			(814,500)
Less: Depreciation Expense	(28,000)	(15,600)	2,600		(46,200)
Less Amortization Expense			5,200		(5,200)
Less: Operating Expense	(204,000)	(85,475)			(289,475)
Less: Interest Expense	(2,000)	(3,705)			(5,705)
Income from Western Ranching	39,416		45,656	6,240	0
Consolidated Net Income	205,416	57,070	53,456	6,240	215,270
NCI in Net Income			11,414	1,560	(9,854)
Controlling Interest in Net Income	205,416	57,070	64,870	7,800	205,416
Statement of Retained Earnings					
Beginning Balance	179,656	28,000	28,000		179,656
Net Income	205,416	57,070	64,870	7,800	205,416
Less: Dividends Declared	(50,000)	(6,030)		6,030	(50,000)
Ending Balance	335,072	79,040	92,870	13,830	335,072
Balance Sheet					
Cash	38,000	26,460			64,460
Accounts Receivable	140,000	43,200			183,200
Receivable from Western Ranching	6,480			6,480	0
Inventory	128,000	51,600			179,600
Plant & Equipment	500,000	144,000	28,000		672,000
Less: Accumulated Depreciation	(90,000)	(36,000)		6,400	(132,400)
Patent			43,200		43,200
Investment in Western Ranching	152,064		13,408	113,632	0
				51,840	
Total Assets	874,544	229,260	84,608	178,352	1,010,060
Accounts Payable	60,000	32,280			92,280
Payable to Alamo		6,480	6,480		0
Interest Payable	2,000	1,800			3,800
Bonds Payable		60,000			60,000
Premium on Bonds Payable		3,420			3,420
Common Stock	500,000	63,000	63,000		500,000
Retained Earnings	335,072	79,040	92,870	13,830	335,072
Accumulated OCI	(22,528)	(16,760)	0	16,760	(22,528)
NCI in NA of Western Ranching			3,352	28,408	38,016
				12,960	
Total Liabilities & Equity	874,544	229,260	165,702	71,958	1,010,060
Other Comprehensive Income					
Accumulated Other Comprehensive Income, 1/1/20X3					0
Other Comp. Income--Translation Adjustment	(22,528)	(16,760)		13,408	(25,880)
Other Comprehensive Income to NCI				3,352	3,352
Accumulated Other Comprehensive Income, 12/31/20X3	(22,528)	(16,760)	0	16,760	(22,528)

P12-26 Remeasurement

a. Western Ranching Company
 Trial Balance Remeasurement
 December 31, 20X3

	<u>Australian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Cash	A\$ 44,100	0.60	\$ 26,460
Accounts Receivable (net)	72,000	0.60	43,200
Inventory	86,000	0.65	55,900
Plant and Equipment	240,000	180,000 x 0.70 60,000 x 0.70	168,000
Cost of Goods Sold	330,000	(a)	217,800
Depreciation Expense	24,000	0.70	16,800
Operating Expense	131,500	0.65	85,475
Interest Expense	5,700	0.65	3,705
Dividends Declared	9,000	0.67	6,030
Total Debits	<u>A\$942,300</u>		<u>\$623,370</u>
Accumulated Depreciation	A\$ 60,000	0.70	\$ 42,000
Accounts Payable	53,800	0.60	32,280
Payable to Alamo, Inc.	10,800	0.60	6,480
Interest Payable	3,000	0.60	1,800
12% Bonds Payable	100,000	0.60	60,000
Premium on Bonds	5,700	0.60	3,420
Common Stock	90,000	0.70	63,000
Retained Earnings	40,000	0.70	28,000
Sales	<u>579,000</u>	0.65	<u>376,350</u>
Total			\$613,330
Remeasurement Gain			10,040
Total Credits	<u>A\$942,300</u>		<u>\$623,370</u>

	<u>Australian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
(a) Cost of Goods Sold:			
Beginning Inventory	A\$ 66,000	0.70	\$ 46,200
Purchases	<u>350,000</u>	0.65	<u>227,500</u>
Goods Available	A\$416,000		\$273,700
Minus Ending Inventory	<u>(86,000)</u>	0.65	<u>(55,900)</u>
Cost of Goods Sold	<u>A\$330,000</u>		<u>\$217,800</u>

P12-26* (continued)

b. Proof of Remeasurement Gain:

Schedule 1: Statement of Net Monetary Position

	<u>End of Year</u>	<u>Beginning of Year</u>
Monetary Assets:		
Cash	A\$ 44,100	
Accounts Receivable (net)	<u>72,000</u>	
Total	<u>A\$116,100</u>	
Monetary Equities:		
Accounts Payable	A\$ 53,800	
Payable to Parent Company	10,800	
Interest Payable	3,000	
12% Bonds Payable	100,000	
Premium on Bonds	<u>5,700</u>	
Total	<u>A\$173,300</u>	
Net Monetary Equities	<u>A\$(57,200)</u>	<u>A\$(80,000)</u>
Decrease in net monetary equities during year	<u>A\$(22,800)</u>	

Schedule 2: Analysis of Changes in Monetary Accounts

	<u>Australian Dollars</u>	<u>Exchange Rate</u>	<u>U.S. Dollars</u>
Exposed Net Monetary Liability Position — January 1	A\$ (80,000)	0.70	\$ (56,000)
Increases:			
From Operations:			
Sales	579,000	0.65	376,350
Decreases:			
From Operations:			
Purchases	(350,000)	0.65	(227,500)
Cash Expense	(131,500)	0.65	(85,475)
Interest Expense	(5,700)	0.65	(3,705)
From Dividends	(9,000)	0.67	(6,030)
From Purchase of Plant and Equipment	<u>(60,000)</u>	0.70	<u>(42,000)</u>
Net Monetary Position Prior to Remeasurement at Year-End Rate			\$ (44,360)
Exposed Net Monetary Liability Position — December 31	<u>A\$ (57,200)</u>	0.60	<u>(34,320)</u>
Remeasurement Gain			<u>\$ 10,040</u>

P12-27 Parent Company Journal Entries and Remeasurement

	<u>Australian Dollar</u>	<u>Rate</u>	<u>US Dollar</u>
Total Purchase Price	A\$ 200,000	0.70	\$ 140,000
Total Fair Value	A\$ 250,000	0.70	\$ 175,000
Less:			
Common Stock	A\$ 90,000	0.70	\$ 63,000
Retained Earnings	A\$ 40,000	0.70	\$ 28,000
Building & Equipment Differential	A\$ 40,000	0.70	\$ 28,000
Patent Value	<u>A\$ 80,000</u>		<u>\$ 56,000</u>

Parent company journal entries – 20X3:

- | | | | |
|-----|--|--------------------------------|---------|
| (1) | Investment in Western Ranching | 140,000 | |
| | Cash | | 140,000 |
| | Acquire foreign investment. | | |
| (2) | Cash | 4,824 | |
| | Investment in Western Ranching | | 4,824 |
| | Receive dividend:
\$4,824 = A\$9,000 x 0.80 x \$.67 | | |
| (3) | Investment in Western Ranching | 50,088 | |
| | Income from Western Ranching | | 50,088 |
| | Equity accrual for percentage of subsidiary's income: | | |
| | | <u>U.S.\$</u> | |
| | Sales | \$ 376,350 | |
| | Cost of goods sold | (217,800) | |
| | Depreciation expense | (16,800) | |
| | Operating expense | (85,475) | |
| | Interest expense | (3,705) | |
| | Remeasurement gain | 10,040 | |
| | Subsidiary's income | <u>\$ 62,610</u> | |
| | Parent's percent | x 0.80 | |
| | Equity accrual | <u>\$ 50,088</u> | |
| (4) | Income from Western Ranching | 6,720 | |
| | Investment in Western Ranching | | 6,720 |
| | Amortization of differential: | | |
| | Buildings and Equipment | = \$2,800 (\$28,000 / 10) | |
| | Patent | = <u>5,600</u> (\$56,000 / 10) | |
| | | <u>\$8,400</u> x 0.80 = 6,720 | |

P12-27 (continued)

NOT REQUIRED: Entries posted to T-accounts

	Investment in Western Ranching			Income from Western Ranching		
Acquisition Price	140,000					
80% Net Income	50,088				50,088	80% Net Income
		4,824	80% Dividends			
		6,720	Amort. of Diff.	6,720		
Ending Balance	178,544				43,368	Ending Balance

P12-28 Consolidation Worksheet after Remeasurement

Book Value Calculations:

	NCI 20%	+	Alamo 80%	=	Common Stock	+	Retained Earnings
Beginning book value	18,200		72,800		63,000		28,000
+ Net Income	12,522		50,088				62,610
- Dividends	(1,206)		(4,824)				(6,030)
Ending book value	29,516		118,064		63,000		84,580

Basic elimination entry

Common stock	63,000
Retained earnings	28,000
Income from Western Ranching	50,088
NCI in NI of Western Ranching	12,522
Dividends declared	6,030
Investment in Western Ranching	118,064
NCI in NA of Western Ranching	29,516

Excess Value (Differential) Calculations:

	NCI 20%	+	Alamo 80%	=	Plant and Equipment	+	Patent	+	Acc. Depr.
Beginning balance	16,800		67,200		28,000		56,000		0
Changes	(1,680)		(6,720)				(5,600)		(2,800)
Ending balance	15,120		60,480		28,000		50,400		(2,800)

Amortized excess value reclassification entry:

Amortization Expense	5,600
Depreciation expense	2,800
Income from Western Ranching	6,720
NCI in NI of Western Ranching	1,680

Excess value (differential) reclassification entry:

Plant and Equipment	28,000
Patent	50,400
Accumulated Depreciation	2,800
Investment in Western Ranching	60,480
NCI in NA of Western Ranching	15,120

Eliminate intercompany accounts:

Payable to Alamo	6,480
Receivable from Western Ranching	6,480

P12-28 (continued)

	Alamo	Western Ranching	Elimination Entries		Consolidated
			DR	CR	
Income Statement					
Sales	1,000,000	376,350			1,376,350
Remeasurement Gain		10,040			10,040
Less: COGS	(600,000)	(217,800)			(817,800)
Less: Depreciation Expense	(28,000)	(16,800)	2,800		(47,600)
Less Amortization Expense			5,600		(5,600)
Less: Operating Expense	(204,000)	(85,475)			(289,475)
Less: Interest Expense	(2,000)	(3,705)			(5,705)
Income from Western Ranching	43,368		50,088	6,720	0
Consolidated Net Income	209,368	62,610	58,488	6,720	220,210
NCI in Net Income			12,522	1,680	(10,842)
Controlling Interest in Net Income	209,368	62,610	71,010	8,400	209,368
Statement of Retained Earnings					
Beginning Balance	179,656	28,000	28,000		179,656
Net Income	209,368	62,610	71,010	8,400	209,368
Less: Dividends Declared	(50,000)	(6,030)		6,030	(50,000)
Ending Balance	339,024	84,580	99,010	14,430	339,024
Balance Sheet					
Cash	38,000	26,460			64,460
Accounts Receivable	140,000	43,200			183,200
Receivable from Western Ranching	6,480			6,480	0
Inventory	128,000	55,900			183,900
Plant & Equipment	500,000	168,000	28,000	0	696,000
Less: Accumulated Depreciation	(90,000)	(42,000)	0	2,800	(134,800)
Patent			50,400		50,400
Investment in Western Ranching	178,544			118,064	0
				60,480	
Total Assets	901,024	251,560	78,400	187,824	1,043,160
Accounts Payable	60,000	32,280			92,280
Payable to Alamo		6,480	6,480		0
Interest Payable	2,000	1,800			3,800
Bonds Payable		60,000			60,000
Premium on Bonds		3,420			3,420
Common Stock	500,000	63,000	63,000		500,000
Retained Earnings	339,024	84,580	99,010	14,430	339,024
NCI in NA of Western Ranching				29,516	44,636
				15,120	
Total Liabilities & Equity	901,024	251,560	168,490	59,066	1,043,160

P12-29 Foreign Currency Remeasurement [AICPA Adapted]

Kiner Company's Foreign Subsidiary
Remeasurement of Selected Captions into United States Dollars
December 31, 20X2, and December 31, 20X1

	<u>Balance in LCUs</u>	<u>Indirect Exchange Rate</u>	<u>Remeasured into U.S. Dollars</u>
<u>December 31, 20X1</u>			
Accounts Receivable (net)	35,000 LCU	1.7 LCU = \$1	\$20,588
Inventories, at cost	75,000	2.0 LCU = \$1	37,500
Property, Plant, and Equipment (net)	150,000	2.0 LCU = \$1	75,000
Long-Term Debt	120,000	1.7 LCU = \$1	70,588
Common Stock	50,000	2.0 LCU = \$1	25,000
<u>December 31, 20X2</u>			
Accounts Receivable (net)	40,000	1.5 LCU = \$1	26,667
Inventories, at cost	80,000	1.7 LCU = \$1	47,059
Property, Plant, and Equipment (net)	163,000	Schedule 1	86,000
Long-Term Debt	100,000	1.5 LCU = \$1	66,667
Common Stock	50,000	2.0 LCU = \$1	25,000

Schedule 1: Computation of Remeasurement of Property, Plant and Equipment
(Net) into United States Dollars on December 31, 20X2

	<u>Balance in LCUs</u>	<u>Indirect Exchange Rate</u>	<u>Remeasured into U.S. Dollars</u>
Land purchased on January 1, 20X1	<u>24,000 LCU</u>	2.0 LCU = \$1	<u>\$12,000</u>
Plant and equipment purchased on January 1, 20X1:			
Original cost	140,000 LCU	2.0 LCU = \$1	\$70,000
Depreciation for 20X1	(14,000)	2.0 LCU = \$1	(7,000)
Depreciation for 20X2	<u>(14,000)</u>	2.0 LCU = \$1	<u>(7,000)</u>
	<u>112,000 LCU</u>	2.0 LCU = \$1	<u>\$56,000</u>
Plant and equipment purchased on July 4, 20X2:			
Original cost	30,000 LCU	1.5 LCU = \$1	\$20,000
Depreciation for 20X2	<u>(3,000)</u>	1.5 LCU = \$1	<u>(2,000)</u>
	<u>27,000 LCU</u>	1.5 LCU = \$1	<u>\$18,000</u>
	<u>163,000 LCU</u>		<u>\$86,000</u>

P12-30 Foreign Currency Translation

Kiner Company's Foreign Subsidiary
 Translation of Selected Captions into United States Dollars
 December 31, 20X2, and December 31, 20X1

	<u>Balance in LCUs</u>	<u>Indirect Exchange Rate</u>	<u>Translated into U.S. Dollars</u>
<u>December 31, 20X1</u>			
Accounts Receivable (net)	35,000 LCU	1.7 LCU = \$1	\$ 20,588
Inventories, at cost	75,000	1.7 LCU = \$1	44,118
Property, Plant, and Equipment (net)	150,000	1.7 LCU = \$1	88,235
Long-Term Debt	120,000	1.7 LCU = \$1	70,588
Common Stock	50,000	2.0 LCU = \$1	25,000
<u>December 31, 20X2</u>			
Accounts Receivable (net)	40,000	1.5 LCU = \$1	26,667
Inventories, at cost	80,000	1.5 LCU = \$1	53,333
Property, Plant, and Equipment (net)	163,000	1.5 LCU = \$1	108,667
Long-Term Debt	100,000	1.5 LCU = \$1	66,667
Common Stock	50,000	2.0 LCU = \$1	25,000

P12-31 Matching Key Terms

1. E
2. I
3. K
4. H
5. A
6. F
7. J
8. B
9. L
10. C

P12-32 Translation Choices

Requirement 1:

- a. (7) LCU 0.83 December 31, 20X4: end of current year
- b. (5) LCU 0.85 Average for year 20X4 for revenues
- c. (6) LCU 0.84 November 1, 20X4: declaration date
- d. (7) LCU 0.83 December 31, 20X4: end of current year
- e. (7) LCU 0.83 December 31, 20X4: end of current year
- f. (5) LCU 0.85 Average for year 20X4 for expenses
- g. (1) LCU 0.74 June 16, 20X1: date foreign company purchased
- h. (7) LCU 0.83 December 31, 20X4: end of current year
- i. (8) Balance computed at end of December 31, 20X4, includes carry forward from prior periods
- j. (7) LCU 0.83 December 31, 20X4: end of current year
- k. (5) LCU 0.85 Average for year 20X4 for expenses

Requirement 2:

- a. Direct exchange rate (DER) for January 1, 20X4:
 DER = \$1 / LCU 0.80
 DER = \$1.25

- b. U.S. dollar versus LCU in 20X4:

	<i>Indirect</i> Exchange Rate <u>(LCU / \$1)</u>	<i>Direct</i> Exchange Rate <u>(\$ / LCU 1)</u>
Exchange rates on January 1, 20X4	LCU 0.80	\$1.25
Exchange rates on December 31, 20X4	LCU 0.83	\$1.2048

During 20X4, the direct exchange rate has decreased reflecting that it costs less U.S. currency for one foreign currency unit at the end of the year as compared with the beginning of the year. Therefore, the U.S. dollar has strengthened during the year 20X4. Alternatively, the indirect exchange rate has increased indicating it costs more in LCU to acquire \$1 at December 31, 20X4, than at January 1, 20X4.

P12-33 Proof of Translation Adjustment

a.

MaMi Co. Ltd.
Proof of Translation Adjustment
Year Ended December 31

	Translation MXP	Rate	\$
Net assets at beginning of year	575,000	\$0.087	50,025
Adjustment for changes in net assets position during year:			
Net income for year	270,000	\$0.090	24,300
Dividends	<u>(150,000)</u>	\$0.0915	<u>(13,725)</u>
Net assets translated at:			
Rates during year			60,600
Rates at end of year	<u>695,000</u>	\$0.093	<u>64,635</u>
Change in other comprehensive income-translation adjustment during year (net increase)			4,035
Accumulated other comprehensive income-translation adjustment, 1/1 (credit)			<u>3,250</u>
Accumulated other comprehensive income-translation adjustment, 12/31 (credit)			<u>7,285</u>

Note that the proof begins with the net assets at the beginning of the year. The proof shows the change in the other comprehensive income during the year of \$4,035. It is a credit or net increase in AOCI because it must offset an increase (debit) in the net assets from \$60,600 to \$64,635 during the year. A mnemonic here is to remember that the debits must equal the credits.

If you were to prove the total AOCI of \$7,285, then the proof should begin with the net assets at the time the subsidiary was acquired and then make the adjustments in net income, dividends, and other changes in net assets over the years since acquisition, at the appropriate exchange rates. Or, the change in this year of \$4,025 credit can simply be added to the beginning of the period AOCI credit balance of \$3,250.

b. The U.S. dollar weakened against the Mexican peso during the year shown by the increase in the direct exchange rate indicating it costs more U.S. currency to acquire one Mexican peso at the end of the year (\$0.093) as opposed to the U.S. currency cost of one Mexican peso at the beginning of the year (\$.087).

P12-33 (continued)

Another way of viewing the proof of the ending balance in AOCI is:

Translated Balance Sheet, 1/1			
Net assets	\$50,025	Stock and RE AOCI (given)	\$46,775 (plug) 3,250
Total	<u>\$50,025</u>		<u>\$50,025</u>

Translated Balance Sheet, 12/31			
Net assets	\$64,635	Stock and RE	\$46,775 (from 1/1)
		Retained earnings change:	
		(\$24,300 – \$13,725)	10,575
		AOCI (plug)	7,285
Total	<u>\$64,635</u>		<u>\$64,635</u>