



## Foreign currency translation (LKAS 21)

### What will you learn?

By completing this module,  
you will be able to:

1. Explain the concepts of functional and presentation currency
2. Describe how to translate foreign currency transactions
3. Describe how to translate foreign currency financial statements for consolidation purposes

## Agenda

Definitions  
Foreign currency transactions  
Foreign currency financial statements  
Know your calculations  
Disclosure  
The closing

## Currencies

Functional currency

Currency of the primary economic environment in which the entity operates

Foreign currency

Currency other than the entity's functional currency

Presentation currency

Currency in which the financial statements are presented

## Foreign Operation

Foreign Operation

Subsidiary, associate, joint arrangement or branch whose activities are conducted in a country or currency other than those of the reporting entity



## Functional Currency: Primary indicators

Currency that mainly influences sales prices

Currency of country whose competitive forces / regulation mainly determine sale prices

Primary indicators are the most important

Currency that mainly influences labour, material and other costs



## Functional Currency: Secondary indicators

Currency in which funds from financing activities are generated

Currency in which operating cash receipts are usually retained

£ \$

## Functional Currency: Additional indicators for foreign operations

Are activities conducted as extension of reporting entity or with significant autonomy?

What is proportion of transactions with reporting entity?

Does the foreign operation generate sufficient cash flows to service existing and normally expected debt obligations?

Do cash flows of the foreign operation directly affect cash flows of reporting entity and are they readily available for remittance?

£ \$

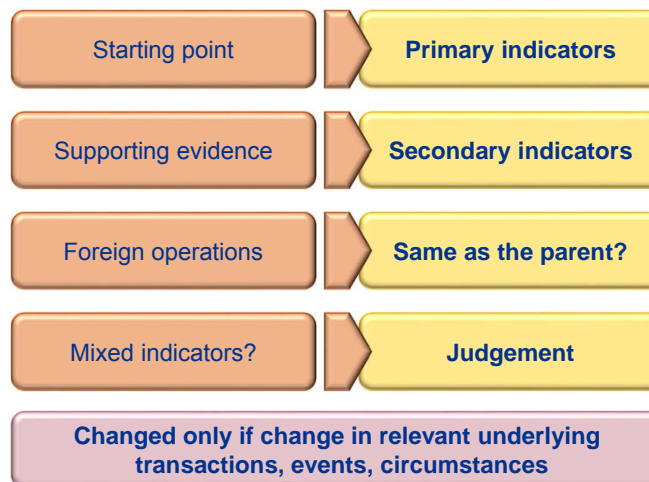
## A question for you: Functional currency

- ◆ Power-Up is an energy drink that is sold by Lila-Vitamins throughout the world
- ◆ Sales of Power-Up comprise over 90% of the revenue of Lila-Vitamins
- ◆ For convenience, Power-Up is priced in USD
- ◆ Lila-Vitamins finances its operations in L\$ and its cash reserves are in L\$, except approximately 20% which is held in USD
- ◆ Almost all of the costs to produce Power-Up are incurred in L\$

**What is the functional currency of Lila-Vitamins?**



## Functional Currency: Summary



## Monetary vs non-monetary

Monetary items

Items that will be received / paid in fixed or determinable number of units of currency

Accounts payable

Plant & equipment

Goodwill

Accrued expenses

Equity securities

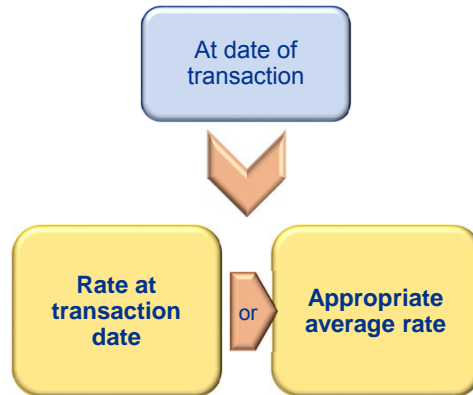
Non-monetary items

Items that will not be received / paid in fixed or determinable number of units of currency

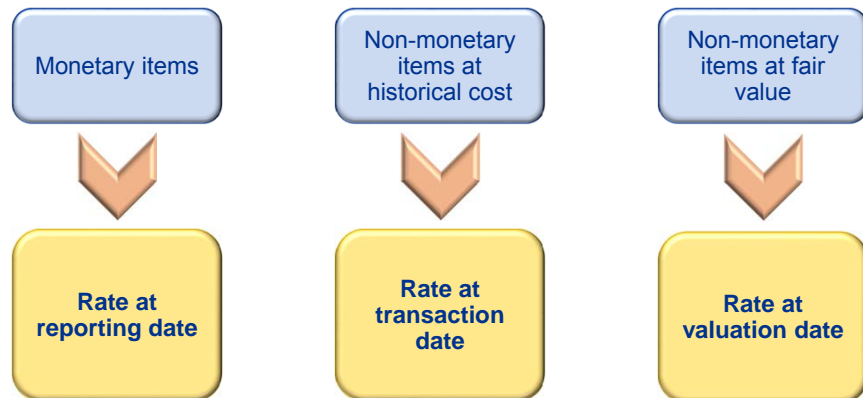
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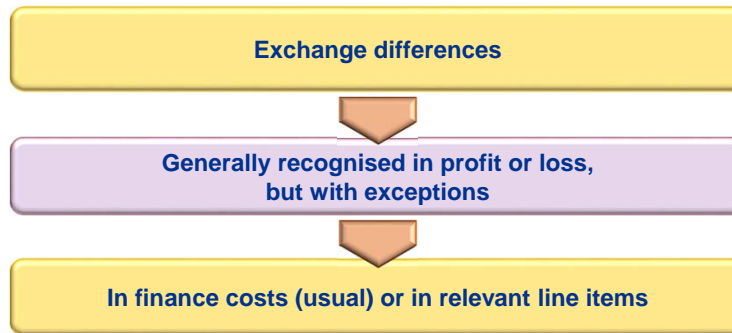
## Initial Recognition



## Reporting at the end of period



## Monetary Items: Exchange differences



## Non-monetary items: Exchange differences



OCI = other comprehensive income



## A question for you: Forex transactions (1)

- ◆ Lila-Cosmetics (functional currency L\$) buys a DNA Replicator machine from Mars for M\$ 20 million
- ◆ Delivery of the Replicator is on 20 December, and payment is due on 31 January
- ◆ The M\$ / L\$ rates are:
  - 20 December: 1 / 0.90
  - 31 December: 1 / 0.95

**What journal entries should Lila-Cosmetics record on 20 December and 31 December (reporting date)?**

M\$ = Mars Dollars



## A question for you: Forex transactions (2)

- ◆ Lila-Rent (functional currency L\$) buys an investment property on Mars for M\$ 625,000
- ◆ The cost of the investment property in functional currency was L\$ 500,000 (M\$ 625,000 x 0.80)
- ◆ At 31 December the fair value of the investment property is L\$ 712,500 (M\$ 750,000 x 0.95)

**At 31 December (reporting date) how much is the fair value gain and how much is the forex gain / loss?**



## A question for you: Forex transactions (3)

- ◆ Lila-Tech gave a loan of L\$ 100,000 to Lila-NewPlanet on 1 January
- ◆ Lila-Tech's functional currency is L\$
- ◆ Lila-NewPlanet's functional currency is NP\$
- ◆ The L\$ / NP\$ rates are:
  - 1 January: 1 / 1.5
  - 31 December: 1 / 2.0

**Based on the mini-case above, is the statement below true or false?**

**No exchange gain or loss will be recognised because the loan will be eliminated on consolidation.**

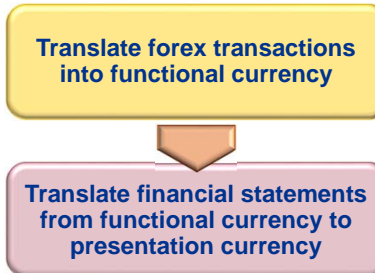


NP\$ = NewPlanet Dollars

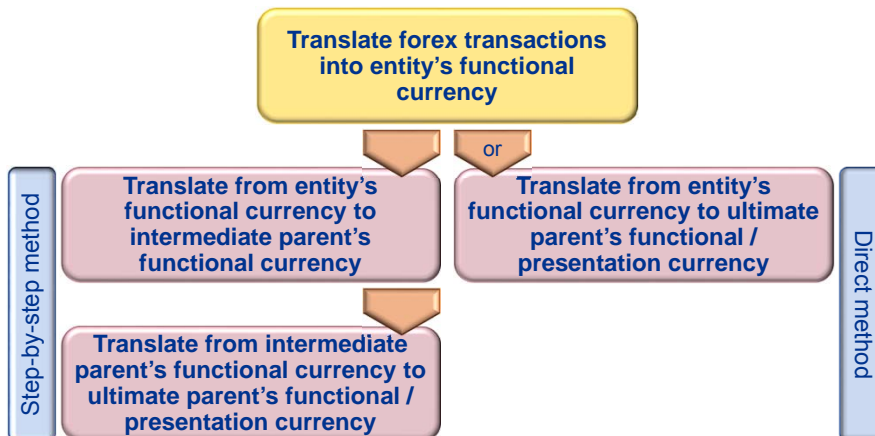
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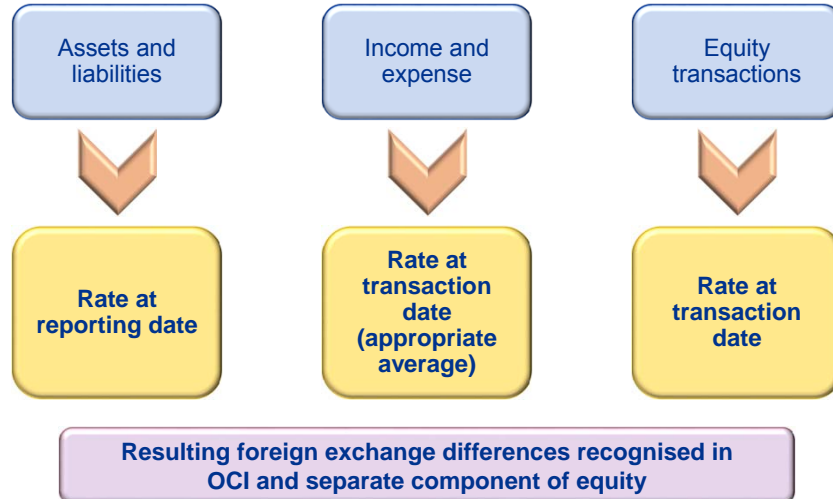
## From functional to presentation currency: Entity's own financial statements



## From functional to presentation currency: Consolidated financial statements



## Translation to presentation currency



## Illustration: Proof of FCTR (1)

- ◆ New office established on Mars on 1 January
- ◆ Share capital of M\$ 100 contributed in cash
- ◆ During the year a profit of M\$ 200 is made (cash sales)
- ◆ There were no other transactions
- ◆ The M\$ / L\$ rates are:
  - 1 January: 1.0 / 1.5
  - 31 December: 1.0 / 2.5
  - Average: 1.0 / 2.0

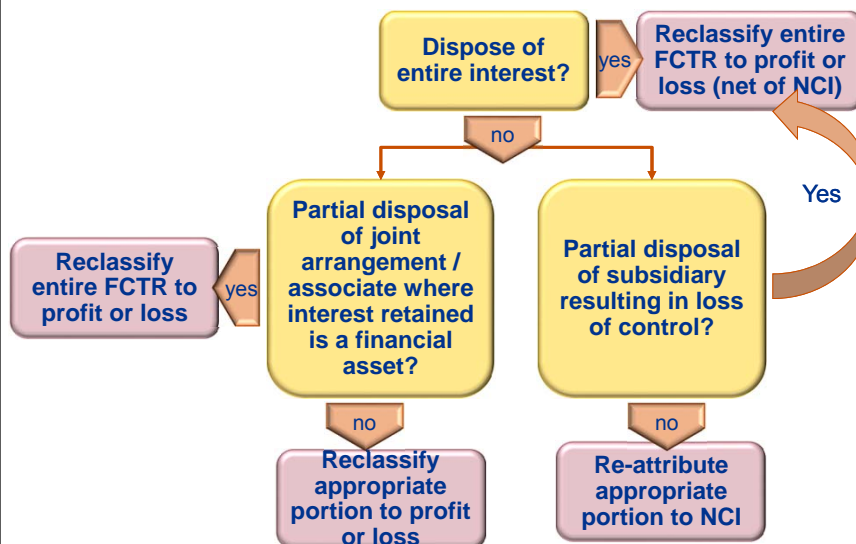
FCTR = foreign currency translation reserve

## Illustration: Proof of FCTR (2)

	M\$	Rate	L\$
Capital	100	1.5	150
Profit	200	2.0	400
<b>Balancing</b>	<b>--</b>		<b>200</b>
Equity	300	2.5	750
Assets	300	2.5	750

	Actual rate	Closing rate	Rate difference	Amount in M\$	Amount in L\$
Capital	1.5	2.5	1.0	100	100
Profit	2.0	2.5	0.5	200	100
<b>FCTR</b>					<b>200</b>

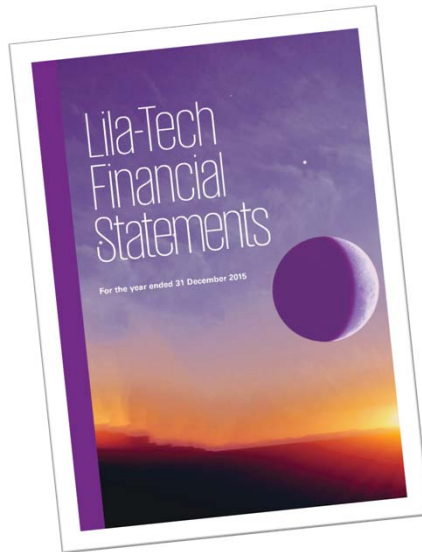
## Reclassification of FCTR to profit or loss



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## Disclosure



- ◆ Accounting policy
- ◆ Presentation in comprehensive income
- ◆ Presentation in equity
- ◆ Other disclosures

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## Which factors are not part of the determination of functional currency?

The currency that influences sales prices for goods and services

The currency that influences labour, material and other costs for producing goods and services

The currency that is the most financially stable and is frequently used in business transactions

The currency in which funds from financing activities are generated

## Which statements are true in respect of translations of foreign currency items?

Monetary items are retranslated at the exchange rate at the reporting date

Non-monetary items carried at fair value at the reporting date are retranslated at the exchange rate at the reporting date

Available for sale equity securities are not retranslated at the exchange rate at the reporting date

Tangible assets carried at historical cost are retranslated at the exchange rate at the reporting date



## Which statements are true in respect of translation into a presentation currency?

An entity's profit or loss is translated to the group presentation currency at the exchange rate at the reporting date

All exchange differences from the translation of a foreign operation are recognised in a separate component of equity

Exchange differences are reclassified to profit or loss when a foreign operation is disposed of

Equity transactions are translated at the exchange rate at the reporting date



- 1) Functional currency is the currency of the primary economic environment in which entity operates
- 2) Presentation currency is the currency in which the financial statements are presented
- 3) Exchange gains / losses from foreign currency transactions generally are recognised in profit or loss
- 4) Exchange gains / losses from the translation of foreign currency financial statements are recognised in OCI

## Scenario1

### 1. Defining operating segments

Below are Pacific's operating segments prior to the acquisition of E&M. Instead of using the external assembly agent, E&M will now assemble engines for the engine products supplied by Pacific and E&M's results will be reported to the CEO of Pacific (the [CODM](#)). Tony wants to know if engine assembly should now be identified as an operating segment of Pacific.

Select the correct answer from the drop-down box.

Operating Segment	Product
1	Electrical spare parts
2	Truck engine
3	Auto engine
4	Fuel components
5	Others

Should engine assembly be identified as an operating segment? (dropdown list)

### 2. Aggregation criteria of operating segments

Tony has asked you what impact the acquisition of E&M will have on how Pacific determines its reportable segments. If truck and auto engine have similar products, production processes, types of customer and methods of distribution, does that mean that Pacific can aggregate the two segments? You may want to take another look at the [segment information](#) Tony sent you for before and after the acquisition of E&M.

Click the **one** correct option, and then click **Confirm**.

Yes

No

### 3. Determining reportable segments based on quantitative thresholds

Tony has prepared a table of segment information, which he asks you to review. What do you tell him? In applying the quantitative thresholds, which of these operating segments are reportable? Segment information for each operating segment is shown below:

Select the correct answers from the drop-down boxes.

Operating Segment	Revenue			Segment Profit (Loss) (\$)	Segment Asset (\$)
	External Revenue (\$)	Internal Revenue (\$)	Total Revenue (\$)		
Electrical spare parts	3,500	800	4,300	1,000	40
Truck and auto engine	1,750	240	1,990	350	28
Fuel Components	1,500	0	1,500	(100)	15
Others	700	50	750	50	6
Engine assembly	100	3,000	3,100	340	22

4.

### Determining reportable segments based on quantitative threshold

Peter tells you that Wynne Corp. and its divisions are engaged solely in manufacturing operations. The [Wynne Corp.xls](#) contains current data (consistent with data from prior years) pertaining to the industries in which operations were conducted for the year.

How many of Wynne's industry segments are reportable segments under *IFRS 8*? Assume that they do not have similar economic characteristics.

Click the **one** correct option, and then click **Confirm**.

- Three
- Four
- Five
- Six

5.

### Knowledge check question 1

Which of the following statements about operating segments is correct?

Click the **one** correct option, and then click **Submit**.

- The amount of each segment item reported is the amount used by the CODM to make decisions about resource allocation and performance results.
- An entity is required to disclose information on all products and services from which the entity as a whole derives its revenue.
- Additional disclosures are required only if an external customer provides 25% or more of an entity's revenues.

6..

### Knowledge check question 2

Although IFRS 8 permits operating segments to be aggregated for reporting purposes, which of the following is true related to quantitative thresholds?

Click the **one** correct option, and then click **Submit**.

- An entity must report separately information about an operating segment whose assets are between 5 and 10 percent of the combined assets of all operating segments.
- At least 75% of the entity's revenue is included in reportable segments.
- An entity may not combine information about several operating segments that do not meet the quantitative thresholds to produce a reportable segment.

7.

### Knowledge check question 3

Which of the following statements about operating segments is true?

Click the **one** correct option, and then click **Submit**.

- An operating segment must be an operation that earns revenues.
- Every part of an entity must be part of an operating segment.
- Two or more operating segments may be aggregated into a single operating segment.

8.

### Knowledge check question 4

Which of the following is true as it relates to the Chief Operating Decision Maker (CODM) discussed in IFRS 8?

Click the **one** correct option, and then click **Submit**.

- The CODM is a manager or executive with that specific title.
- The CODM is a single person in the organization.
- The CODM regularly reviews the operating results of an operating segment to make decisions about the resources to be allocated to the segment and assess its performance.

**Pacific Group**  
**Segment**  
**Information**

Before acquisition of E&M

In applying the revenue test, electrical spare parts, truck engine, auto engine, fuel components and others are the operating segments prior to acquisition of E&M:

Operating segment	External revenue (\$)	Internal revenue (\$)
Electrical spare parts	3,500	800
Truck engine	950	40
Auto engine	800	200
Fuel components	1,500	0
Others	700	50

After acquisition of E&M

The internal and external revenues of each segment are shown below:

Operating segment	External revenue (\$)	Internal revenue (\$)
Electrical spare parts	3,500	800
Truck engine	950	40
Auto engine	800	200
Fuel components	1,500	0
Others	700	50
Engine assembly	100	3,000

Wynne Corp's Industry Segments data

Industry	Revenue (\$)	Profit (\$)	Assets (\$)
Car parts	3,100,000	132,000	1,600,000
Motor vehicles	1,350,000	112,000	1,400,000
Software	3,000,000	96,000	1,000,000
Electronics	900,000	44,000	520,000
Finance	950,000	40,000	460,000
All others	800,000	18,000	240,000
	10,100,000	442,000	5,220,000

## Scenario 2 – Measurement and Disclosure Requirements

In this scenario you will learn the following:

- **describe** and **apply** the measurement requirements of operating segments

**describe** and **apply** the disclosure requirements of *IFRS 8* including:

- **reconciliations** of total reportable segments' **revenue** to the entity's revenue
- **reconciliations** of reportable segments' measure of **profit or loss** to the entity's profit or loss
- **other** entity-wide disclosures

1. Tony has sent you a **table** of figures relating to Pacific Group and **two** of its operating segments. The allocation of operating expenses is made on a **reasonable** basis. What is the segment profit or loss for the two segments?

### Pacific and operating segments

	Corp/Head Office (\$)	Segment A (\$)	Segment B (\$)
Operating revenues	x	70,000	85,000
Cost of goods sold	x	27,000	36,000
Allocated operating expenses	x	13,000	11,000
General corporate expenses	15,000	0	0
Payroll and benefits	9,000	35,000	8,000
Fixed assets	5,000	70,000	55,000

Click the **one** correct option, and then click **Submit**.

- \$30,000 and \$38,000
- \$43,000 and \$49,000
- \$(5,000) and \$30,000
- \$8,000 and \$31,000

2.

## Disclosure requirements

You've helped Tony calculate the operating profit for individual segments. But now he wants to know what information Pacific is **required to disclose** (bearing in mind the **core principle** of *IFRS 8*).

Select one or more options and click **Submit**.

- Factors used to identify the entity's reportable segments
- The chief operating decision maker
- The measure of segment profit or loss, assets and liabilities (only if reviewed by CODM) and an explanation of the measurements of such information for each reportable segment
- Information about quantitative thresholds
- Reconciliations of segment revenues, profit or loss, assets, liabilities to corresponding entity amounts

3.

## Reconciliation of segment information

Andrew's first question is about reconciliation of segment information. What will you tell him?

In the reconciliation of segment profit or loss to the general purpose consolidated financial statements, *IFRS 8* requires that the reported segment profit or loss be reconciled to:

Click the **one** correct option, and then click **Submit**.

- The consolidated operating profit or loss
- The consolidated net profit or loss
- The level of the consolidated profit or loss before tax expense to which the segment profit or loss most closely corresponds
- The consolidated other comprehensive income for the year



4.

## Reconciliation of segment information

Andrew seems pleased with your answer. But he has a second question about reconciliation requirements: 'I've made a list of reconciliations of reportable segments' data against Pacific's financial statement data. Which of these items are we required to provide under *IFRS 8*?'

Click the **one** correct option, and then click **Submit**.

- Revenue, cost of goods sold, current assets and current liabilities (if regularly reported and reviewed by the CODM) and other material items
- Revenue, profit or loss, current assets, current liabilities and other material items
- Profit or loss, income tax, total assets and total liabilities (if regularly reported and reviewed by the CODM) and other material items
- Revenue, profit or loss, total assets and total liabilities (if regularly reported and reviewed by the CODM) and other material items disclosed

## 5. Entity-wide disclosures – information about major customers

MX is required to disclose its reliance on any customer to whom it sells more than a certain amount. Peter would like to know what that amount is.

Select the correct answer from the drop-down box.

	A	B	C	Total
External Sales (\$)	15,000	5,000	10,000	30,000
Internal Sales (\$)	10,000	4,000	6,000	20,000
Total Revenues (\$)	25,000	9,000	16,000	50,000
Operating Profit/ (loss) (\$)	-2,000	2,000	4,000	4,000
Fixed Assets (\$)	14,000	8,000	18,000	40,000

MX should disclose its reliance on any customer to whom it sells more than

## Knowledge check question

Which of the following statements about reconciliations is not correct?

Click the **one** correct option, and then click **Submit**.

- An entity shall provide a reconciliation of the total of the reportable segment's revenues to the entity's revenue.
- An entity shall provide a reconciliation of the total of the reportable segments' measures of profit or loss to the entity's profit or loss before tax expense (tax income) and discontinued operations.
- An entity is not required to provide a reconciliation of the total of the reportable segments' assets to the entity's assets.