CHAPTER 24

Accounting for the effects of changes in foreign exchange rates under IAS 21

24.1 Introduction

The increasing globalisation of business means that it is becoming more and more common for entities to enter into transactions that are denominated in a foreign currency. This causes accounting issues because the entity needs to record these transactions in its own currency in order to prepare its financial statements. A further complication is that entities can either enter into such transactions directly or via an overseas operation (a branch or subsidiary that it has established for the purposes of carrying out business in a particular location).

Objectives

By the end of this chapter, you should be able to:

- explain the meaning of the term 'functional currency';
- distinguish between functional currency and presentational currency;
- reflect foreign currency transactions carried out directly by the reporting entity in the financial statements;
- prepare consolidated financial statements to include subsidiaries with a functional currency that differs from the functional currency of the group;
- explain the particular accounting issues involved when a parent has a subsidiary that is located in a hyper-inflationary environment.

24.2 The difference between conversion and translation and the definition of a foreign currency transaction

Conversion is the exchange of one currency for another while **translation** is the expression of another currency in the terms of the currency of the reporting operation. Only in the case of conversion is there a **foreign currency transaction**, which IAS 21 *The Effects of Changes in Foreign Exchange Rates* defines as follows:[1]

> A foreign transaction is a transaction, which is denominated in or requires settlement in a foreign currency, including transactions arising when an entity:
>
> **(a)** buys or sells goods or services whose price is denominated in a foreign currency;
>
> **(b)** borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency;
>
> **(c)** otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.

24.3 The functional currency

The **functional currency** is the currency of the primary economic environment in which the entity operates.

IAS 21 sets out the factors which a reporting entity (a company preparing financial statements) will consider in determining its functional currency.[2] These are:

(a) the currency:
  - (i) that mainly influences sales prices for goods and services; and
  - (ii) of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services;

(b) the currency that mainly influences labour, material, and other costs of providing goods and services.

The following factors may also provide evidence of an entity's functional currency:[3]

(a) the currency in which funds from financing activities are generated;

(b) the currency in which the receipts from operating activities are usually retained.

If the functional currency is not obvious from the above, then managers have to make a judgement as to which currency most represents the economic effects of its transactions.

A company must also decide whether or not any of its foreign operations, such as a branch or subsidiary, has the same functional currency. In doing so the following factors will be considered:[4]

(a) Whether the activities of the foreign operation are carried out as an extension of the reporting entity, rather than being carried out with a significant degree of autonomy. An example of the former is when the foreign operation only sells goods imported from the reporting entity and remits the proceeds to it. An example of the latter is when the operation accumulates cash and other monetary items, incurs expenses, generates income and arranges borrowings, all substantially in its local currency.

(b) Whether transactions with the reporting entity are a high or low proportion of the foreign operation's activities.

(c) Whether cash flows from the activities of the foreign operation directly affect the cash flows of the reporting entity and are readily available for remittance to it.

(d) Whether cash flows from the activities of the foreign operation are sufficient to service existing and normally expected debt obligations without funds being made available by the reporting entity.

24.4 The presentation currency[5]

The **presentation currency** is the currency a reporting entity uses for its financial statements. The reporting entity is entitled to present its financial statement in any currency, so that in some cases the presentation currency may differ from the functional currency.

24.5 Monetary and non-monetary items

Monetary items are balances owed by or to an entity that will be settled in cash. Examples will be payables for goods supplied, loans, cash and debtors for goods supplied. Non-monetary assets will include property, plant and equipment, inventory and amounts prepaid for goods.

24.6 The rules on the recording of foreign currency transactions carried out directly by the reporting entity

Initial recognition[6]

All transactions are entered in the books at the spot currency exchange rate between the foreign currency and the functional currency on the transaction date. An average rate may be used for a period where it is appropriate. It will be inappropriate where exchange rates fluctuate significantly. Therefore in practice the spot rate is almost always used.

At subsequent dates

Amounts paid or received in settlement of foreign currency monetary items during an accounting period are translated at the date of settlement.

At the statement of financial position date monetary balances are retranslated at closing rate.

Non-monetary items at historical cost remain at their original rate. Non-monetary items at fair value are translated at the rate on the date the fair value was determined.[7]

24.7 The treatment of exchange differences on foreign currency transactions

Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period, or in previous financial statements, must be recognised in the statement of comprehensive income during the period in which they arise,[8] unless the company has entered into a hedging transaction under IAS 39 *Financial Instruments: Recognition and Measurement*. If the parent has taken a foreign loan to act as a hedge against the foreign investment the exchange differences on the loan can be recognised directly in equity to offset the exchange differences on the foreign subsidiary. Hedge accounting is only available if the group meets strict criteria which can prove difficult to meet in practice.

Note that the profits or losses on foreign currency transactions affect the cash flow and are therefore realised.

The following extract is from the Nemetschek AC 1999 group accounts:

> In the individual annual accounts of Nemetschek AC and its subsidiaries, business transactions in a foreign currency are valued at the exchange rate at the time of their original posting. Any exchange losses from the valuation of receivables and payables are taken into account up to the statement of financial position cutoff date. Profits and losses from fluctuations in the exchange rate are taken into account as affecting net income.

24.8 Foreign exchange transactions in the individual accounts of companies illustrated – Boil plc

Boil plc is a UK company that buys and sells catering equipment. The following information is available for foreign currency transactions entered into by Boil plc during the year ended 31 December 20X0:

1/11	Buys goods for $30,000 on credit from Nevada Inc
15/11	Sells goods for $40,000 on credit to Union Inc
15/11	Pays Nevada Inc $20,000 for on account for the goods purchased
10/12	Receives $25,000 on account from Union Inc in payment for the goods sold
10/12	Buys machinery for $80,000 from Florida Inc on credit
10/12	Borrowed $60,000 from an American bank; this is held in a dollar bank account
22/12	Pays Florida Inc $80,000 for the machinery

The exchange rates at the relevant dates were:

1/11	£1 = $2.00
15/11	£1 = $2.20
10/12	£1 = $2.40
22/12	£1 = $2.50
31/12	£1 = $2.60

Required:
Calculate the profit or loss on foreign currency to be reported in the financial statements of Boil plc at 31/12/20X0.

(Assume that Boil plc buys foreign currency to pay for goods and non-current assets on the day of settlement and immediately converts into sterling any currency received from sales.)

Solution
We need to calculate any exchange differences on monetary accounts, non-monetary accounts, and sales and purchases as follows:

Monetary accounts

Profits or losses on foreign transactions will arise on monetary accounts from the difference between the exchange rate on the date of the initial transaction and the rate on the date of its settlement or the statement of financial position date, whichever is earlier. Profits or losses on exchange differences will arise on the following monetary accounts:

Nevada Inc	–	Trade payables
Union Inc	–	Trade receivable
Florida Inc	–	Payable for machinery
American bank	–	Payable for a loan

The profit or loss on foreign exchange in these cases will be as follows:

Name of account	*Nevada Inc payable*	*Union Inc receivable*	*Florida Inc payable*	*American bank loan payable*
Foreign currency at exchange rate on date of initial transaction	$30,000/2.00 = £15,000	$40,000/2.20 = £18,182	$80,000/2.40 = £33,333	$60,000/2.40 = £25,000
Foreign currency at exchange rate on date of settlement	$20,000/2.20 = £9,091	$25,000/2.40 = £10,417	$80,000/2.50 = £32,000	
Foreign currency at exchange rate on date of statement of financial position	$10,000/2.60 = £3,846	$15,000/2.60 = £5,769		$60,000/2.60 = £23,077
Profit/(loss) on foreign exchange (£)	£2,063	(£1,996)	£1,333	£1,923

Other balances

All other balances, i.e. purchases and sales in the statement of comprehensive income and machinery (non-monetary) will be translated on the day of the initial transaction and no profit or loss on foreign exchange will arise. These balances will therefore appear in the financial statements as follows:

Purchases	$30,000/2.00	= £15,000
Sales	$40,000/2.20	= £18,182
Machinery	$80,000/2.40	= £33,333

The profit or loss on exchange differences is realised as they have either already affected the cash flows of Boil plc or will do so in the foreseeable future. This profit or loss must therefore be taken to the statement of comprehensive income.

24.9 The translation of the accounts of foreign operations where the functional currency is the same as that of the parent

If the functional currency of the foreign operation is the same as that of the parent then this means the foreign operation is primarily influenced by the parent's currency and will be evaluating its financial performance in the parent's currency. Therefore, the financial statements that will be the starting point for the consolidation will be prepared in the 'home' currency and the consolidation will be just as for any other subsidiary.

24.10 The use of a presentation currency other than the functional currency

Whenever the presentation currency is different from the functional currency, it is necessary to translate the financial statements into the presentation currency. In this situation there is no realisation of the exchange gain/loss in the cash flows and therefore any gain/loss will go to reserves.

The translation rules used in this situation are set out in para. 39 of IAS 21 as follows:

(a) assets and liabilities . . . shall be translated at the closing rate at the date of the statement of financial position;

(b) income and expenses . . . shall be translated at exchange rates at the dates of the transactions [or average rate if this is a reasonable approximation]; and

(c) all resulting exchange differences shall be recognised as a separate component of equity.

The following is an extract from the Uniq Group's 2005 Interim Accounts:

Foreign currency translation

Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in pound sterling, rounded to the nearest hundred thousand, which is the Group and Company's functional and presentation currency.

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income.

Group companies

The results and financial position of all the group entities (none of which has the functional currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

(a) assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position;

(b) income and expenses for each statement of comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

(c) all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the statement of comprehensive income as part of the gain or loss on sale. Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

24.11 Granby Ltd illustration

On 30 June 20X0 Granby Ltd acquired 60% of the common shares of a German subsidiary Berlin Gmbh. At that date the balance on the retained earnings of Berlin was €20,000,000. The summarised statements of comprehensive income and statement of financial position of Granby Ltd and Berlin Gmbh at 30 June 20X3 were as follows:

Statements of comprehensive income for the year ended 30 June 20X3

	Granby Ltd	*Berlin Gmbh*
	£000	*€000*
Sales	430,000	140,000
Opening inventories	70,000	21,200
Purchases	250,000	80,000
Closing inventories	25,000	17,200
Cost of sales	295,000	84,000
Gross profit	135,000	56,000
Dividend received	2,400	NIL
Depreciation	40,000	12,000
Other expenses	10,600	4,000
Interest paid	7,000	2,000
Total expenses	57,600	18,000
Profit before taxation	79,800	38,000
Taxation	20,000	12,000
Profit after taxation	59,800	26,000
Dividend paid 30.6.20X3	25,000	8,000

Statements of financial position as at 30 June 20X3

	£000	€000
Non-current assets	140,000	90,000
Investment in Berlin Gmbh	4,500	
Current assets:		
Inventories	25,000	17,200
Trade receivables	60,500	20,000
Berlin Gmbh	4,000	
Cash	11,000	800
	100,500	38,000
Current liabilities:		
Trade payables	60,000	18,000
Granby Ltd		8,000
Taxation	20,000	12,000
	80,000	38,000
Bonds	50,000	16,000
Total assets *less* liabilities	115,000	74,000
Share capital	52,000	6,000
Retained earnings	63,000	68,000
	115,000	74,000

The following information is also available:

1 Exchange rates were as follows:

At 30 June 20X0	£1 = €5
Average for the year ending 30 June 20X3, an approximation of the rate on the date of trading transactions and expenses	£1 = €4
At 30 June/1 July 20X2	£1 = €3.5
At 30 June 20X3	£1 = €2

2 It is assumed that the functional currency of Berlin is the euro.

3 An amount of €1,380,000 was written off goodwill as an impairment charge in the current year, and €2,760,000 in previous years.

4 Non-controlling interests are measured using method 1.

Required:
Prepare consolidated accounts.

24.12 Granby Ltd illustration continued

24.12.1 Solution – note all numbers expressed in '000s.

Stage 1 – Translate the net assets of Berlin into £

This is all done at the closing rate as shown below:

	€'000	£'000
Non-current assets	90,000	45,000
Inventories	17,200	8,600
Trade receivables	20,000	10,000
Cash	800	400
Trade payables	(18,000)	(9,000)
Owing to Granby	(8,000)	(4,000)
Taxation	(12,000)	(6,000)
Bonds	(16,000)	(8,000)
Net assets	74,000	37,000

Stage 2 – compute goodwill on acquisition

Goodwill is treated as a foreign currency asset so this is initially done in euros:

(£4,500 × 5) – 60% (€6,000 + €20,000) = 6,900 in euros.
€4,140 (€1,380 + €2,760) has been written off as impairment so €2,760 remains.
This is translated at the year end rate to give a figure in the statement of financial position of **£1,380** (€2,760 × $^1/_2$).

Stage 3 – prepare the consolidated statement of financial position

		£'000
Goodwill (see stage 2 above)		1,380
Non-current assets	(140,000 + 45,000)	185,000
Inventories	(25,000 + 8,600)	33,600
Trade receivables	(60,500 + 10,000)	70,500
Cash	(11,000 + 400)	11,400
Trade payables	(60,000 + 9,000)	(69,000)
Taxation	(20,000 + 6,000)	(26,000)
Bonds	(50,000 + 8,000)	(58,000)
		148,880
Share capital		52,000
Retained earnings	(see below)	82,080
Non-controlling interest	(40% × 37,000)	14,800
		148,880

Working – reconciliation of retained earnings

	£'000
Granby	63,000
Berlin [60% (68,000 – 20,000) × $^1/_2$]	14,400
Impairment of goodwill (4,140 × $^1/_2$)	(2,070)
Notional exchange difference on investment in Berlin	6,750
(See note below)	82,080

Note:
The notional exchange difference on the investment in Berlin of €22,500 that would have arisen had the investment been retranslated at the closing rate of 2 is necessary because of the way in which goodwill on consolidation is computed and translated. All other components

of the calculation bar this are already treated at the closing rate so this needs to be too in order to reconcile retained earnings.

This number includes all the exchange differences that have arisen on the consolidation of Granby since the date of acquisition. Some companies would show these exchange differences in a separate foreign exchange reserve but we do not have enough information to separately compute them.

Stage 4 – prepare the consolidated statement of comprehensive income

Note that where foreign subsidiaries are involved it is usually easier to take a 'two statement' approach to the preparation of the statement of comprehensive income. This is because the exchange differences are not shown in profit and loss but are included as 'other comprehensive income'. The statement of comprehensive income itself translates every item relating to Berlin at the average rate for the period, which is €4 to £1.

		£'000
Sales	(430,000 + (140,000 × 1/4))	465,000
Cost of sales	(295,000 + (84,000 × 1/4))	(316,000)
Gross profit		149,000
Impairment of goodwill	(1,380 × 1/2)	(690)
Depreciation	(40,000 + (12,000 × 1/4))	(43,000)
Other expenses	(10,600 + (4,000 × 1/4))	(11,600)
Interest	(7,000 + (2,000 × 1/4))	(7,500)
Profit before taxation		86,210
Taxation	(20,000 + (12,000 × 1/4))	(23,000)
Profit for the period		63,210
Attributed to:		
Shareholders of Granby	60,610	
Non-controlling interest	(40% × 26,000 × 1/4)	2,600
		63,210

Stage 5 – compute the exchange differences

These arise in two ways:

On net assets of Berlin

		Euros	*Rate*	*£'000*
At start of period	(balancing figure in euros)	56,000	3.5	16,000
Profit for the period		26,000	4	6,500
Dividend		(8,000)	2	(4,000)
Exchange translation difference	(balancing figure in £)	Nil		18,500
At end of period		74,000	2	37,000

On goodwill on consolidation

		Euros	*Rate*	*£'000*
At start of period	(6,900 – 2,760)	4,140	3.5	1,183
Impairment at the **end** of the period		(1,380)	2	(690)
Exchange translation difference	(balancing figure in £)	Nil		887
At end of period		2,760	2	1,380

Step 6 – prepare the statement of total comprehensive income

		£'000
Consolidated profit for the period		63,210
Other comprehensive income	(18,500 + 887)	19,387
Total comprehensive income		82,597
Attributed to:		
Shareholders of Granby		72,597
Non-controlling interest	(2,600 + (40% × 18,500))	10,000
		82,597

Note that none of the exchange difference on goodwill is allocated to the non-controlling interest because method 1 is used to measure it.

24.13 Implications of IAS 21

IAS 21 was revised in December 2003, and it was at this revision that the concept of the functional and presentation currencies was introduced. Whilst the implications for the standard are not significant for all businesses, they can have an effect. For example, a company may, in the past, have viewed foreign operations as separate to their existing parent business, but under IAS 21 as revised, if the foreign operations have a functional currency the same as the parent business, this is no longer permitted.

Also, the revision to IAS 21 changed the translation rules for statement of comprehensive incomes of businesses with a different functional and presentation currency, and gave new rules for the restatement of goodwill and fair value adjustments. These changes affected profits, net asset values and exchange differences that companies declared.

The following extract from Shell highlights some potential impacts:

> The Group has a range of inter-company funding arrangements in place in order to optimise the sourcing of financing for the Group and optimise the funding of its subsidiaries. IAS 21 is more prescriptive on the treatment of gains and losses taken to reserves [equity], for example, gains/losses where the currency of the loan is neither in the functional currency of the borrower nor of the lender are to be recognised in the statement of comprehensive income. IAS 21 is thus expected to increase volatility in the statement of comprehensive income. However, the Group is currently investigating whether to change its treasury policies to reduce this volatility.

24.14 Critique of use of presentation currency

Multinational companies may have subsidiaries in many different countries, each of which may report by choice or legal requirement internally in their local currency. With globalisation, reporting the group in a presentation currency assists the efficiency of international capital markets, particularly where a group raises funds in more than one market. Although each subsidiary might be controlled through financial statements prepared in the local currency, realism requires the use of a single presentation currency.

Summary

The conversion and translation of foreign currency for presentation in the financial statements has always been a difficult area of accounting with different views on approach. The approach taken in IAS 21 attempts to translate transactions and operations in a way that reflects the economic circumstances of the transaction. This gives no significant problems for individual foreign transactions but has led to two methods being adopted for foreign operations.

A foreign operation which has the same functional currency as its parent is treated as in integral part of the parent operations and therefore is translated in the same way as individual company transactions. A foreign operation with a functional currency different to the parent's (or a company with different functional and presentation currencies) follows different rules.

REVIEW QUESTIONS

1 Discuss the desirability or otherwise of isolating profits or losses caused by exchange differences from other profit or losses in financial statements.

2 How can different relationships between a parent operation and its controlled foreign operation affect the treatment of exchange profits or losses in the consolidated financial statements? Why should the treatment be different?

3 How does the treatment of changes in foreign exchange rates relate to the prudence and accruals concepts?

4 Explain the term functional currency and describe the factors an entity should take into account when determining which is the functional currency.

EXERCISES

An extract from the solution is provided on the Companion Website (www.pearsoned.co.uk/elliott-elliott) for exercises marked with an asterisk (*).

Question 1

Fry Ltd has the following foreign currency transactions in the year to 31/12/20X0:

15/11 Buys goods for $40,000 on credit from Texas Inc

15/11 Sells goods for $60,000 on credit to Alamos Inc

20/11 Pays Texas Inc $40,000 for the goods purchased

20/11 Receives $30,000 on account from Alamos Inc in payment for the goods sold

20/11 Buys machinery for $100,000 from Chicago Inc on credit

20/11 Borrows $90,000 from an American bank

21/12 Pays Chicago Inc $80,000 for the machinery

The exchange rates at the relevant dates were:

15/11 £1 = $2.60

20/11 £1 = $2.40

21/12 £1 = $2.30

31/12 £1 = $2.10

Required:
Calculate the profit or loss to be reported in the financial statements of Fry Ltd at 31/12/20X0.

* Question 2

On 1 January 20X0 Walpole Ltd acquired 90% of the ordinary shares of a French subsidiary Paris SA. At that date the balance on the retained earnings of Paris SA was €10,000. The non-controlling interest in Paris was measured using method 1. No shares have been issued by Paris since acquisition. The summarised statements of comprehensive income and statements of financial position of Walpole Ltd and Paris SA at 31 December 20X2 were as follows:

Statements of comprehensive income for the year ended 31 December 20X2

	Walpole Ltd	*Paris SA*
	£000	*€000*
Sales	317,200	200,000
Opening inventories	50,000	22,000
Purchases	180,000	90,000
Closing inventories	60,000	12,000
Cost of sales	170,000	100,000
Gross profit	147,200	100,000
Dividend received from Paris SA	1,800	NIL
Depreciation	30,000	30,000
Other expenses	15,000	7,000
Interest paid	6,000	3,000
Total expenses	51,000	40,000
Profit before taxation	98,000	60,000
Taxation	21,000	15,000
Profit after taxation	77,000	45,000
Dividend paid	20,000	10,000

Statement of financial position as at 31 December 20X2

	£000	*€000*
Non-current assets	94,950	150,000
Investment in Paris SA	41,050	
Current assets:		
Inventories	60,000	12,000
Trade receivables	59,600	40,000
Paris SA	2,400	
Cash	11,000	11,000
Total current assets	133,000	63,000
Current liabilities:		
Trade payables	45,000	18,000
Walpole Ltd		12,000
Taxation	21,000	15,000
Total current liabilities	66,000	45,000
Debentures	40,000	10,000
Total assets less liabilities	163,000	158,000
Share capital	80,000	60,000
Share premium	6,000	20,000
Revaluation reserve	10,000	12,000
Retained earnings	67,000	66,000
	163,000	158,000

The following information is also available:

(i) The revaluation reserve in Paris SA arose from the revaluation of non-current assets on 1/1/20X2.

(ii) No impairment of goodwill has occurred since acquisition.

(iii) Exchange rates were as follows:

At 1 January 20X0	£1 = €2
Average for the year ending 31 December 20X2	£1 = €4
At 31 December 20X1/1 January 20X2	£1 = €3
At 31 December 20X2	£1 = €5

Required:
Assuming that the functional currency of Paris SA is the euro, prepare the consolidated accounts for the Walpole group at 31 December 20X2.

Question 3

(a) According to IAS 21 *The Effects of Changes in Foreign Exchange Rates*, how should a company decide what its functional currency is?

(b) Until recently Eufonion, a UK limited liability company, reported using the euro (€) as its functional currency. However, on 1 November 2007 the company decided that its functional currency should now be the dollar ($).

The summarised balance sheet of Eufonion as at 31 October 2008 in € million was as follows:

ASSETS		€m
Non-current assets		420
Current assets		
Inventories	26	
Trade and other receivables	42	
Cash and cash equivalents	8	
		76
Total assets		496
EQUITY AND LIABILIITES		
Equity		
Share capital		200
Retained earnings		107
		307
Non-current liabilities	85	
Current liabilities		
Trade and other payables	63	
Current taxation	41	
	104	
Total liabilities		189
Total equity and liabilities		496

Non-current liabilities includes a loan of $70 million which was raised in dollars ($) and translated at the closing rate of $1 = €0.72425.

Trade receivables include an amount of $20 million invoiced in dollars ($) to an American customer which has been translated at the closing rate of $1 = €0.72425.

All items of property, plant and equipment were purchased in euros (€) except for plant which was purchased in British pounds (£) in 2007 and which cost £150 million. This was translated at the exchange rate of £1 = €1.46015 as at the date of purchase. The carrying value of the equipment was £90 million as at 31 October 2008.

Required:
Translate the balance sheet of Eufonion as at 31 October 2008 into dollars ($m), the company's new functional currency.

(c) The directors of Eufonion (as in (b) above) are now considering using the British pound (£) as the company's presentation currency for the financial statements for the year ended 31 October 2009.

Required:
Advise the directors how they should translate the company's income statement for the year ended 31 October 2009 and its balance sheet as at 31 October 2009 into the new presentation currency.

(d) Discuss whether or not a reporting entity should be allowed to present its financial statements in a currency which is different from its functional currency.

(*The Association of International Accountants*)

References

1 IAS 21 *The Effects of Changes in Foreign Exchange Rates*, IASB, revised 2003, para. 20.
2 *Ibid*., para. 20.
3 *Ibid*., para. 10.
4 *Ibid*., para. 11.
5 *Ibid*., para. 38.
6 *Ibid*., para. 21.
7 *Ibid*., para. 23.
8 *Ibid*., para. 28.