8. Which translation method does U.S. GAAP require for operations in hig inflationary countries? What is the rationale for mandating use of this meth
9. Why might a company want to hedge its balance sheet exposure? What is paradox associated with hedging balance sheet exposure?
10. How are gains and losses on foreign currency borrowings used to hedge net investment in a foreign subsidiary reported in the consolidated fina statements?

Exercises and Problems

1. Which of the following items is normally translated the same way under b the current rate and temporal methods of translation?
   a. Inventory
   b. Equipment
   c. Sales revenue
   d. Depreciation expense
2. In translating the financial statements of a foreign subsidiary into the pare reporting currency under the current rate method, which of the following sta ments is true?
   a. Expenses are translated using a combination of current and histo exchange rates.
   b. Intangible assets are translated at the historical exchange rates in effec the date the assets are purchased.
   c. The translation adjustment is a function of the foreign subsidiary's net ass
   d. The translation adjustment is a function of the relative amount of mone assets and monetary liabilities held by the foreign subsidiary.
3. A foreign subsidiary of Wampoa Ltd. has one asset (inventory) and no bilities. The subsidiary operates with a significant degree of autonomy Wampoa and primarily uses the local currency (the won) in carrying out transactions. Since the date the inventory was acquired, the won has decre in value in relation to Wampoa's reporting currency. In translating the for subsidiary's peso financial statements into the parent's reporting curre which of the following is true?
   a. A translation gain must be reported in net income.
   b. A positive translation adjustment must be reported in stockholders' equi
   c. A negative translation adjustment must be reported in stockholders' equi
   d. A translation loss must be reported in net income.
4. Which of the following best explains how a translation loss arises when t temporal method of translation is used to translate the foreign currency fina cial statements of a foreign subsidiary?
   a. The foreign subsidiary has more monetary assets than monetary liabili and the foreign currency appreciates in value.
   b. The foreign subsidiary has more monetary liabilities than monetary asse and the foreign currency depreciates in value.
   c. The foreign subsidiary has more monetary assets than monetary liabili and the foreign currency depreciates in value.

d. The foreign subsidiary has more total assets than total liabilities, and the foreign currency appreciates in value.

5. Which method of translation maintains, in the translated financial statements, the underlying valuation methods used in the foreign currency financial statements?
   a. Current rate method; income statement translated at average exchange rate for the year.
   b. Current rate method; income statement translated at exchange rate at the balance sheet date.
   c. Temporal method.
   d. Monetary/nonmonetary method.
6. In accordance with U.S. generally accepted accounting principles (GAAP), which translation combination would be appropriate for a foreign operation whose functional currency is the U.S. dollar?

	Method	Treatment of Translation Adjustment
a.	Temporal	Separate component of stockholders' equity
b.	Temporal	Gain or loss in income statement
c.	Current rate	Separate component of stockholders' equity
d.	Current rate	Gain or loss in income statement

7. The functional currency of Garland Inc.'s Japanese subsidiary is the Japanese yen. Garland borrowed Japanese yen as a partial hedge of its investment in the subsidiary. How should the transaction gain on the foreign currency borrowing be reported in Garland's consolidated financial statements?
   a. The transaction gain is reported as an adjustment to interest expense in the income statement.
   b. The transaction gain is reported as an extraordinary item in the income statement.
   c. The transaction gain is offset against the negative translation adjustment related to the Japanese subsidiary in the stockholders' equity section of the balance sheet.
   d. The transaction gain is offset against the negative translation adjustment related to the Japanese subsidiary on the income statement.
8. Selected balance sheet accounts of a foreign subsidiary of the Pacter Company have been translated into parent currency (F) as follows:

	Translated at	
	Current Rates	Historical Rates
Accounts receivable	₣100,000	₣120,000
Marketable securities, at cost	200,000	240,000
Prepaid insurance	120,000	130,000
Goodwill	250,000	300,000
	₣670,000	₣790,000

Required:

a. Assuming that the foreign subsidiary is determined to have the foreign currency as its functional currency in accordance with IAS 21, determine the total amount that should be included in Pacter's consolidated balance sheet for the assets listed in accordance with International Financial Reporting Standards (IFRS).

b. Assuming that the foreign subsidiary is determined to have Pacter's reporting currency as its functional currency in accordance with IAS 21, determine the total amount that should be included in Pacter's consolidated balance sheet for the assets listed in accordance with IFRS.

9. The Year 1 financial statements of the Brazilian subsidiary of Artemis Corporation (a Canadian company) revealed the following:

	Brazilian Reals (BRL)
Beginning inventory	100,000
Purchases	500,000
Ending inventory	150,000
Cost of goods sold	450,000

Canadian dollar (C$) exchange rates for 1 BRL as follows:

January 1, Year 1	C$0.45
Average, Year 1	0.42
December 31, Year 1	0.38

The beginning inventory was acquired in the last quarter of the previous year when the exchange rate was C$0.50 = BRL 1; ending inventory was acquired in the last quarter of the current year when the exchange rate was C$0.40 = BRL 1.

Required:

a. Assuming that the current rate method is the appropriate method of translation, determine the amounts at which the Brazilian subsidiary's ending inventory and cost of goods sold should be included in Artemis's Year 1 consolidated financial statements.

b. Assuming that the temporal method is the appropriate method of translation, determine the amounts at which the Brazilian subsidiary's ending inventory and cost of goods sold should be included in Artemis's Year 1 consolidated financial statements.

10. Simga Company's Turkish subsidiary reported the following amounts in Turkish lire (TL) on its December 31, Year 4, balance sheet:

Equipment	TL 100,000,000,000
Accumulated depreciation (straight-line)	32,000,000,000

Additional information related to the equipment is as follows:

Date	Amount Purchased	Useful Life	US$/TL Exchange Rate
1/1/Y1	TL 60,000,000,000	10 years	$0.0000070 = TL 1
1/1/Y3	TL 40,000,000,000	10 years	$0.0000020 = TL 1

U.S.-dollar exchange rates for the Turkish lira for Year 4 are as follows:

January 1, Year 4	$0.0000010
December 31, Year 4	0.0000006

Required:

a. Assume that Turkey is a highly inflationary economy. Determine the amounts at which the Turkish subsidiary's equipment and accumulated depreciation should be reported on Simga Company's December 31, Year 4, consolidated balance sheet in accordance with U.S. GAAP. Determine the net book value for equipment.

b. Now assume that Turkey is not a highly inflationary economy and that the Turkish subsidiary primarily uses Turkish lire in conducting its operations. Determine the amounts at which the Turkish subsidiary's equipment and accumulated depreciation should be reported on Simga Company's December 31, Year 4, consolidated balance sheet in accordance with U.S. GAAP. Determine the net book value for equipment.

11. Alliance Corporation (an Australian company) invests 1,000,000 marks in a foreign subsidiary on January 1, Year 1. The subsidiary commences operations on that date, and generates net income of 200,000 marks during its first year of operations. No dividends are sent to the parent this year. Relevant exchange rates between Alliance's reporting currency (A$) and the mark are as follows:

January 1, Year 1	A$0.15
Average, Year 1	0.17
December 31, 1997	0.21

Required:

Determine the amount of translation adjustment that Alliance will report on its December 31, Year 1, balance sheet.

12. Zesto Company (a U.S. company) establishes a subsidiary in Mexico on January 1, Year 1. The subsidiary begins the year with 1,000,000 Mexican pesos (MXN) in cash and no other assets or liabilities. It immediately uses MXN600,000 to acquire equipment. Inventory costing MXN300,000 is acquired evenly throughout the year and sold for Mex$500,000 cash. A dividend of MXN100,000 is paid to the parent on October 1, Year 1. Depreciation on the equipment for the year is MXN60,000. Currency exchange rates between the U.S. dollar and MXN for Year 1 are as follows:

January 1	U.S.$0.090
October 1	0.080
December 31	0.078
Average for the year	0.085

Required:

Determine the amount of remeasurement loss under the temporal method to be recognized in the Year 1 consolidated income statement.

13. Alexander Corporation (a U.S.-based company) acquired 100 percent of a Swiss company for 8.2 million Swiss francs on December 20, Year 1. At the date