



PASSFR.EU

A Digital Learning Platform for Generation Z:
Passport to IFRS®

IAS® Standard 21 The Effects of Changes in Foreign Exchange Rates



SCOPE

Foreign Currency
Transactions

Foreign Currency
Translations

KEY DEFINITIONS

Functional Currency

- The functional currency of an entity is the currency of the primary economic environment in which that entity operates

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Foreign Operations

- Is a subsidiary, associate, joint arrangement, or branch of a reporting entity, and
- Has activities that are based or conducted in a country or currency other than those of the reporting entity.

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- Is a subsidiary, associate, joint arrangement, or branch of a reporting entity, and
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Presentation Currency

- The currency in which the reporting entity's financial statements are prepared.

Functional Currency

- The functional currency of an entity is the currency of the primary economic environment in which that entity operates

Foreign Operations

- Is a subsidiary, associate, joint arrangement, or branch of a reporting entity, and
- Has activities that are based or conducted in a country or currency other than those of the reporting entity.

Presentation Currency

- The currency in which the reporting entity's financial statements are prepared.

Foreign Currency Transaction

- A foreign currency transaction is one that is denominated or requires settlement in a foreign currency.

FUNCTIONAL CURRENCY

FUNCTIONAL CURRENCY

Primary Factors

Secondary Factors

Primary Factors

- Operating Revenue and Cash Inflows

Primary Factors

- Operating Revenue and Cash Inflows
- Operating Expenses and Cash Outflows

Primary Factors

- Revenue and Operating Cash Inflows
- Operating Expenses and Cash Outflows

Secondary Factors

Primary Factors

- Revenue and Operating Cash Inflows
- Operating Expenses and Cash Outflows

Secondary Factors

- Financial Activities

Primary Factors

- Revenue and Operating Cash Inflows
- Operating Expenses and Cash Outflows

Secondary Factors

- Financial Activities
- Retention of Operating Income

EXAMPLE

- On 1 October 2021, Entity A buys an inventory for CUX 115,000. The exchange rate is CUY 1 = CUX 1.15. The inventory has a cost of CUY 100,000.

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- On 1 October 2021, Entity A buys an inventory for CUX 115,000. The exchange rate is CUY 1 = CUX 1.15. The inventory has a cost of CUY 100,000.
- On 31 October 2021, the payable is settled and the exchange rate is CUY 1 = CUX 1.16. The payment is settled at CUX 115,000, which is now equivalent to CUY 99,138.

EXAMPLE

- If the entity has a *functional currency of CUY*, a gain of CUY 862 will be taken to the statement of profit or loss and other comprehensive income.

$$\text{CUY } 100,000 - \text{CUY } 99,138 = \text{CUY } 862$$

EXAMPLE

- If the entity has a ***functional currency of CUY***, a gain of CUX 862 will be taken to the statement of profit or loss and other comprehensive income.
- If the entity's ***functional currency is the CUX***, the payment has not changed in value (CUX 115,000) so ***there is no gain or loss***.

**FUNCTIONAL
CURRENCY OF A
FOREIGN OPERATION**

Whether the operations of the foreign entity are conducted substantially autonomously or as an extension of the reporting entity

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Whether the transactions with the reporting entity are a high proportion of the activities of the foreign operation

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Whether the transactions with the reporting entity are a high proportion of the activities of the foreign operation

Whether the cash flows from the operations of the foreign operation directly affect the cash flows of the reporting entity and whether it is possible to transfer it to it at any time.

Whether the operations of the foreign entity are conducted substantially autonomously or as an extension of the reporting entity

Whether the transactions with the reporting entity are a high proportion of the activities of the foreign operation

Whether the cash flows from the operations of the foreign operation directly affect the cash flows of the reporting entity and whether it is possible to transfer it to it at any time.

Whether the cash flows from its own activities are sufficient to meet the current and normally expected debt obligations without requiring funding from the reporting entity.

PRESENTATION CURRENCY

Entity A
CUX

Entity B
CUY

Entity C
CUZ

A corporate group may have extensive operations in many countries and conduct its business largely in international markets. It may be difficult to identify an appropriate presentation currency. An international currency such as USD or Euro may be used.

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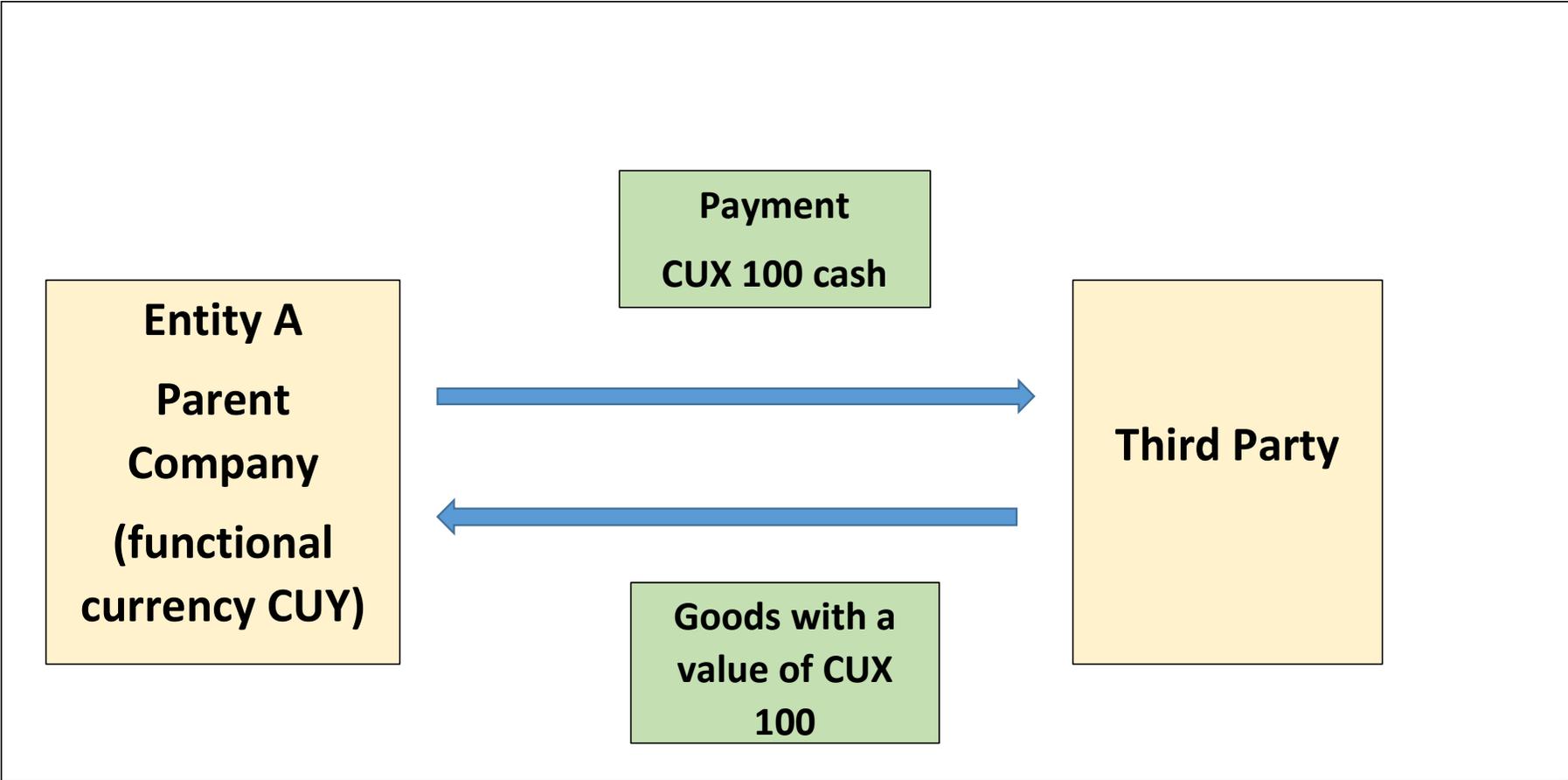
In some jurisdictions, entities are required to present their financial statements in the local currency even if this is not the functional currency.

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In some jurisdictions, entities are required to present their financial statements in the local currency even if this is not the functional currency.

An entity may wish to present its financial statements in the functional currency of the parent if it is different from its own functional currency.

FOREIGN CURRENCY TRANSACTIONS



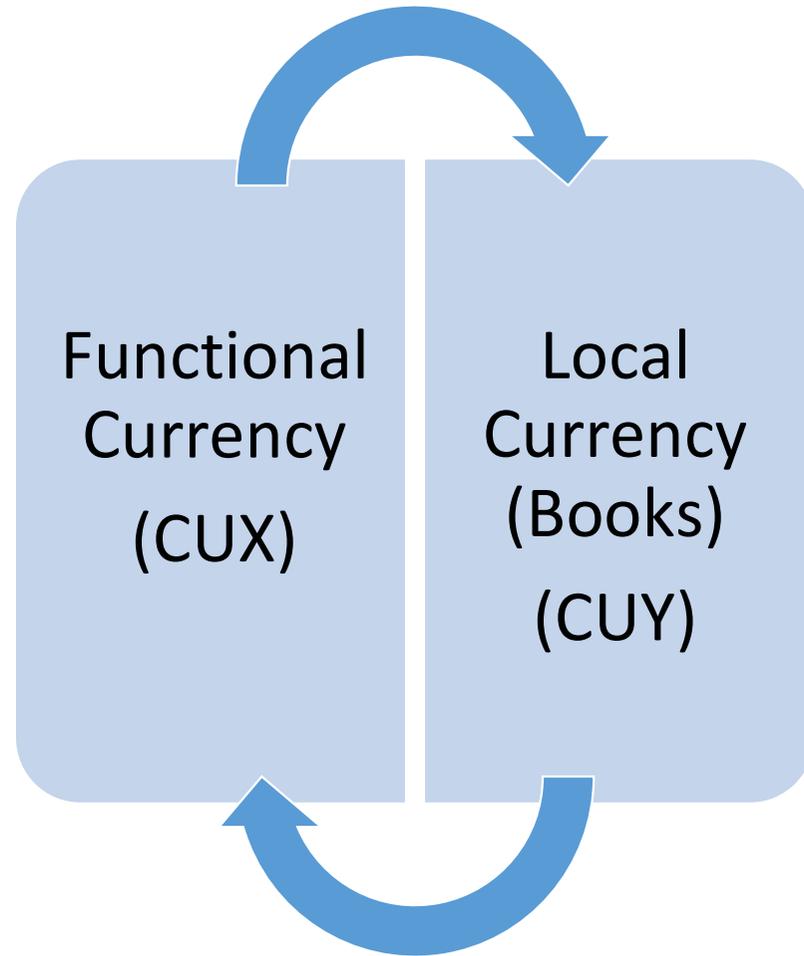
Foreign Currency Transactions

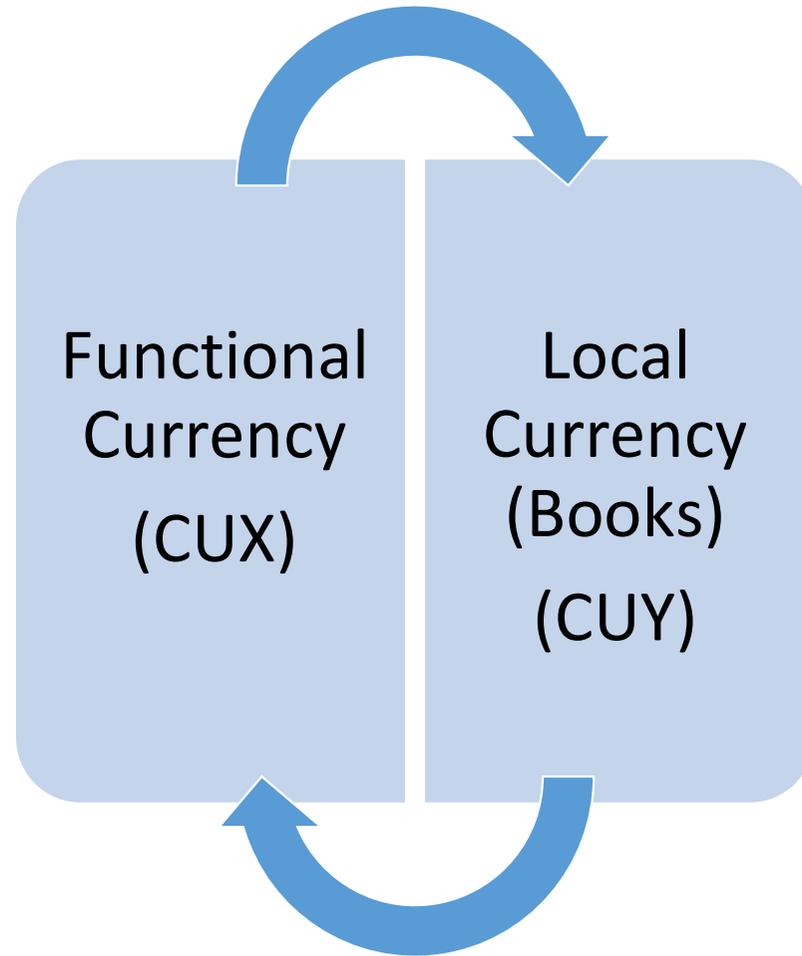
Functional Currency * Spot Exchange Rate

EXAMPLE

- An entity (functional currency CUX) buys inventory for CUY 15,000 on credit on February 23, 2022. The spot rate is CUX 1 = CUY 1.5.

Date	Entry (in CUX)
23.2.2022	Dr. Inventory 10,000 Cr. Trade Payable 10,000





Monetary Items

Non-monetary Items

Monetary Items

Non-monetary Items

Historical Cost

Fair Value

Monetary Items



Closing Rate

EXAMPLE

Monetary Item

- An entity (functional currency CUY) has an outstanding trade payable for CUX 1,500 which arose from a transaction when the spot exchange rate was CUY 1 = CUX 1.2 and hence was initially recorded at CUY 1,250.



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- An entity (functional currency CUY) has an outstanding trade payable for CUX 1,500 which arose from a transaction when the spot exchange rate was CUY 1 = CUX 1.2 and hence was initially recorded at CUY 1,250.
- The closing rate is CUY 1 = CUX 1.5 on December 31, 2021.

Date	Entry (in CUX)
31.12.2021	Dr. Trade Payable 250* Cr. Gain on Foreign Currency Transaction 250

$$\text{CUY } 250 = \text{CUY } 1,250 - \text{CUY } 1,000$$

Non-Monetary Items
(Historical Cost)



The exchange rate at
the date of
transaction



Non-Monetary Item (Historical Cost)

- An entity (functional currency CUY) purchased a machine for CUX 12,000 when the spot exchange rate was CUY 1 = CUX 1.2. The closing rate is CUY 1 = CUX 1.5.
- The machine is shown as CUY 10,000 ($12,000/1.2$) at the end of the reporting period.



Non-Monetary Item (Historical Cost)

- An entity (functional currency CUY) purchased a machine for CUX 12,000 when the spot exchange rate was CUY 1 = CUX 1.2. The closing rate is CUY 1 = CUX 1.5.
- The machine is shown as CUY 10,000 ($12,000/1.2$) at the end of the reporting period. **No journal entry** will be made as a result of the change in the exchange rates regarding the machine purchased in foreign currency.

Non-Monetary Items
(Fair Value)



The exchange rates at
the date when the
value is determined



Non-Monetary Item (Fair Value)

- An entity (functional currency CUY) owns a building. The entity carries buildings at their fair value.
- The valuation of the building was done at the end of the reporting period and fair value was CUX 150,000. The building was purchased for CUX 100,000 when the spot exchange rate was CUY 1 = CUX 1.2.

EXAMPLE

Non-Monetary Item (Fair Value)

- An entity (functional currency CUY) owns a building. The entity carries buildings at their fair value. The valuation of the building was done at the end of the reporting period and fair value was CUX 150,000. The building was purchased for CUX 100,000 when the spot exchange rate was CUY 1 = CUX 1.2.
- The closing rate is CUY 1 = CUX 1.5 on December 31, 2021.

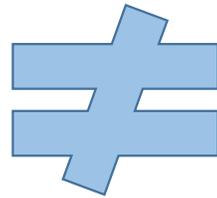
Date	Entry (in CUX)
31.12.2021	Dr. Buildings 16,667 Cr. Other Comprehensive Income 16,667

$$\text{CUY } 16,667 = \text{CUY } 100,000 - \text{CUY } 83,333$$

FOREIGN CURRENCY TRANSLATIONS

FOREIGN CURRENCY TRANSLATIONS

Presentation
Currency



Functional
Currency

Statement of
Financial Position

- Assets are translated at the closing rate
- Liabilities are translated at the closing rate

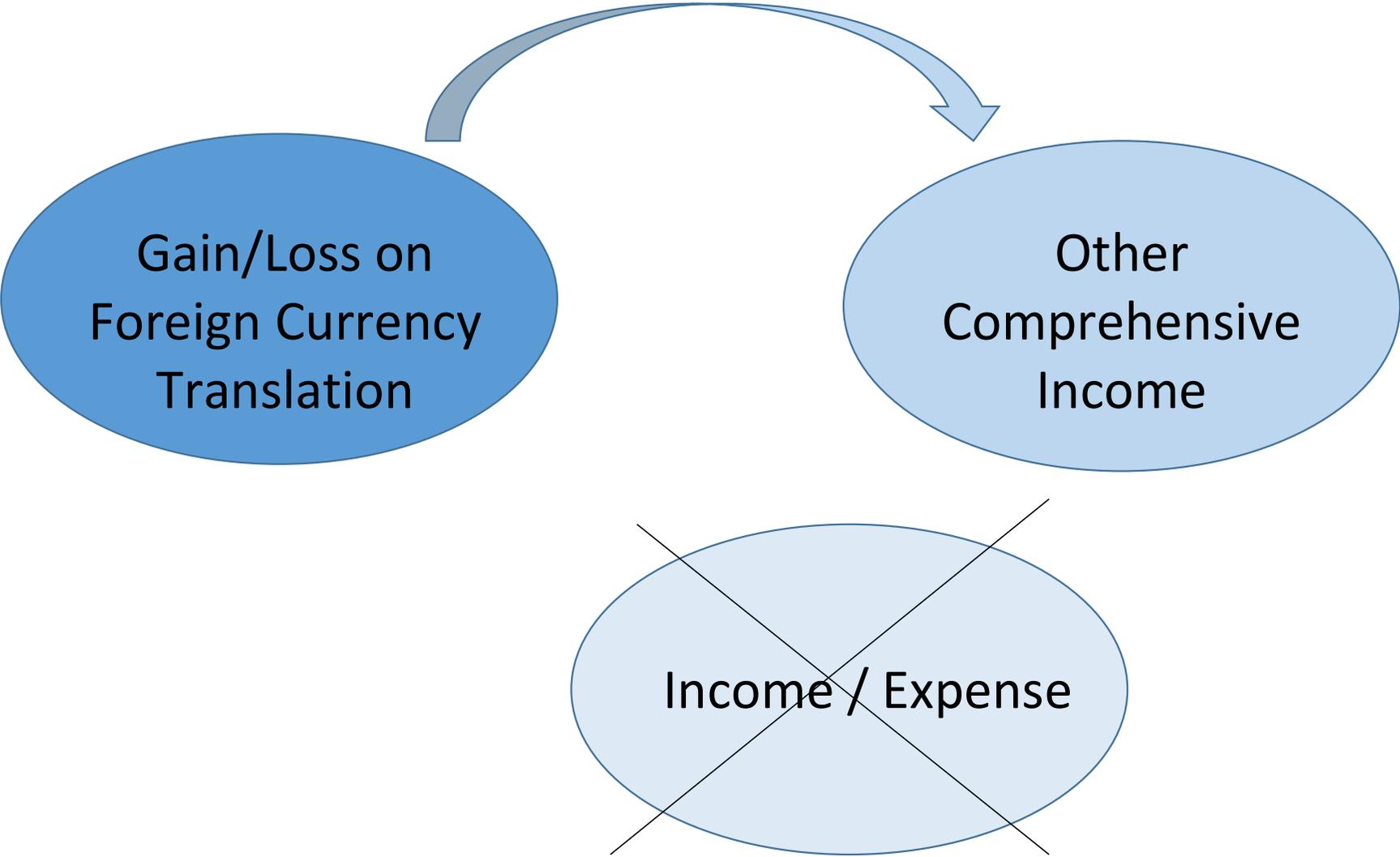
Statement of Profit
and Loss and
Other
Comprehensive
Income

Statement of Financial Position

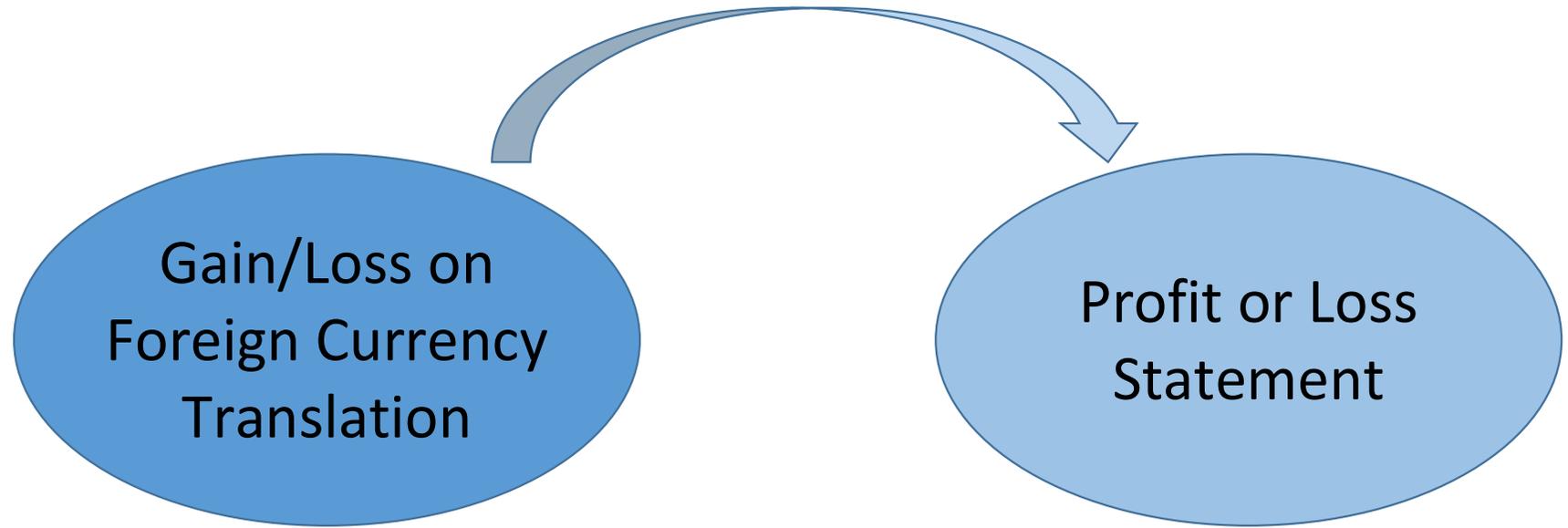
- Assets are translated at the closing rate
- Liabilities are translated at the closing rate

Statement of Profit and Loss and Other Comprehensive Income

- Income and Expenses are translated at the transaction date's rate



DISPOSAL OF FOREIGN OPERATION



Gain/Loss on
Foreign Currency
Translation

Profit or Loss
Statement

Disclosures

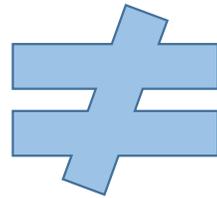
The amount of exchange differences recognised in profit or loss except for those arising on financial instruments measured at fair value through profit or loss in accordance with IFRS Standard 9.

Disclosures

The amount of exchange differences recognised in profit or loss except for those arising on financial instruments measured at fair value through profit or loss in accordance with IFRS Standard 9.

Net exchange differences recognised in other comprehensive income and accumulated in a separate component of equity, and a reconciliation of the amount of such exchange differences at the beginning and end of the period.

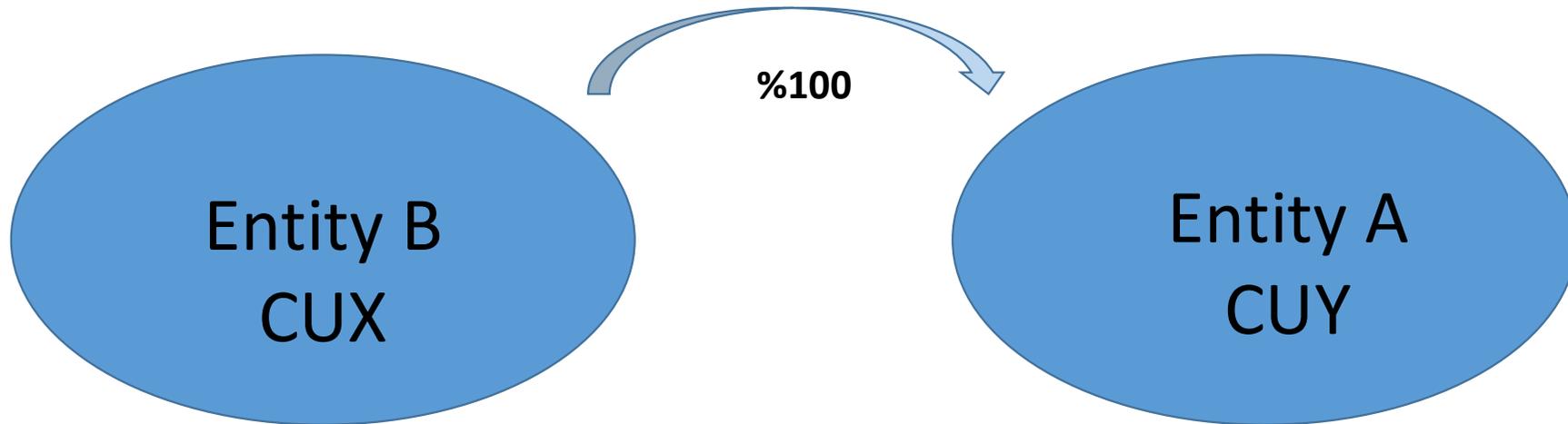
Presentation
Currency



Functional
Currency

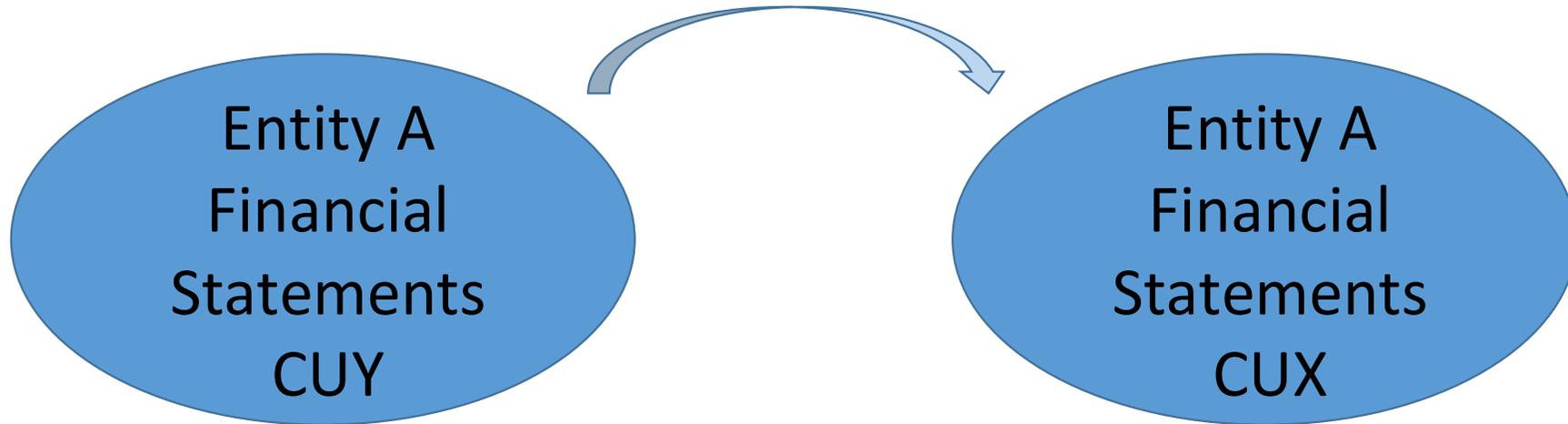
EXAMPLE

Foreign Currency Translation



EXAMPLE

Foreign Currency Translation



Entity A
Statement of Financial Position
as of December 31, 2021 (in CUY)

Cash	10,000	Accounts Payable	50,000
Accounts Receivable	40,000	Unearned Revenue	20,000
Inventories	70,000		
Equipment	100,000	Retained Earnings	30,000
Accumulated Depreciation	(20,000)	Equity	100,000
Total Assets	200,000	Total Liabilities and Owners Equity	200,000

Entity A
Statement of Profit and Loss and Other Comprehensive Income
For the Year 2021 (in CUY)

Revenues	260,000
Expenses	<u>220,000</u>
Net Income	40,000

January 1, 2021	CUY 1 = CUX 0.90
Weighted-average for 2021	CUY 1 = CUX 1.05
April 15, 2021	CUY 1 = CUX 1.10
December 31, 2021	CUY 1 = CUX 1.25

Entity A
Statement of Financial Position Translation
December 31, 2021

Assets	CUY			
Cash	10,000			
Accounts Receivable	40,000			
Inventories	70,000			
Equipment (net)	<u>80,000</u>			
Total Assets	200,000			
Liabilities and Owner's Equity				
Accounts Payable	50,000			
Unearned Revenue	20,000			
Retained Earnings	30,000			
Equity	100,000			
Total Liabilities and Owner's Equity	200,000			

Entity A
Statement of Financial Position Translation
December 31, 2021

Assets	CUY	Exchange Rates		
Cash	10,000	1.25		
Accounts Receivable	40,000	1.25		
Inventories	70,000	1.25		
Equipment (net)	<u>80,000</u>	1.25		
Total Assets	200,000			
Liabilities and Owner's Equity				
Accounts Payable	50,000	1.25		
Unearned Revenue	20,000	1.25		
Retained Earnings	30,000			
Equity	100,000			
Total Liabilities and Owner's Equity	200,000			

Entity A
Statement of Financial Position Translation
December 31, 2021

Assets	CUY	Exchange Rates	CUX	
Cash	10,000	1.25	12,500	
Accounts Receivable	40,000	1.25	50,000	
Inventories	70,000	1.25	87,500	
Equipment (net)	<u>80,000</u>	1.25	<u>100,000</u>	
Total Assets	200,000		250,000	
Liabilities and Owner's Equity				
Accounts Payable	50,000	1.25	62,500	
Unearned Revenue	20,000	1.25	25,000	
Retained Earnings	30,000			
Equity	100,000			
Total Liabilities and Owner's Equity	200,000		250,000	

Entity A
Statement of Financial Position Translation
December 31, 2021

Assets	CUY	Exchange Rates	CUX	
Cash	10,000	1.25	12,500	
Accounts Receivable	40,000	1.25	50,000	
Inventories	70,000	1.25	87,500	
Equipment (net)	<u>80,000</u>	1.25	<u>100,000</u>	
Total Assets	200,000		250,000	
Liabilities and Owner's Equity				
Accounts Payable	50,000	1.25	62,500	
Unearned Revenue	20,000	1.25	25,000	
Retained Earnings	30,000			
Equity	100,000	0.90	90,000	
Total Liabilities and Owner's Equity	200,000		250,000	

Entity A
Statement of Profit and Loss and Other Comprehensive Income Translation
For the Year 2021

	CUY		
Revenues	260,000		
Expenses	<u>220,000</u>		
Net Income	40,000		

Entity A
Statement of Profit and Loss and Other Comprehensive Income Translation
For the Year 2021

	CUY	Exchange Rates	
Revenues	260,000	1.05	
Expenses	<u>220,000</u>	1.05	
Net Income	40,000		

Entity A
Statement of Profit and Loss and Other Comprehensive Income Translation
For the Year 2021

	CUY	Exchange Rates	CUX
Revenues	260,000	1.05	273,000
Expenses	<u>220,000</u>	1.05	<u>(231,000)</u>
Net Income	40,000		42,000

	CUY	Exchange Rates	CUX
Net Income	40,000		42,000
(-) Dividend	<u>(10,000)</u>	1.15	<u>(11,500)</u>
Retained Earnings	30,000		30,500

Entity A
Statement of Financial Position Translation
December 31, 2021

Assets	CUY	Exchange Rates	CUX	
Cash	10,000	1.25	12,500	
Accounts Receivable	40,000	1.25	50,000	
Inventories	70,000	1.25	87,500	
Equipment (net)	<u>80,000</u>	1.25	<u>100,000</u>	
Total Assets	200,000		250,000	
Liabilities and Owner's Equity				
Accounts Payable	50,000	1.25	62,500	
Unearned Revenue	20,000	1.25	25,000	
Retained Earnings	30,000		30,500	
Equity	100,000	0.90	90,000	
Gain on Foreign Currency Translation				
Total Liabilities and Owner's Equity	200,000		250,000	

Entity A
Statement of Financial Position Translation
December 31, 2021

Assets	CUY	Exchange Rates	CUX	
Cash	10,000	1.25	12,500	
Accounts Receivable	40,000	1.25	50,000	
Inventories	70,000	1.25	87,500	
Equipment (net)	<u>80,000</u>	1.25	<u>100,000</u>	
Total Assets	200,000		250,000	
Liabilities and Owner's Equity				
Accounts Payable	50,000	1.25	62,500	
Unearned Revenue	20,000	1.25	25,000	
Retained Earnings	30,000		30,500	
Equity	100,000	0.90	90,000	
Gain on Foreign Currency Translation			<u>42,000</u>	
Total Liabilities and Owner's Equity	200,000		250,000	



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