**OGBEWELE EHINOMEN**

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**SUMMARY ON THE TRANSLATION OF FOREIGN CURRENCY FINANCIAL STATEMENTS**

**Statement of Financial Position Exposure**

As exchange rates change, assets and liabilities translated at the current exchange rate change in value from Statement of Financial Position to Statement of Financial Position in terms of the parent company’s reporting currency (for example, U.S. dollar). These items are exposed to translation adjustment. Exposure to translation adjustment is referred to as Statement of Financial Position, translation, or accounting exposure. Each item translated at the current exchange rate is exposed to translation adjustment. However, positive translation adjustments on assets when the foreign currency appreciates are offset by negative translation adjustments on liabilities. If total exposed assets are equal to total exposed liabilities throughout the year, the translation adjustments (although perhaps significant on an individual basis) net to a zero balance.

A foreign operation will have a net asset Statement of Financial Position exposure when assets translated at the current exchange rate are greater in amount than liabilities translated at the current exchange rate. A net liability Statement of Financial Position exposure exists when liabilities translated at the current exchange rate are greater than assets translated at the current exchange rate. The relationship between exchange rate fluctuations, Statement of Financial Position exposure, and translation adjustments can be summarized as follows:

|  |  |  |
| --- | --- | --- |
| **Statement of Financial**  **Position Exposure** | **Foreign Currency** | |
| **Appreciates** | **Depreciates** |
| Net Asset | Positive Translation adjustment | Negative Translation adjustment |
| Net Liability | Negative Translation adjustment | Positive Translation adjustment |

**TRANSLATION METHODS**

Four major methods of translating foreign currency financial statements have been used worldwide:

1. Current/noncurrent method,
2. Monetary/nonmonetary method,
3. Temporal method, and
4. Current rate (or closing rate) method.

**Current/Noncurrent Method**

The rules for the current/noncurrent method are as follows: current assets and current liabilities are translated at the current exchange rate; noncurrent assets, noncurrent liabilities, and stockholders’ equity accounts are translated at historical exchange rates.

**Monetary/Nonmonetary Method**

Under this method, monetary assets and liabilities are translated at the current exchange rates; nonmonetary assets, nonmonetary liabilities, and stockholders’ equity accounts are translated at historical exchange rates. Monetary assets are those assets whose value does not fluctuate over time—primarily cash and receivables. Nonmonetary assets are assets whose monetary value can fluctuate. They consist of marketable securities, inventory, prepaid expenses, investments, non-current assets, and intangible assets; that is, all assets other than cash and receivables. Monetary liabilities are those liabilities whose monetary value cannot fluctuate over time, which is true for most payables.

**Temporal Method**

The basic objective underlying the temporal method of translation is to produce a set of parent currency translated financial statements as if the foreign subsidiary had actually used the parent currency in conducting its operations.

**Current Rate Method**

The fundamental concept underlying the current rate method is that a parent’s entire investment in a foreign operation is exposed to foreign exchange risk and translation of the foreign operation’s financial statements should reflect this risk.