**TRANSALATION OF FOREIGN CURRENCY FINANCIAL STATEMENTS**

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**16/SMS02/042**

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**Summary of Translation of foreign currency financial statements**

Foreign currency translation is used to convert the results of a parent company’s foreign subsidiaries to its reporting currency. It is a key part of financial statement consolidation process. The steps in the translation process are as follows:

* Determine the functional currency of the foreign entity
* Re measure the financial statements of the foreign entity into the reporting currency of the parent company
* Record gains and losses on the translation of currencies

**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. 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. In effect, a separate translation adjustment exists for each of these exposed items. However, negative translation adjustments on liabilities offset positive translation adjustments on assets when the foreign currency appreciates.

**Translation methods**

There are four major methods of translating foreign currency financial statements which are:

* Current/noncurrent method
* Monetary/non-monetary method
* Temporal method
* Current rate (or closing rate) method.

Current/noncurrent method is where all current assets and liabilities in a foreign currency are translated to the domestic currency at the current exchange rate while all long term assets and liabilities are translated at the exchange rate in effect when each asset or liability was acquired.

Monetary/non-monetary method is where monetary items like cash, accounts payable and receivable, and long term debt are translated at the current rate while non-monetary items like inventory, fixed assets and long term investments are translated at historical rates.

Temporal method converts the currency of a foreign subsidiary into the currency of the parent company, it is used when the local currency of the subsidiary is not the same as the currency of the parent company.

Current rate method utilizes the current market exchange rate under the current rate method, revenues and expenses are translated using the exchange rate in effect at the date of accounting recognition.