



ACCOUNTING STANDARDS – 11

“EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES”

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Quote:

“The Pessimist Sees Difficulty in Every Opportunity. The Optimist Sees Opportunity in Every Difficulty.”



SECTION A – CONCEPTS

THIS AS DEALS WITH: -

- Treatment of Foreign Currency Transactions
- Translation of Financial Statements of Foreign Operations (Branch/Subsidiary)
- Forward Exchange Contracts. (Hedge and Speculation)

1. FOREIGN CURRENCY TRANSACTIONS

1.1 DEFINITIONS

Currencies – For the purpose of this AS, there are two types of Currencies

- (a) **Reporting Currency** – Any Currency in which Financial Statements are reported.
- (b) **Foreign Currency** – Any Currency other than Reporting currency.

A Foreign Currency Transaction is a transaction which is denominated in or requires settlement in a foreign currency for example – sale or purchase of goods in Foreign Currency, Borrowings or Lending or Investing in Foreign Currencies etc.

Monetary items are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money. For example, cash, receivables and payables.

Non-monetary items are assets and liabilities other than monetary items. For example, fixed assets, inventories and investments in equity shares.

Foreign Currency Monetary Items are Monetary Items which are to be settled in Foreign Currency (i.e., Receivable or Payable in Foreign Currency)

1.2 RECOGNITION AND MEASUREMENT

Two important questions?

Q1. What is Initial Recognition?

Initial Recognition means first time recording in the books of accounts of Foreign Currency Transaction.

Q2. What is Subsequent measurement?

Subsequent Measurement means measurement at Balance Sheet date of Foreign Currency Monetary Items (FCMI) arising out of Foreign Currency Transactions.

Initial Recognition: All foreign exchange transactions are converted into reporting currency using **Spot exchange rate** or approximate rates (i.e., the exchange rate prevailing on the date of Transaction).

Examples of Foreign Currency Transactions:

- Buying or selling of Goods and Services in Foreign Currency;
- Borrowing or Lending Money in Foreign Currency;
- Acquisition or Disposal of Assets in Foreign Currency;
- Incurring or Settling any Liability in Foreign Currency



Subsequent Measurement (at BS date):

- This recognition is applied on **Foreign currency Monetary Items (FCMI)** and **Non-Monetary Items carried at fair value** or measured at other than cost.
- Subsequent measurement is applied for preparing financial statements.
- Any exchange difference arising on subsequent measurement at Balance Sheet date shall be transferred to **Profit & Loss a/c.**

Financial Statement Items	Exchange Rates
Monetary Items i.e. FCMI (e.g., Foreign Receivables or Payables)	Exchange Rate at the Reporting Date (i.e., Closing Exchange Rate)
Non-Monetary items at historical cost (e.g., PPE)	Exchange Rate at the date of transaction (i.e., Spot Rate)
Revalued Non-monetary items or Items Measured at Fair Value (E.g., Inventory, Investments in Equity Shares) Refer Example No 3	Exchange Rate at the date of Fair valuation or Revaluation Example: the cost or carrying amount, as appropriate, is translated at the exchange rate at the date when that amount was determined; and the net realisable value or recoverable amount, as appropriate, is translated at the exchange rate at the date when that value was determined.

Note: Foreign Currency Monetary Items (FCMI): FCMI are those **Assets/Liabilities** whose amount is **Fixed** under contract and they are to be **settled in foreign currency**. For example, Receivable, Payables, Cash Balances.

Example 1:

Mr. A Purchased Goods of \$30,000 on 1/Feb for which payment to made in next year 30/4

Issue 1: How to record on 1/Feb because it is in \$

Issue 2: What to do on Balance Sheet Date i.e., 31/3 because \$ Changes

Issue 3: on 30/4 Settlement is in \$ the how to Measure?

Solution:

Issue 1:

As per AS 11, all Foreign Currency transaction must be recorded at the rate prevailing on transaction Date (i.e. SPOT Rate)

Suppose 1st Feb \$1 = 76/-

Transaction Vale = \$30,000 x 76 = 22,80,000/-

1st Feb:

Purchase A/c	Dr.	22,80,000	
To Foreign Creditor A/c			22,80,000

Trading A/c

To Purchases	22,80,000		
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Balance Sheet

Foreign Creditors (\$30,000)	22,80,000		
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Issue 2:

On 31st March \$1 = ₹ 77

As per AS 11, All Monetary Assets/Liabilities which are in foreign Currency (FCMI) should be measured at Closing Exchange Rate on Balance Sheet Date.

Revised Foreign Creditors = \$30,000 x 77 = 23,10,000

Exchange Difference (Loss) = 23,10,000 - 22,80,000 = 30,000

31/3

Exchange Loss A/c	Dr.	30,000	
To Foreign Creditor A/c			30,000

As per AS 11, Exchange Difference due to measurement of FCMI should be transfer to P&L A/c
31/3

P&L A/c	Dr.	30,000	
To Exchange Loss A/c			30,000

Trading A/c

To Purchases	22,80,000		
To Exchange Loss	30,000		

Balance Sheet

Foreign Creditors (\$30,000)	23,10,000		
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Issue 3:

At the time of settlement \$ again Change to ₹ 77.80

Amount to be paid in ₹ = \$30,000 x 77.80 = 23,34,000/-

30/4

Foreign Creditors A/c	Dr.	23,10,000	
Exchange Loss A/c	Dr.	24,000	
To Bank A/c			23,34,000

As per AS 11, Exchange Difference at settlement shall be transferred to P&L A/c

Example 2:

On 1st Feb, Entity purchased PPE at \$25,000 & Paid immediately

\$1 = ₹ 76 (on 1st Feb)

\$1 = ₹ 77 (on 31/3)

Apply AS 11.

Solution:

As per AS 11, all foreign Currency Transaction must be recorded & measured at the rate prevailing on transaction date. (SPOT Rate)

Transaction Value in ₹ = \$25,000 x 76 = 19,00,000/-

PPE A/c	Dr.	19,00,000	
To Bank A/c			19,00,000

Example 3: (Subsequent Measurement of Foreign Currency Non-Monetary Item)

Inventory purchased costing \$10,000 in cash as 1/4/23. On 30th June inventory is unsold.

Case 1: NRV is \$12,000 on 30th June

Case 2: NRV is \$ 9000 on 30th June & it is measured on 10th July

Rate of \$1 on 1/4/23 = ₹80, on 30th June \$1 = ₹ 82/- and on 10th July \$1 = ₹ 82.5/-

Solution:**1) Initial recognition of Foreign Currency Transaction**

Cost of Acquisition = \$10,000 x 80/- = Rs. 8,00,000

01/04/23	Purchase a/c Dr	8,00,000	
	To Bank a/c	8,00,000	

2) Subsequent measurement on 30th June (BS Date)

Case 1:

Cost = \$10,000

NRV = \$12,000

Since Cost is Lower, It is a non-monetary item measured at cost.

Conclusion:

No need to remeasure at New Ex Rate, it should be Continued at Historical Rate.

Balance Sheet	
Inventory (\$10000)	8,00,000

Case 2: Cost = \$10,000; NVR = \$ 9000

Therefore, Inventory is non-monetary item, measured at other than cost.

As per AS 11, this is to be measured at Exchange Rate on the date of Valuation of NRV i.e 10th July = \$1 = Rs. 82.50/-

Total Inventory value = \$9000 x 82.5/- = Rs. 7,42,500/-

Trending a/c	
Debit	Credit
Purchase 8,00,000	Closing stock 742500

PARA 46 OF AS 11 ON TREATMENT OF LONG TERM FOREIGN CURRENCY MONETARY ITEMS UNDER SUBSEQUENT MEASUREMENT

Para 46 has been introduced in AS 11 with retrospective effect from 7th December 2006 amended on 31st March, 2009.

- (a) Corporate/Non-Corporate entities can opt for the application of this Para & option is irrevocable.
- (b) FCMI of Long Term in nature (whose realization/payment is beyond 12 months from the date of original transaction) will be converted using closing rate in subsequent recognition.

Exchange difference arising from above point will be recognized as follows:

- Transfer Exchange difference to value of Depreciable Fixed Assets (PPE) if long term monetary item was taken to finance such Depreciable F.A. (i.e., to be capitalized if debit difference and subtracted if credit difference) (Refer Example No. 4)
- Transfer Exchange difference to Foreign Currency Monetary Items Translation Diff a/c (FC MIT Diff a/c) if Long Term Monetary Item has no relation with Depreciable Fixed Assets. (Refer Example No. 5)
- FC MIT Diff a/c will be amortised over the balance period of such long-term assets or liability, by recognition as income or expense in each of such periods (Written off in periods equally till the life of LTFCMI.)

The balance in FC MIT Diff a/c (debit or credit) should be shown on the "Equity and Liabilities" side of the balance sheet under the head "Reserves and Surplus" as a separate line item. (As decided by the council of ICAI)



Example 4:

Vsmart Ltd. took a Foreign Currency Loan of \$1,00,000 to purchase machine of the same amount. On 1st April, 2022 Loan is of 5 Years. To be repaid in lumpsum after 5 Years.

Depreciation Rate is 10%

Exchange rates are as follows:

On 1/4/22 - \$1 = ₹ 78

On 31/3/23 - \$1 = ₹ 82

On 31/3/24 - \$1 = ₹ 80.5

Show A/c as per AS 11 in following cases:

(a) Without PARA 46

(b) With PARA 46

Solution:**1) Initial Recognition:**

Foreign Currency should recognise at the rate prevailing on transaction Date (i.e. SPOT Rate) i.e. \$1 = ₹ 78

Transaction Value = \$1,00,000 × 78 = 78,00,000

1/4/22

Machine A/c	Dr.	78,00,000	
To Foreign Currency Loan A/c			78,00,000

(Note: assuming machine is measured at cost always)

(Note: Foreign Currency Loan is a LTFCMI)

2) Subsequent measurement:**Case 1: without PARA 46**

Exchange Difference due to Subsequent measurement shall be transfer to Profit & Loss A/c

1st Year end: 31/3/23

Foreign Currency Loan Should be = \$1,00,000 × 82 = 82,00,000

Exchange Difference (Loss) = 4,00,000

31/3/23

Exchange Difference (P&L) A/c	Dr.	4,00,000	
To Foreign Currency Loan A/c			4,00,000
Profit & Loss A/c	Dr.	4,00,000	
To Exchange Difference A/c			4,00,000

2nd Year end: 31/3/24

Foreign Currency Loan Should be = \$1,00,000 × 80.5 = 80,50,000

Exchange Difference (Gain) = 82 - 80.5 = 1,50,000

Foreign Currency Loan A/c	Dr.	1,50,000	
To Exchange Difference (P&L) A/c			1,50,000
Exchange Difference (Gain) A/c	Dr.	1,50,000	
To Profit & Loss A/c			1,50,000

Case 2: with PARA 46

Exchange Difference should be adjusted to the cost of machine

31/3/23

Exchange Difference (Loss) = 4,00,000

Machine A/c	Dr.	4,00,000	
To Foreign Currency Loan A/c			4,00,000

Depreciation @ 10% = 82,00,000 × 10% = 8,20,000

Remaining Balance of Machine = 73,80,000

31/3/24



Exchange Difference (Gain) = 1,50,000

Deduct From Machines Book Value

Foreign Currency Loan A/c To Machine A/c	Dr.	1,50,000	1,50,000
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Depreciation @ 10% on (73,80,000 - 1,50,000) = 72,30,000 x 10% = 7,23,000

Example 5:

Vsmart Ltd. took a loan of \$75,000 on 1/4/22 when \$1 = ₹ 78. Loan is utilized for working capital requirement loan is of 6 Years. Principal repayment equally every year.

1st year end - \$1 = ₹ 81.30

2nd year end - \$1 = ₹ 82.15

3rd year end - \$1 = ₹ 82

4th year end - \$1 = ₹ 81.50

5th year end - \$1 = ₹ 81.90

6th year end - \$1 = ₹ 82

Apply PARA 46 of AS 11:

Solution:

1) Initial Recognition:

Bank A/c To Foreign Currency Loan A/c	Dr.	58,50,000	58,50,000
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2) Subsequent Measurement:

31/3/23 (First remeasure then part installment)

FCMIT Difference A/c To FC Loan A/c (\$75,000 x 3.30)	Dr.	2,47,500	2,47,500
FC Loan A/c To Bank A/c (\$12,500 x 81.30)	Dr.	10,16,250	10,16,250

Foreign Currency Book Value = 50,81,250

Amortize FCMIT Difference in 6 Years = 2,47,500 / 6 = 41,250

Profit & Loss A/c To FCMIT Difference A/c	Dr.	41,250	41,250
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Balance unamortised FCMIT = 2,06,250 (Dr. Balance)

31/3/25	31/3/25	31/3/26	31/3/27	31/3/28
\$1 = ₹ 82.15	\$1 = ₹ 82	\$1 = ₹ 81.50	\$1 = ₹ 81.90	\$1 = ₹ 82
Prev. rate = 81.30	Prev. rate = 81.25	Prev. rate = 82	Prev. rate = 81.50	Prev. rate = 81.90
Loss = 0.85 x \$62,500	Gain = 0.15 x \$50,000	Gain = 0.5 x \$37,500	Loss = 0.4 x \$12,500	Loss = 0.10 x \$12,500
Total Loss = 53,125	Total Gain = 7,500	Total Gain = 18,750	Total Loss = 10,000	Total Loss = 1,250
Loss added to FCMIT Difference	Deduct from FCMIT Difference	Deduct from FCMIT Difference	Added to FCMIT Difference	Added to FCMIT Difference
Revised FCMIT Difference = 2,59,375	Revised FCMIT Difference = 2,00,000	Revised FCMIT Difference = 1,31,250	Revised FCMIT Difference = 97,500	Revised FCMIT Difference = 50,000
Year = 5	Year = 4	Year = 3	Year = 2	Year = 1
P&L A/c = 51,875	P&L A/c amortised = 50,000	P&L A/c amortised = 43,750	P&L A/c amortised = 48,750	Fully amortised to P&L A/c = 50,000
Closing Balance of FCMIT = 2,07,500	Closing Balance of FCMIT = 1,50,000	Closing Balance of FCMIT = 87,500	Closing Balance of FCMIT = 48,750	



2. TRANSLATION OF FINANCIAL STATEMENTS OF FOREIGN OPERATIONS

AS 11 (Effect of Changes in Foreign Exchange Rates), classifies the foreign branches as:

- **INTEGRAL FOREIGN OPERATION:** The activities of which are an integral part of those of the reporting enterprise (i.e. Head Office). An integral foreign operation carries on its business as *if it were an extension* of the reporting enterprise's operations. (Example - Foreign Branch)
- **NON-INTEGRAL FOREIGN OPERATION:** The business of such branch is carried on in a substantially independent way. (Example - Foreign Subsidiary Co.)
A non-integral foreign operation accumulates cash and other monetary items, incurs expenses, generates income and perhaps arranges borrowings, all substantially in its local currency.

TECHNIQUES FOR TRANSLATION:

(A) Integral Foreign Branch:

Items to be Translated	Translation at
Monetary Items (such as Debtors/creditors, Cash/Bank, Prepaid/Outstanding expense)	At Closing exchange rate
Non-Monetary items (such FA, Accumulated depreciation on FA, Investments etc.)	At Cost i.e., at the exchange rate on the date of purchase
Opening Stock	Opening exchange rate
Closing Stock	Closing exchange rate
Revenue nature items (Incomes and expenses)	Average rate
Goods sent to branch a/c and HO a/c	Actual balance in HO books

Any Exchange difference arising on the translation of the Branch Trial Balance should be *transferred to Profit & Loss a/c* of Branch.

(B) Non-Integral Foreign Branch:

1. **Balance Sheet items** i.e., Assets and Liabilities both Monetary and Non-monetary apply Closing exchange rate.
2. **Items of Income and Expenses** – At the actual exchange rates on the date of transactions. However, AS 11 allows average rate subject to materiality.
3. Any Exchange rate difference should be accumulated in a “Foreign Currency Translation Reserve” (FCTR).
4. FCTR shall be accumulated under Reserves & Surplus as a separate line item.
5. FCTR shall be reclassified to Profit and Loss account on Conversion from Non-Integral to Integral FO.
6. FCTR shall be reclassified to Profit and Loss account on sale/dispose of Non-Integral FO. However, if there is no disposal or sale of FO but only carrying amount is written off then no reclassification is allowed.
7. In the case of a partial disposal, only the proportionate share of the related accumulated exchange differences is included in the gain or loss.



How to Identify Non-Integral Foreign Operation?

The following are indications that a foreign operation is a non-integral foreign operation rather than an integral foreign operation:

- I. While the reporting enterprise may **control** the foreign operation, the activities of the foreign operation are carried out with a significant degree of autonomy from those of the reporting enterprise.
- II. Transactions with the reporting enterprise **are not a high proportion** of the foreign operation's activities.
- III. The activities of the foreign operation are **financed mainly from its own operations** or local borrowings rather than from the reporting enterprise.
- IV. Costs of labour, material and other components of the foreign operation's products or services are primarily paid or **settled in the local currency** rather than in the reporting currency.
- V. The foreign operation's sales are **mainly in currencies other than the reporting currency**.



3. FORWARD EXCHANGE CONTRACTS (FEC)

Meaning:

- A FEC is an agreement between two parties where by one party **agrees to buy or sell to other party an asset at future date for an agreed price.**
- These contracts are over the counter in an unregulated market.

Accounting Treatment:

FEC have been classified into two types for the purpose of accounting treatment:

- (1) Forward exchange contracts entered for managing risk (Hedging)
- (2) Forward exchange contracts entered for trading or speculation.

Forward Exchange Contracts entered For Managing Risk (Hedging):

- Any forward premium/discount should be **amortized/recognized over the tenor** of contract in the profit and loss a/c.
- If the forward contract is cancelled or renewed, the profit or loss arising on cancellation or renewal is recognized in the profit & loss statement for the period.

Forward Exchange Contracts entered for Trading or Speculation:

- **Here forward premium/discount should be ignored.**
- At each balance sheet date the value of contract is marked to market, **any gain or loss on the contract is recognized immediately.**
- Upon sell of forward contract, any profit or loss to be recognized **immediately in the statement of profit & loss.**

Example 6: (Foreign Exchange Contracts Hedge)

Shubham Purchased an asset @ 35,000 on Credit for 3 months. Date of transaction is 1/3/23 (Payable on 1/6/23)

Exchange Rate on 1/3/23 is \$1 = ₹ 80/-

Shubham is worried that \$ may rise in future & hence Shubham entered into Hedge Contract with HDFC to buy after 3 months. Forward Rate is \$1 = ₹ 82.35/-

Show Accounting in the books of Shubham.

Solution:

- 1) Shubham has purchased an Asset in \$35,000. Therefore, this is a "Foreign Currency Transaction". Foreign Currency Transaction should be recorded initially @ SPOT Rate i.e., 80/- 1/3/23

Asset A/c	Dr.	28,00,000	
To Foreign Creditors A/c (\$35,000 x 80)			28,00,000

- 2) On the same day i.e., 1/3/23, Shubham entered into Foreign Exchange (Hedge) Contract to buy dollar @ 82.35 after 3 months.

It means Shubham has fixed its loss at ₹ 2.35 x \$35,000 = 82,250

As per AS 11, this loss to Shubham is called as "Forward Premium" & it is to be amortised over the life of



contract to P&L A/c

$$82,250/3 = 27,417/-$$

3) On 31st March 23, Shubham shall recognise 27,417/- loss as under: -

Forward Premium A/c	Dr.	27,417	
To Foreign Creditor A/c			27,417
Profit & Loss A/c	Dr.	27,417	
To Forward Premium A/c			27,417

4) On 30th April & 31st May: Shubham shall pass following entries
30/4/23

Forward Premium A/c	Dr.	27,417	
To Foreign Creditor A/c			27,417
Profit & Loss A/c	Dr.	27,417	
To Forward Premium A/c			27,417

31/5/23

Forward Premium A/c	Dr.	27,416	
To Foreign Creditor A/c			27,416
Profit & Loss A/c	Dr.	27,416	
To Forward Premium A/c			27,416

1/6/23

Foreign Creditor A/c	Dr.	28,82,250	
To Bank A/c			28,82,250

Example 7: (Speculation)

Shubham entered into a contract with broker to buy (Long) \$10,000. Contract is made @ \$1 = 80/- . Actual SPOT Rate today is \$79.75/-

Contract date is 1st Feb; Contract is for 3 months

Show the Accounting as per AS 11.

Suppose on 31/3, same contract for 1 month can be made at \$1 = 80.40/-

Actual rate on Contract expiry \$1 = ₹ 81.25/-

Solution:

1) Shubham is doing speculation in dollars. Shubham feels that dollar may go up Shubham doesn't want to buy dollar physically.

2) Accounting Entries:

(a) On Contract Date: No Entry

(b) On Balance Sheet Date:

Foreign Exchange Contract Receivable A/c	Dr.	4,000	
To Foreign Exchange Gain (P&L) A/c			4,000
Foreign Exchange Gain A/c	Dr.	4,000	
To P&L A/c			4,000

(c) On Expiry Date / Settlement Date

Foreign Exchange Contract Receivable A/c	Dr.	8,500	
To Foreign Exchange Gain (P&L) A/c			8,500
Cash/Bank A/c	Dr.	12,500	
To Foreign Exchange Contract Receivable A/c			12,500



SECTION B – QUESTIONS

(Questions of Study Material, RTPs, MTPs and Past Exams to be Practiced in the Class)

SERIES 100

FOREIGN CURRENCY TRANSACTIONS

Q.ASII.RMP.101: (EXAM May 21)

(a) Classify the following items into Monetary and Non-monetary:

(i) Share capital; (ii) Trade Payables; (iii) Cash balance; (iv) Property, plant and equipment

(b) Trade payables of CAT Ltd. include amount payable to JBB Ltd., Rs. 10,00,000 recorded at the prevailing exchange rate on the date of transaction, transaction recorded at US \$1 = Rs. 80.00. The exchange rate on balance sheet date (31.03.2020) was US \$1 = Rs. 85.00. You are required to calculate the amount of exchange difference and also explain the accounting treatment needed for this as per AS II in the books of CAT Ltd.

SOLUTION

(a) Share capital - Non-monetary; Trade Payables - Monetary

Cash balance - Monetary; Property, plant and equipment - non-monetary

(b) Amount of Exchange difference and its Accounting Treatment

	Foreign Currency Rate	Rs.
Trade payables		
Initial recognition US \$ 12,500 (Rs. 10,00,000/80)	1 US \$ = Rs. 80	10,00,000
Rate on Balance sheet date		
Exchange Difference loss US \$ 12,500 x Rs. (85-80)	1 US \$ = Rs. 85	62,500
Treatment:		
Debit Profit and Loss A/c by Rs. 62,500 and Credit Trade Payables		

Thus, Exchange Difference on trade payables amounting Rs. 62,500 is required to be transferred to Profit and Loss.

Q.ASII.SM.102

	Exchange Rate per \$
Goods purchased on 1.1.20X1 for US \$ 15,000	₹75
Exchange rate on 31.3.20X1	₹74
Date of actual payment 7.7.20X1	₹73

You are required to ascertain the loss/gain to be recognized for financial years ended 31st March, 20X1 and 31st March, 20X2 as per AS II.

SOLUTION

As per AS II on 'The Effects of Changes in Foreign Exchange Rates', all foreign currency transactions should be recorded by applying the exchange rate on the date of transactions. Thus, goods purchased on



1.1.20X1 and corresponding creditors would be recorded at ₹11,25,000 (i.e. \$15,000 × ₹75)

According to the standard, at the balance sheet date all monetary transactions should be reported using the closing rate. Thus, creditors of US \$15,000 on 31.3.20X1 will be reported at ₹11,10,000 (i.e. \$15,000 × ₹74) and exchange profit of ₹15,000 (i.e. 11,25,000 – 11,10,000) should be credited to Profit and Loss account in the year ended 31st March, 20X1.

On 7.7.20X1, creditors of \$15,000 is paid at the rate of ₹73. As per AS 11, exchange difference on settlement of the account should also be transferred to Profit and Loss account. Therefore, ₹15,000 (i.e. 11,10,000 – 10,95,000) will be credited to Profit and Loss account in the year ended 31st March, 20X2.

Q.AS11.RMP.103: (RTP Nov22)

A company had imported raw materials worth US Dollars 6,00,000 on 5th January, 2022, when the exchange rate was Rs. 43 per US Dollar. The company had recorded the transaction in the books at the above-mentioned rate. The payment for the import transaction was made on 5th April, 2022 when the exchange rate was Rs. 47 per US Dollar. However, on 31st March, 2022, the rate of exchange was Rs. 48 per US Dollar. The company passed an entry on 31st March, 2022 adjusting the cost of raw materials consumed for the difference between Rs. 47 and Rs. 43 per US Dollar.

In the background of the relevant accounting standard, is the company's accounting treatment correct? Discuss

SOLUTION

As per AS 11 (revised 2003), 'The Effects of Changes in Foreign Exchange Rates', monetary items denominated in a foreign currency should be reported using the closing rate at each balance sheet date. The effect of exchange difference should be taken into profit and loss account. Trade payables is a monetary item, hence should be valued at the closing rate i.e., Rs. 48 at 31st March, 2022 irrespective of the payment for the same subsequently at lower rate in the next financial year. The difference of Rs. 5 (Rs. 48 – Rs. 43) per US dollar should be shown as an exchange loss in the profit and loss account for the year ended 31st March, 2022 and is not to be adjusted against the cost of raw materials. In the subsequent year, the company would record an exchange gain of Rs. 1 per US dollar, i.e., the difference between Rs. 48 and Rs. 47 per US dollar. Hence, the accounting treatment adopted by the company is incorrect.

Q.AS11.SM.104

Explain briefly the accounting treatment needed in the following cases as per AS 11 as on 31.3. 20X1.

Trade receivables include amount receivable from Umesh ₹5,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US \$ 1 = ₹58.50.

Long term loan taken from a U.S. Company, amounting to ₹60,00,000. It was recorded at US \$ 1 = ₹55.60, taking exchange rate prevailing at the date of transaction. US \$ 1 = ₹61.20 was on 31.3. 20X1.

Answer

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognised as income or as expenses in the period in which they arise. However, at the option of an entity, exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-



depreciable capital asset can be accumulated in a “Foreign Currency Monetary Item Translation Difference Account” in the enterprise’s financial statements and amortised over the balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

Trade receivables	Foreign Currency Rate	₹
Initial recognition US \$8,547 (5,00,000/58.50)	1 US \$ = ₹ 58.50	5,00,000
Rate on Balance sheet date	1 US \$ = ₹ 61.20	
Exchange Difference Gain US \$ 8,547 X (61.20-58.50)		23,077
Treatment: Credit Profit and Loss A/c by ₹23,077		
Long term Loan		
Initial recognition US \$ 1,07,913.67 (60,00,000/55.60)	1 US \$ = ₹ 55.60	60,00,000
Rate on Balance sheet date	1 US \$ = ₹ 61.20	
Exchange Difference Loss US \$ 1,07,913.67 X (61.20 - 55.60)		6,04,317
Treatment: Credit Loan A/c And Debit FCMITD A/C or Profit and Loss A/c by ₹ 6,04,317		

Thus, Exchange Difference on Long term loan amounting ₹6,04,317 may either be charged to Profit and Loss A/c or to Foreign Currency Monetary Item Translation Difference Account but exchange difference on debtors amounting ₹23,077 is required to be transferred to Profit and Loss A/c.

Q.ASII.SM.105

Kalim Ltd. borrowed US\$ 4,50,000 on 01/01/2016, which will be repaid as on 31/07/2016. Kalim Ltd. prepares financial statement ending on 31/03/2016. Rate of exchange between reporting currency (INR) and foreign currency (USD) on different dates are as under:

01/01/2016 1 US\$ = Rs 48.00

31/03/2016 1 US\$ = Rs 49.00

31/07/2016 1 US\$ = Rs 49.50

SOLUTION

Journal Entries in the Books of Kalim Ltd.

Date	Particulars	Rs (Dr.)	Rs (Cr.)
Jan. 01, 2016	Bank Account (4,50,000 x 48) Dr.	216,00,000	
	To Foreign Loan Account		216,00,000
Mar. 31, 2016	Foreign Exchange Difference Account Dr.	4,50,000	
	To Foreign Loan Account [4,50,000 x (49-48)]		4,50,000
Jul. 01, 2016	Foreign Exchange Difference Account Dr. [4,50,000 x (49.5-49)]	2,25,000	
	Foreign Loan Account Dr.	220,50,000	
	To Bank Account		2,22,75,000

Q.ASII.OM.106

Opportunity Ltd. purchased an equipment costing Rs 24,00,000 on 1.4.2015 and the same was fully financed by foreign currency loan (US Dollars) payable in four annual equal installments. Exchange rates were 1 Dollar = Rs 60.00 and Rs 62.50 as on 1.4.2015 and 31.3.2016 respectively. First installment was paid on 31.3.2016. The entire difference in foreign exchange has been capitalised. You are required to state that how these transactions would be accounted for.



SOLUTION

As per AS 11 'The Effects of Changes in Foreign Exchange Rates', exchange differences arising on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, should be recognised as income or expenses in the period in which they arise. Thus, exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets will be recognised as income or expense.

Calculation of Exchange Difference:

Foreign currency loan =	Rs 24,00,000/60 = 40,000 US Dollars
Exchange difference =	40,000 US Dollars × (62.50-60.00) = Rs 1,00,000
(Including exchange loss on payment of first instalment)	

Therefore, entire loss due to exchange differences amounting Rs 1,00,000 should be charged to profit and loss account for the year.

Note: The above answer has been given on the basis that the company has not availed the option for capitalisation of exchange difference as per paragraph 46/ 46A of AS 11.

However, as per paragraph 46A of the standard, the exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, in so far as they relate to the acquisition of a depreciable capital asset, can be added to or deducted from the cost of the asset and should be depreciated over the balance life of the asset.

Accordingly, in case Opportunity Ltd. opts for capitalising the exchange difference, then the entire amount of exchange difference of Rs 1,00,000 will be capitalised to 'Equipment account'. This capitalised exchange difference will be depreciated over the useful life of the asset.

Cost of the asset on the reporting date

Initial cost of Equipment	Rs 24,00,000
Add: Exchange difference	<u>Rs 1,00,000</u>
Total cost on the reporting date	<u>Rs 25,00,000</u>

Q.AS11.RMP.107: (MTP May18, Nov21)

Om Ltd. purchased an item of property, plant and equipment for US \$ 50 lakh on 01.04.2019 and the same was fully financed by the foreign currency loan [US \$] repayable in five equal installments annually. (Exchange rate at the time of purchase was 1 US \$ = Rs. 60). As on 31.03.2020 the first installment was paid when 1 US \$ fetched ₹ 62.00. The entire loss on exchange was included in cost of goods sold. Om Ltd. normally provides depreciation on an item of property, plant and equipment at 20% on WDV basis and exercised the option to adjust the cost of asset for exchange difference arising out of loan restatement and payment. Calculate the amount of exchange loss, its treatment and depreciation on this item of property, plant and equipment.

SOLUTION

Exchange differences arising on restatement or repayment of liabilities incurred for the purpose of acquiring an item of property, plant and equipment should be adjusted in the carrying amount of the respective item of property, plant and equipment as Om Ltd. has exercised the option and it is long term foreign currency monetary item. Thus, the entire exchange loss due to variation of Rs. 20 lakhs



on 31.03.2020 on payment of US \$ 10 lakh, should be added to the carrying amount of an item of property, plant and equipment and not to the cost of goods sold. Further, depreciation on the unamortized depreciable amount should also be provided.

Calculation of Exchange loss:

Foreign currency loan (in Rs.) = (50 lakh \$ x Rs. 60) = Rs. 3,000 lakhs

Exchange loss on outstanding loan on 31.03.2020 = Rs. 40 lakh US \$ x (62.00-60.00) = Rs. 80 lakhs.

So, Rs. 80 lakhs should also be added to cost of an item of property, plant and equipment with corresponding credit to outstanding loan in addition to Rs. 20 lakhs on account of exchange loss on payment of installment. The total cost of an item of property, plant and equipment to be increased by Rs. 100 lakh. Total depreciation to be provided for the year 2019-2020 = 20% of (Rs. 3,000 lakh + 100 lakh) = Rs. 620 lakhs.

Q.ASII.RMP.108 (EXAM May23)

Trower Limited is an Indian importer. It imports goods from True View Limited situated at London. Trower Limited has a payable of £ 50,000 to True view Limited as on 31st March, 2023. True View Limited has given Trower Limited the following two option:

(i) Pay immediately with a cash discount of 1% on the payable.

(ii) Pay after 6 months with interest @ 5% p.a. on the Payable.

The borrowing rate for Trower Limited in rupees is 15% p.a.

The following are the exchange rates:

Date	₹/£
31 st March, 2023	97
30 th September, 2023	99

You are required to give your opinion to Trower Limited on which of the above two options to be chosen.

Solution

Option (i) Pay immediately with Cash discount of 1% on the payable

	₹
Total amount payable as on 31.3.2023 (50,000 x ₹ 97)	48,50,000
Less: Cash discount	(48,500)
	48,01,500
Add: Borrowing cost @ 15% p.a. for 6 months	3,60,112.50
If payment made immediate	51,61,612.50

Option (ii) Pay after 6 months with interest @ 5% p.a. on the payable

	₹
Total amount payable as on 31.3.2023 (50,000 x ₹ 99)	49,50,000
Interest for 6 months @ 5%	1,23,750
If payment made after 6 months	50,73,750

Thus, Option (ii) is beneficial to Trower Limited as the Rupee outflow will be lower by ₹ (51,61,612 - 50,73,750) = ₹ 87,862 in option (ii).

Note: The above answer be presented in the alternative manner given as below:



Option (i) Pay immediately with Cash discount of 1% on the payable

Total amount payable on 31.3.2023	50,000
Less: Cash discount $(50,000 \times 1 / 100)$	(500)
	49,500
$49,500 \times ₹ 97$	48,01,500
Add: Borrowing cost @ 15% p.a. for 6 months	3,60,112.50
If payment made immediate	₹ 51,61,612.50

Option (ii) Pay after 6 months with interest @ 5% p.a. on the payable

	₹
Total amount payable on 31.3.2023	50,000
Interest for 6 months @ 5% $(50,000 \times 5 / 100 \times 6 / 12)$	1,250
	51,250
If payment made after 6 months $(51,250 \times 99)$	50,73,750

Thus, Option (ii) is beneficial to Trower Limited as the Rupee outflow will be lower by ₹ $(51,61,612 - 50,73,750) = ₹ 87,862$ in option (ii).

SERIES 200
FOREIGN OPERATIONS (BRANCHES)

Q.ASII.SM.201

A business having the Head Office in Kolkata has a branch in UK. The following is the trial balance of Branch as at 31.03.20X4:

Account Name	Amount in £	
	Dr.	Cr.
Property, Plant and Equipment (Purchased on 01.04.20X1)	5,000	20,000
Debtors	1,600	
Opening Stock	400	
Goods received from Head Office Account (Recorded in HO books as ₹4,02,000)	6,100	
Sales		
Purchases	10,000	7,400 4,000
Wages	1,000	
Salaries	1,200	
Cash	3,200	
Remittances to Head Office (Recorded in HO books as ₹1,91,000)	2,900	
Head Office Account (Recorded in HO books as ₹4,90,000)		
Creditors		

- Closing stock at branch is £ 700 on 31.03.20X4.
- Depreciation @ 10% p.a. is to be charged on Property, plant and equipment.
- Prepare the trial balance after been converted in Indian Rupees.

Exchange rates of Pounds on different dates are as follow: 01.04.20X1- ₹61; 01.04.20X3- ₹63 & 31.03.20X4 - ₹67

SOLUTION

Trial Balance of the Foreign Branch converted into Indian Rupees as on March 31, 20X4

Particulars	£ (Dr.)	£ (Cr.)	Conversion Basis	₹ (Dr.)	₹ (Cr.)
Property, plant and equipment	5,000		Transaction Date Rate	3,05,000	
Debtors	1,600		Closing Rate	1,07,200	
Opening Stock	400		Opening Rate	25,200	
Goods Received from HO	6,100		Actuals	4,02,000	
Sales		20,000	Average Rate		13,00,000
Purchases	10,000		Average Rate	6,50,000	
Wages	1,000		Average Rate	65,000	
Salaries	1,200		Average Rate	78,000	
Cash	3,200		Closing Rate	2,14,400	
Remittance to HO	2,900		Actuals	1,91,000	
HO Account		7,400	Actuals		4,90,000
Creditors		4,000	Closing Rate		2,68,000
Exchange Rate Difference			Balancing Figure	20,200	



	31,400	31,400		20,58,000	20,58,000
Closing Stock	700		Closing Rate	46,900	
Depreciation	500		Fixed Asset Rate	30,500	

SERIES 300

FORWARD EXCHANGE CONTRACTS

Q.ASII.SM.301

Mr. A bought a forward contract for three months of US\$ 1,00,000 on 1st December at 1 US\$ = Rs 47.10 when exchange rate was US\$ 1 = Rs 47.02. On 31st December when he closed his books exchange rate was US\$ 1 = Rs 47.15. On 31st January, he decided to sell the contract at Rs 47.18 per dollar. Show how the profits from contract will be recognised in the books.

SOLUTION

Since the forward contract was for speculation purpose the premium on contract i.e. the difference between the spot rate and contract rate will not be recorded in the books. Only when the contract is sold the difference between the contract rate and sale rate will be recorded in the Profit & Loss Account.

Sale Rate	Rs 47.18
Less: Contract Rate	(Rs 47.10)
Premium on Contract	<u>Rs 0.08</u>
Contract Amount	US\$ 1,00,000
Total Profit (1,00,000 x 0.08)	Rs 8,000



SECTION C – MCQ's

(MCQ's from ICAI Study Material)

1. As per AS 11 assets and liabilities of non-integral foreign operations should be converted at rate.
 - (a) Opening
 - (b) Average
 - (c) Closing
 - (d) Transaction
2. The debit or credit balance of "Foreign Currency Monetary Item Translation Difference Account"
 - (a) Is shown as "Miscellaneous Expenditure" in the Balance Sheet
 - (b) Is shown under "Reserves and Surplus" as a separate line item
 - (c) Is shown as "Other Non-current" in the Balance Sheet
 - (d) Is shown as "Current Assets" in the Balance Sheet
3. If asset of an integral foreign operation is carried at cost, cost and depreciation of tangible fixed asset is translated at
 - (a) Average exchange rate
 - (b) Closing exchange rate
 - (c) Exchange rate at the date of purchase of asset
 - (d) Opening exchange rate
4. Which of the following can be classified as an integral foreign operation?
 - (a) Branch office serving as an extension of the head office in terms of operations
 - (b) Independent subsidiary of the parent company
 - (c) Branch office independent of the head office in terms of operational decisions
 - (d) None of the above
5. Which of the following items should be converted to closing rate for the purposes of financial reporting?
 - (a) Items of Property, Plant and Equipment
 - (b) Inventory
 - (c) Trade Payables, Trade Receivables and Foreign Currency Borrowings
 - (d) All of the above

ANSWERS	1	2	3	4	5
	c	b	c	a	c



SECTION D – QUESTIONS FOR SELF PRACTICE

(Questions of Study Material, RTPs, MTPs and Past Exams to be Practiced at Home)

SERIES 100

FOREIGN CURRENCY TRANSACTIONS

Q.AS11.SM.109

Classify the following items as monetary or non-monetary item:

Inventories

Trade Receivables

Investment in Equity shares

Property, Plant and Equipment.

SOLUTION

Inventories	Non-monetary
Trade receivables	Monetary
Investment in equity shares	Non-monetary
Property, Plant and Equipment	Non-monetary

Q.AS11.RMP.110: (RTP May22; EXAM May18; MTP Nov22)

Kumar Ltd. borrowed US \$ 3,00,000 on 31-12-2020 which will repaid as on 30-06-2021. Kumar Ltd. prepares its financial statements ending on 31-03-2021. Rate of exchange between reporting currency (Rupee) and foreign currency (US\$) on different dates are as under:

31-12-2020	1 US \$ = Rs. 44.00
31-03-2021	1 US \$ = Rs. 44.50
30-06-2021	1 US \$ = Rs. 44.75

- (i) Calculate Borrowings in reporting currency to be recognized in the books on above mentioned dates and also show journal entries for the same.
- (ii) if borrowings were repaid on 28-2-2021 on which date exchange rate was 1 US \$ = Rs. 44.20 then what entry should be passed?

SOLUTION

- (i) As per AS 11 'The Effect of Changes in Foreign Exchange Rates', a foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction. Moreover, at each balance sheet date, foreign currency monetary items should be reported using the closing rate. Accordingly, on 31.12.2020 borrowings will be recorded at Rs. 1,32,00,000 (i.e., Rs. 3,00,000 × Rs. 44.00). On 31.3.2021 borrowings (monetary items) will be recorded at Rs. 1,33,50,000 (i.e. \$ 3,00,000 × Rs. 44.50).

Journal of Kumar Ltd.

Date	Particular	Dr. (Rs.)	Cr. (Rs.)
31-12-2020	Bank A/c	Dr. 1,32,00,000	



	To Foreign Loan Account		1,32,00,000
31-03-2021	Foreign Exchange Difference Account A/c Dr.	1,50,000	
	To Foreign Loan Account		1,50,000
30-06-2021	Foreign Loan Account A/c Dr.	1,33,50,000	
	Foreign Exchange Difference Account A/c Dr.	75,000	
	To Bank A/c		1,34,25,0000

(ii) In case borrowings were repaid before Balance Sheet Date, then the entry would be as follows:

Date	Particular	Dr. (Rs.)	Cr. (Rs.)
28-02-2021	Foreign Loan Account A/c Dr.	1,32,00,000	
	Foreign Exchange Difference Account A/c Dr.	60,000	
	To Bank A/c		1,32,60,000

Working Notes:

- (i) The exchange difference of Rs. 1,50,000 is arising because the transaction has been reported at different rate (Rs. 44.50 = 1 US \$) from the rate initially recorded (i.e., Rs. 44 = 1 US \$) from the rate initially recorded (i.e., Rs. 44 = 1 US \$)
- (ii) The exchange difference of Rs. 75,000 is arising because the transaction has been settled at an exchange rate (Rs. 44.75 = 1 US\$) different from the rate at which reported in the last financial statements (Rs. 44.50 = 1 US\$).
- (iii) The exchange difference of Rs. 60,000 is arising because the transaction has been settled at a different rate (i.e., Rs. 44.20 = 1 US \$) than the rate at which initially recorded (1 US \$ = Rs. 44.00)

Q.ASII.SM.III

A Ltd. has borrowed USD 10,000 in foreign currency on April 1, 20X1 at 5% p.a. annual interest and acquired a depreciable asset. The exchange rates are as under:

01/04/20X1 1 US\$ = ₹ 48.00

31/03/20X2 1 US\$ = ₹ 51.00

You are required to pass the journal entries in the following cases:

- (i) Option under Para 46A is not availed.
- (ii) Option under Para 46A is availed.
- (iii) The loan was taken to finance the operations of the entity (and not to procure a depreciable asset).

In all cases, assume interest accrued on 31 March 20X2 is paid on the same date.

Solution

Journal Entries in the Books of A Ltd.

(i) Option under Para 46A is not availed

Date	Particulars	₹(Dr.)	₹(Cr.)
20X1			
Apr. 01	Bank Account (10,000 x 48) Dr.	4,80,000	
	To Foreign Loan Account		4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹51) Dr.	25,500	
	To Bank Account		25,500
Mar 31	Foreign Exchange Difference Account (P/L) Dr.	30,000	
	To Foreign Loan Account [10,000 x (51-48)]		30,000

In this case, since the option under Para 46A is **NOT** availed, the Exchange Loss of ₹ 30,000 is recognised as an expense in the Statement of Profit and Loss for the year ending 31 March 20X2.



(ii) Option under Para 46A is availed

Date	Particulars		₹(Dr.)	₹(Cr.)
20X1				
Apr. 01	Bank Account (10,000 x 48) Dr.		4,80,000	
	To Foreign Loan Account			4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹51) Dr.		25,500	
	To Bank Account			25,500
Mar 31	Foreign Exchange Difference Account (P/L) Dr.		30,000	
	To Foreign Loan Account [10,000 x (51-48)]			30,000
Mar 31	Property Plant & Equipment A/c Dr.		30,000	
	To Foreign Exchange Difference A/c			30,000

In this case, since the option under Para 46A is availed, the Exchange Loss of ₹ 30,000 is capitalized in the cost of Property, Plant and Equipment, which will indirectly get recognized in the Profit & Loss A/c by way of increased depreciation over the remaining useful life of the asset.

(iii) Option under Para 46A is availed

Date	Particulars		₹(Dr.)	₹(Cr.)
20X1				
Apr. 01	Bank Account (10,000 x 48) Dr.		4,80,000	
	To Foreign Loan Account			4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹51) Dr.		25,500	
	To Bank Account			25,500
Mar 31	Foreign Exchange Difference Account (P/L) Dr.		30,000	
	To Foreign Loan Account [10,000 x (51-48)]			30,000
Mar 31	Foreign Currency Monetary Item Translation Difference A/c (FCMITDA) Dr.		30,000	
	To Foreign Exchange Difference A/c			30,000

In this case, since the option under Para 46A is availed, the Exchange Loss of ₹ 30,000 is accumulated in the FCMITD A/c, which will be subsequently spread over and debited to P&L A/c over the tenure of the loan.

Q.ASII.SM.112

A Ltd. purchased fixed assets costing Rs 3,000 lakhs on 1.1.2016 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal instalments. Exchange rates were 1 Dollar = Rs 40.00 and Rs 42.50 as on 1.1.2016 and 31.12.2016 respectively. First instalment was paid on 31.12.2016. The entire difference in foreign exchange has been capitalised.

You are required to state, how these transactions would be accounted for.

SOLUTION

As per AS II 'The Effects of Changes in Foreign Exchange Rates', exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognised as income or expenses in the period in which they arise. Thus exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets are recognised as income or expense.

Calculation of Exchange Difference:

$$\text{Foreign currency loan} = \frac{\text{Rs 3000 lakhs}}{\text{Rs 40}} = 75 \text{ lakhs US Dollars}$$



Exchange difference = 75 lakhs US Dollars \times (42.50 – 40.00) = Rs 187.50 lakhs (including exchange loss on payment of first instalment)

Therefore, entire loss due to exchange differences amounting Rs 187.50 lakhs should be charged to profit and loss account for the year.

Note: The above answer has been given on the basis that the company has not exercised the option of capitalisation available under paragraph 46 of AS 11. However, if the company opts to avail the benefit given in paragraph 46A, then nothing is required to be done since the company has done the correct treatment.

Q.AS11.RMP.113:(EXAM Nov18)

- (i) ABC Ltd. an Indian Company obtained long term loan from WWW private Ltd., a U.S. company amounting to Rs. 30,00,000. It was recorded at US \$1 = Rs. 60.00, taking exchange rate prevailing at the date of transaction. The exchange rate on balance sheet date (31.03.2018) was US \$1 = Rs. 62.00.
- (ii) Trade receivable includes amount receivable from Preksha Ltd., Rs. 10,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US \$1 = Rs. 59.00. The exchange rate on balance sheet date (31.03.2018) was US \$1 = Rs. 62.00.

You are required to calculate the amount of exchange difference and also explain the accounting treatment needed in the above two cases as per AS 11 in the books of ABC Ltd.

SOLUTION

Amount of Exchange difference and its Accounting Treatment

Long term Loan		Foreign Currency Rate	Rs
(i)	Initial recognition US \$ 50,000 Rs. (30,00,000/60) Rate on Balance sheet date Exchange Difference Loss US \$ 50,000 \times Rs. (62 – 60) Treatment: Credit Loan A/c and Debit FCMITD A/c or Profit and Loss A/c by Rs. 1,00,000 Trade receivables	1 US \$ = Rs. 60 1 US \$ = Rs. 62	30,00,000 1,00,000
(ii)	Initial recognition US \$ 16,949.152* (Rs. 10,00,000/59) Rate on Balance sheet date Exchange Difference Gain US \$ 16,949.152* \times Rs. (62–59) Treatment: Credit Profit and Loss A/c by Rs. 50,847.456* And Debit Trade Receivables	1 US \$ = Rs. 59 1 US \$ = Rs. 62	10,00,000 50,847.456*

Thus, Exchange Difference on Long term loan amounting Rs. 1,00,000 may either be charged to Profit and Loss A/c or to Foreign Currency Monetary Item Translation Difference Account but exchange difference on trade receivables amounting Rs. 50,847.456 is required to be transferred to Profit and Loss A/c.

Q.AS11.RMP.114: (EXAM Jan21) (Similar to Q.113)

Explain briefly the accounting treatment needed in the following cases as per AS 11 as on 31.03.2020.

- (i) Debtors include amount due from Mr. SRs. 9,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US \$ 1 = Rs. 72.00
US \$ 1 = Rs. 73.50 on 31st March 2020
US \$ 1 = Rs. 72.50 on 1st April 2019
- (ii) Long term loan taken on 1st April 2019 from a US Company amounting to Rs. 75,00,000. Rs. 5,00,000 was repaid on 31st December 2019 recorded at US \$ 1 = Rs. 70.50. Interest has been paid as and



when debited by the US Company.

US \$ 1 = Rs. 73.50 on 31st March 2020

US \$ 1 = Rs. 72.50 on 1st April 2019

SOLUTION

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.

However, at the option of an entity, exchange differences arising on reporting of long term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-depreciable capital asset can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over the balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

	Foreign Rate	Currency	Rs.
Debtors			
Initial recognition US \$12,500 (9,00,000/72)	1 US \$ = Rs. 72		9,00,000
Rate on Balance sheet date	1 US \$ = Rs. 73.50		
Exchange Difference Gain US \$ 12,500 X (73.50/72)			18,750
Treatment: Credit Profit and Loss A/c by Rs. 18,750			
Long term Loan			
Initial recognition US \$ 1,03,448.28 (75,00,000/72.50)	1 US \$ = Rs. 73.50		75,00,000
Rate on Balance sheet date	1 US \$ = Rs. 73.50		
Exchange Difference Loss after adjustment of exchange gain on repayment of Rs. 5,00,000			
Rs. 67,987.48 [82,171.88 (US \$ 96,356.08 X Rs. 73.5 less Rs. 70,00,000) less profit 14,184.40 [US \$ 7,092.2 (5,00,000/70.5) X Rs. 2]] NET LOSS			67,987.48*
Treatment: Credit Loan A/c and Debit FCMITD A/C or Profit and Loss A/c by Rs. 67,987.48			

Thus, Exchange Difference on Long term loan amounting Rs. 67,987.48 may either be charged to Profit and Loss A/c or to Foreign Currency Monetary Item Translation Difference Account but exchange difference on debtors amounting Rs. 18,750 is required to be transferred to Profit and Loss A/c.

NOTE 1: *Exchange Difference Loss (net of adjustment of exchange gain on repayment of Rs. 5,00,000) has been calculated in the above solution. Alternative considering otherwise also possible.

NOTE 2: Date of sales transaction of Rs. 9 lakhs has not been given in the question and hence it has been assumed that the transaction took place during the year ended 31 March 2020.

Q.AS11.RMP.115: (EXAM Dec21) (Similar to Q.113)

(i) PP Ltd. an Indian Company acquired long term finance from WW (p) Ltd, a U.S. company, amounting to Rs. 40,88,952. The transaction was recorded at US \$1 = Rs. 72.00, tanking exchange rate prevailing at the date of transaction. The exchange rate on balance sheet date (31.03.2021) is US \$1 = Rs. 73.60.



(ii) Trade receivable of PP Ltd. include amount receivable from Preksha Ltd. Rs. 20,00,150 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US \$1 = Rs. 73.40. The exchange rate on balance sheet date (31.03.2021) is US \$1 = Rs. 73.60. Exchange rate on 1st April, 2020 is US \$1 = Rs. 74.00

You are required to calculate the amount of exchange difference and also explain the accounting treatment needed in the above two cases as per AS 11 in the books of PP Ltd.

Solution

(i) Long term Finance

	Foreign Currency Rate	Rs.
Initial recognition US \$ 56,791 (40,88,952/72)	1 US \$ = Rs. 72	40,88,952
Rate on Balance sheet date	1 US \$ = Rs. 73.60	
Exchange Difference Loss [US \$ 56,791 x (73.60 - 72)]		90,866 (Rounded off)

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.

However, at the option of an entity, exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-depreciable capital asset can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over the balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

Treatment needed in this case: PP Ltd. can either Debit Foreign Currency Monetary Item Translation Difference (FCMITD) A/c or Debit Profit and Loss A/c by Rs. 90,866 and Credit Loan A/c

(ii) Trade Receivables

	Foreign Currency Rate	Rs.
Initial recognition US \$ 27,250 (20,00,150/ 73.40)	1 US \$ = Rs. 73.40	20,00,150
Rate on Balance sheet date	1 US \$ = Rs. 73.60	
Exchange Difference Gain [US \$ 27,250 X (73.60-73.40)]		5,450

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences on trade receivables amounting Rs. 5,450 is required to be transferred to Profit and Loss A/c.

Treatment needed in this case: Credit Profit and loss account by Rs. 5,450.

SERIES 200
FOREIGN OPERATIONS (BRANCHES)

Q.ASII.SM.202

Assets and liabilities and income and expenditure items in respect of foreign branches (integral foreign operations) are translated into Indian rupees at the prevailing rate of exchange at the end of the year. The resultant exchange differences in the case of profit, is carried to other Liabilities Account and the Loss, if any, is charged to the statement of profit and loss. Comment.

SOLUTION

The financial statements of an integral foreign operation (for example, dependent foreign branches) should be translated using the principles and procedures described in AS 11. The individual items in the financial statements of a foreign operation are translated as if all its transactions had been entered into by the reporting enterprise itself.

Individual items in the financial statements of the foreign operation are translated at the actual rate on the date of transaction. For practical reasons, a rate that approximates the actual rate at the date of transaction is often used, for example, an average rate for a week or a month may be used for all transactions in each foreign currency during the period. The foreign currency monetary items (for example cash, receivables, payables) should be reported using the closing rate at each balance sheet date. Non-monetary items (for example, fixed assets, inventories, investments in equity shares) which are carried in terms of historical cost denominated in a foreign currency should be reported using the exchange rate at the date of transaction. Thus the cost and depreciation of the tangible fixed assets is translated using the exchange rate at the date of purchase of the asset if asset is carried at cost. If the fixed asset is carried at fair value, translation should be done using the rate existed on the date of the valuation. The cost of inventories is translated at the exchange rates that existed when the cost of inventory was incurred and realisable value is translated applying exchange rate when realisable value is determined which is generally closing rate.

Exchange difference arising on the translation of the financial statements of integral foreign operation should be charged to profit and loss account. Exchange difference arising on the translation of the financial statement of foreign operation may have tax effect which should be dealt as per AS 22 'Accounting for Taxes on Income'.

Thus, the treatment by the management of translating all assets and liabilities; income and expenditure items in respect of foreign branches at the prevailing rate at the year end and also the treatment of resultant exchange difference is not in consonance with AS 11.

Q.ASII.RMP.203: (EXAM Nov19)

Karan Enterprises having its Head Office in Mangalore, Karnataka has a branch in Greenville, USA. Following is the trial balance of Branch as at 31-3-2019:

Particulars	Amount (\$)	Amount (\$)
	Dr.	Cr.
Fixed assets	8,000	
Opening inventory	800	
Cash	700	
Goods received from Head Office	2,800	
Sales		24,050

Purchases	11,800	
Expenses	1,800	
Remittance to head office	2,450	
Head office account		4,300
	28,350	28,350

- (i) Fixed assets were purchased on 1st April, 2015.
(ii) Depreciation at 10% p.a. is to be charged on fixed assets on straight line method.
(iii) Closing inventory at branch is \$ 700 as on 31-3-2019.
(iv) Goods received from Head Office (HO) were recorded at Rs. 1,85,500 in HO books.
(v) Remittances to HO were recorded at Rs. 1,62,000 in HO books.
(vi) HO account is recorded in HO books at Rs. 2,84,500.
(vii) Exchange rates of US Dollar at different dates can be taken as:

1-4-2015 Rs. 63

1-4-2018 Rs. 65

31-3-2019 Rs. 67

Prepare the trial balance after been converted into Indian rupees in accordance with AS-11.

SOLUTION

Trial Balance of Foreign Branch (converted into Indian Rupees) as on March 31, 2019

Particulars	\$ (Dr.)	\$ (Cr.)	Conversion Basis	Rate	Rs (Dr.)	Rs (Cr.)
Fixed Assets	8,000		Transaction Date Rate	63	5,04,000	
Opening Inventory	800		Opening Rate	65	52,000	
Goods Received from HO	2,800		Actuals		1,85,500	
Sales		24,050	Average Rate	66		15,87,300
Purchases	11,800		Average Rate	66	7,78,800	
Expenses	1,800		Average Rate	66	1,18,800	
Cash	700		Closing Rate	67	46,900	
Remittance to HO	2,450		Actuals		1,62,000	
HO Account		4,300	Actuals			2,84,500
Exchange Rate Difference			Balancing Figure		23,800	
	28,350	28,350			18,71,800	18,71,800
Closing Stock	700		Closing Rate	67	46,900	
Depreciation	800		Fixed Asset Rate	63	50,400	



SERIES 300
FORWARD EXCHANGE CONTRACTS

Q.ASII.RMP.302 (RTP May19, MTP March20)

Rau Ltd. purchased a plant for US\$ 1,00,000 on 01st February 20X1, payable after three months. Company entered into a forward contract for three months @ ₹49.15 per dollar. Exchange rate per dollar on 01st Feb. was ₹48.85. How will you recognise the profit or loss on forward contract in the books of Rau Ltd.?

SOLUTION

Forward Rate	₹49.15
Less: Spot Rate	(₹48.85)
Premium on Contract	₹0.30
Contract Amount	US\$ 1,00,000
Total Loss (1,00,000 x 0.30)	₹30,000

Contract period 3 months (2 months falling in the year ended 31st March, 20X1)

Loss to be recognised (30,000/3) x 2 = ₹20,000 in the year ended 31st March, 20X1. Rest ₹10,000 will be recognised in the following year.

In recording a forward exchange contract intended for trading or speculation purposes, the premium or discount on the contract is ignored and at each balance sheet date, the value of the contract is marked to its current market value and the gain or loss on the contract is recognised.

Q.ASII.RMP.303 (RTP May18) (Similar to Q.302)

Power Track Ltd. purchased a plant for US\$ 50,000 on 31st October, 2016 payable after 6 months. The company entered into a forward contract for 6 months @ Rs. 64.25 per Dollar. On 31st October, 2016, the exchange rate was Rs. 61.50 per Dollar.

You are required to calculate the amount of the profit or loss on forward contract to be recognized in the books of the company for the year ended 31st March, 2017.

SOLUTION

Calculation of profit or loss to be recognized in the books of Power Track Limited

Forward contract rate	64.25
Less: Spot rate	(61.50)
Loss on forward contract	2.75
Forward Contract Amount	\$ 50,000
Total loss on entering into forward contract = (\$ 50,000 x Rs. 2.75)	Rs. 1,37,500
Contract period	6 months
Loss for the period 1st November, 2016 to 31st March, 2017 i.e., 5 months falling in the year 2016-2017	5 months
Hence, Loss for 5 months will be Rs. 1,37,500 $\times \frac{5}{6}$	Rs. 1,14,583

Thus, the loss amounting to Rs. 1,14,583 for the period is to be recognized in the year ended 31st March, 2017.



Q.ASII.RMP.304 (RTP Nov 19)

- (i) Trade receivables as on 31.3.2019 in the books of XYZ Ltd. include an amount receivable from Umesh Rs. 5,00,000 recorded at the prevailing exchange rate on the date of sales, i.e., at US \$ 1 = Rs. 58.50. US \$ 1 = Rs. 61.20 on 31.3.2019.

Explain briefly the accounting treatment needed in this case as per AS II as on 31.3.2019.

- (ii) Power Track Ltd. purchased a plant for US\$ 50,000 on 31st October, 2018 payable after 6 months. The company entered into a forward contract for 6 months @ Rs. 64.25 per Dollar. On 31st October, 2018, the exchange rate was Rs. 61.50 per Dollar.

You are required to recognise the profit or loss on forward contract in the books of the company for the year ended 31st March, 2019.

SOLUTION

- (i) As per AS II “The Effects of Changes in Foreign Exchange Rates”, exchange differences arising on the settlement of monetary items or on reporting an enterprise’s monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.

Accordingly, exchange difference on trade receivables amounting Rs. 23,076 {Rs. 5,23,076(US \$ 8547 x Rs. 61.20) less Rs. 5,00,000} should be charged to profit & Loss account.

- (ii) Calculation of profit or loss to be recognized in the books of Power Track Limited

	Rs.
Forward contract rate	64.25
Less: Spot rate	(61.50)
Loss on forward contract	2.75
Forward Contract Amount	\$ 50,000
Total loss on entering into forward contract = (\$ 50,000 × Rs. 2.75)	Rs. 1,37,500
Contract period	6 months
Loss for the period 1 st November, 2018 to 31 st March, 2019 i.e., 5 months falling in the year 2018-2019	5 months
Hence, Loss for 5 months will be Rs. 1,37,500 X 5/6 =	Rs. 1,14,583

Thus, the loss amounting to Rs. 1,14,583 for the period is to be recognized in the year ended 31st March, 2019.

Q.ASII.RMP.305: (EXAM Nov22) Similar to 304

- (i) Jared Limited purchased a Machine for US \$ 20,000 on 31st December, 2021 payable after four months. It entered into a forward contract for four months @ ₹ 78.85 per US \$. On 31st December, 2021 the exchange rate was ₹ 77.50 per US \$.

How will you recognize the Profit or Loss on Forward Contract for the year ended 31st March, 2022 in the books of Jared Limited?

- (ii) Trade Payables of Jared Limited includes amount due to Sterling Limited ₹ 9,75,000 recorded at



the prevailing exchange rate on the date of purchase; transaction recorded at US \$ 1 = ₹ 75.00. The exchange rate on Balance Sheet date (31st March, 2022) was US \$ 1 = ₹ 79.00 The payment was made on 1st May, 2022 when the exchange rate was US \$ 1 = ₹ 78.30.

You are required to calculate the amount of exchange difference on 31st March, 2022 and 1st May, 2022 and also explain the accounting treatment needed in the above case as per AS 11 in the books of Jared Limited.

Solution

(i)

	₹
Forward Rate	78.85
Less: Spot Rate	(77.50)
Premium on Contract	1.35
Contract Amount	US\$ 20,000
Total Loss (20,000 x 1.35)	₹ 27,000

Contract period 4 months (3 months falling in the year ended 31st March, 2022)

Loss to be recognized ($₹27,000 \times 3/4$) = ₹ 20,250 in the year ended 31st March, 2022.

(ii) As per AS 11 “The Effects of Changes in Foreign Exchange Rates”, exchange differences arising on the settlement of monetary items or on reporting an enterprise’s monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.

Trade payables	Foreign Currency Rate	Amount ₹
Initial recognition US \$13,000 (9,75,000/75)	1 US \$ = ₹ 75	
Exchange Rate on Balance sheet date	1 US \$ = ₹ 79	
Exchange Difference Loss US \$ 13,000 X (79-75)		52,000
Exchange Rate on Settlement date	1 US \$ = ₹ 78.30	
Exchange Difference Profit US \$ 13,000x(79-78.30)		9,100

For the year ended 31st March, 2022 exchange difference loss amounting ₹ 52,000 will be charged to statement of Profit & Loss A/c.

However, there is exchange difference gain of ₹ 13,000 x (79-78.30) = 9,100 on 1st May, 2022. Thus, gain of ₹ 9,100 will be credited to statement of Profit & Loss A/c for the year ended 31st March, 2023.





Student Notes:-

