AS-11 :- Foreign Currency Transaction

→ **Foreign Country Transaction**

USA ← INR Rupees → India

↓

Transaction

↓

Foreign Currency Involved → ✗

↓

Exchange Difference ✗

↓

AS-11 ✗

→ **Foreign Currency Transaction**

USA/India ← $ Foreign currency → India

↓

Location not material → ✗

Exchange Diff → ✓

↓

AS-11 → ✓

Foreign currency :-

AS – Indian Company → Financial Statements → Indian Rupees → Reporting Currency

↓

Any other currency

↓

Foreign currency

1. Foreign Currency Transactions

   ↳ Applicability of Para 46 and Para 46A.

2. Translation of Financial Statement of foreign operations → Branch A/c's

   ↓

   Foreign Branch

3. Forward Exchange Contract.

Foreign Currency Transaction

1) Goods purchase (on credit)

   31.5.20

   $ 100000

   Exchange Rate = 75

Financial Year Ending 31.3.21

↓

Amount is still outstanding

↓

Creditor settled on 31.5.21

Payment = $ 100000

↓

Initial Recognition

100000 x 75
= 7500000

Exchange Rate on the date of transaction

Spot Rate

Journal Entry

Purchase	Dr.	7500000
To, Creditor		7500000

Balance Sheet

Creditor

$ 100000

Exchange Rate on B/s Date
1 $ = 81

Reporting on B/s Date
= 100000 x 81
= 8100000

Exchange Rate on B/s Date
= Closing Rate

Journal Entry

P&L	Dr.	600000
To, Creditor		600000

Exchange Difference

Exchange loss

Exchange Rate = 1$ = 79

= ₹ 7900000

Journal Entry

Creditor	8100000
To, P&L a/c	200000
To, Bank	7900000

Exchange Difference
Exchange Gain

1. Foreign Currency Transaction :- Asset / Liability Arise

Initial Recognition → Exchange Rate on Date of Trans (Spot Rate)

B/s Date : Report → Closing Rate (Monetary Item)

Exchange Difference (Gain / Loss) → P&L a/c

On Settlement

Exchange Difference (Gain / Loss) → P&L a/c

Initial Recognition → Spot Rate

Reporting in B/s

- Monetary → Closing Rate
- Non-mon.
  - HC → HR
  - Rev → ER on DoR

Settlement → Spot Rate

Exchange Diff → P&L

Exchange Diff → P&L

Tata : US $ loan → Foreign currency loan

Example: $1\$ = 41$

B/s Date: $\$1 = 45$

Recession

$$\begin{aligned} ED &= ₹4/\$ \\ &\times 6 \text{ billion } \$ \\ \hline &24\ldots \end{aligned}$$

Foreign currency Loan → Acquisition of a depreciation asset

100

a) LT → FC → MI

Exchange Difference (loss) → Asset cost : Adjust

Exchange Difference → P&L ×

Adjust cost : Depreciate

100 + 10

(Asset Dr.
To Loan)

This is an option.
But once exercised it is irrecovable

b) LT FC MI → Loan taken → purpose is other than a)

Loan given → Exchange Diff → FCMITD a/c

Long Term foreign Currency Monetary Item

For acquisition of a depreciable asset
↓
(foreign currency Loan)
↓
Exchange Diff
- P&L Dr./Cr.
- Adjusted to the cost of asset.
  ↓
  Adjusted Cost will be depreciation over useful life.
  ↓
  This option is irrevocable.

For Any other Purpose
↓
→ Loan Given
→ Loan Taken
↓
Exchange Difference
- P&L Dr./Cr.
- foreign currency Monetary Item Translation Diff. a/c (FCMITD a/c)
  ↓
  Amortise to P&L over the life of LTFCMI.

Translation of Financial Statements of a foreign operation

foreign Operation
↓
financial statements
↓
Trial Balance
↓
$
↓
₹ convert (translate)

foreign operation

Integral Foreign Operation
↓
Trial Balance
↓
foreign Currency → $
↓
Convert into Report. Curr → ₹

(convert to ₹ as if ye aapke khud ke transactions ho.)

Non-Integral Operation
↓
Trial Balance
↓
foreign currency → $
↓
Convert to Indian Rupees

Asset — Liability → Monetary / Non-monetary
Income — Expense → Average Rate

Monetary → Closing Rate

Non-monetary → Historical Cost → Historical Rate
Non-monetary → Revalue → Exchange Rate on Date of Rev.

Depreciation (exp) → Historical Rate

Opening Stock → Exchange Rate on opening Date

H/O → Foreign Operation : balances between the two : → Actual figures will be considered.

Foreign Operation's Trial Balance

Particulars	Dr.	Cr.	
	$	$	
1. Asset : M → CR	x	→	₹
Liab. NM : HC x HR			₹
Rev x DOR			₹
Depn x HR			₹
Incomes & Exp AR			
Opening Stock OR	$		₹
		$	
Amount payable to UCA India		xxx	→ Use the
Goods purchased from H/O	xxx		actual ₹ fig. ↓ no need to convert.
	2cr.	1.5	
		0.5	

Difference arising on Translation will be recognised in P&L.

Asset — Liability → Closing Rate
Income — Expense → Average Rate

Opening Stock → Exchange Rate on opening Date

H/O → Foreign Operation : balances between the two : → Actual figures will be considered.

Translation Difference is not transferred to P&L immediately. This will be accumulated in Foreign Currency Translation Reserve (FCTR) a/c. On disposal the balance of FCTR will be transferred to P&L a/c.

Integral /Non-Integral

Contingent liability → Closing Rate.

Reclassification of Foreign Operation

Integral FO → Non-Integral FO

Assets — Liabilities → Monetary / Non-monetary
Income — Expense → Average Rate

Closing Rate

HC → HR

RV → DOR

ED

ED

Closing Rate

FCTR a/c

Non-Integral F.O. → Integral F.O.

Assets, Liabilities → Closing Rate

Income, Expense → Average Rate

Monetary → Closing Rate

Non-Monetary → HC ✓ → HR; Rev. → DOR

The closing value (PPE $ × CR) on the date of such reclassification

Exchange difference accumulated in FCTR will be retained in FCTR only. Only on disposal of such operation will such FCTR be recognised in P&L.

Forward Exchange Contracts

US loan : $ 1,00,000

ER : 1$ = ₹ 50

70 = 70,00,000

Risk Exposure :- Hedge : minimise

Bank → Contract

1$ = 50

after 6m

1$ = 60

Tejas will buy $ from bank after 6m @ ₹53/$

Date fix, Rate fix

"Risk Hedge"

Hedging Purpose | Speculation Purpose

foreign currency Transaction

1. Exposure : 1\$ = 45 (Loan taken)
2. forward Cont : 1\$ = 47
3. Premium 1\$ = 2

Total premium = 100000 x 2
= 200000

↓

Recognise over the term of contract

1·2·22 | 31·3·22 | 30·4·22

1. Exp = 45
2. FC = 47 (3months) .... 48 .... 47·5
P = 2 | P = 1 | L = 0·5

\$ = 100000 | 100000 | 100000
200000 | 100000 → P&L Cr. | 50000 → P&L Dr.

21-22 | 22-23

200000 x 2/3
= 133333

200000 x 1/3
= 66667

1. Premium / Discount
2. Exchange Gain/Loss

foreign currency Transaction → x

1. Exposure : x
2. forward Cont : 1\$ = 47
3. Premium / D 1\$ = x

1·2·22 | 31·3·22 | 30·4·

1. Exp = x
2. FC = 47 .... 48 49
3. P/D = x

P = 1
↓
100000
₹100000
↓
P&L Cr.

P = 1
100000
₹100000
↓
P&L Cr.

STUDENT NOTES

Monetary Items & Non-Monetary Items

Monetary Items :

1. Cash & Cash Equivalent
2. Assets Receivables in Money.
3. Liability Payable in Money.

Non-Monetary Items :-

Assets & Liabilities that are not monetary.

→ Debtor :- Monetary ✓

→ Land :-Non- Monetary ✗

→ Stock:- Non- Monetary ✗

→ Creditor:- Monetary ✓

→ Bank Loan :- Monetary ✓

→ Debentures :- Monetary ✓

→ Fully Conv. Deb :- Non- Monetary ✓

→ Red. Preference Shares :- Monetary ✓

→ Equity Share Capital :-Non- Monetary ✗

→ Investment in Debentures :- Monetary ✓

→ Investment in Equity Shares :- Non-Monetary ✗

monetary items

money receivable → Debtors / BR

money payable

Assets → Report on B/S → ER : B/S Date → Closing Rate

non monetary → Land / Stock

Reporting in B/S

Historical Cost → Land / Building → Historical Rate → Exchange Rate on the date of Trans.

Revalue → Stock → Exchange Rate on date of revaluation

→ monetary item → closing rate

non-monetary item → historical cost

• historical rate

→ Revalue

• ER on DoR

1.1 31.3 7.7

75 (74) (73)

Creditor = 75 -1 -1

P=1 P=1

Solution

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

Illustration 2

IR To, C P M 15000 x 75 Rep B/s : CE → Creditor Dr. 15000×1 To, P&L 15000×1

	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 11.

Solution

As per AS 11 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.

Illustration 3

Kalim Ltd. borrowed US$ 4,50,000 on 01/01/20X1, which will be repaid as on 31/07/20X1. Kalim Ltd. prepares financial statement ending on 31/03/20X1. Rate of exchange between reporting currency (INR) and foreign currency (USD) on different dates are as under:

01/01/20X1 1 US$ = ₹ 48.00

31/03/20X1 1 US$ = ₹ 49.00

31/07/20X1 1 US$ = ₹ 49.50

Solution

Journal Entries in the Books of Kalim Ltd.

Date	Particulars	₹ (Dr.)	₹ (Cr.)
20X1		216,00,000	
Jan. 01	Bank Account (4,50,000 x 48) Dr.		
	To Foreign Loan Account		216,00,000
March 31	Foreign Exchange Difference Account Dr.	4,50,000	
	To Foreign Loan Account P&L		4,50,000
	[4,50,000 x (49-48)]		
July 01	Foreign Exchange Difference Account Dr. [4,50,000 x (49.5-49)] P&L 450000 x 0.5	2,25,000	
	Foreign Loan Account "450000x49" Dr.	220,50,000	
	To Bank Account $\boxed{450000 \times 49.5}$		2,22,75,000

3.9 CHANGE IN THE CLASSIFICATION OF A FOREIGN OPERATION

When a foreign operation that is integral to the operations of the reporting enterprise is reclassified as a non-integral foreign operation, exchange differences arising on the translation of non-monetary assets at the date of the reclassification are accumulated in a foreign currency translation reserve.

NIO → Exchange Diff → Accumulate → FCTR a/c → retain in FCTR only
Recognise in P&L only on disposal
NM : PPE XCR = Value (Translated amount)

When a non-integral foreign operation is reclassified as an integral foreign operation, the translated amounts for non-monetary items at the date of the change are treated as the historical cost for those items in the period of change and subsequent periods. Exchange differences which have been deferred are not recognised as income or expenses until the disposal of the operation.

3.10 TAX EFFECTS OF EXCHANGE DIFFERENCES

Gains and losses on foreign currency transactions and exchange differences arising on the translation of the financial statements of foreign operations may have associated tax effects which are accounted for in accordance with AS 22.

3.11 FORWARD EXCHANGE CONTRACT

An enterprise may enter into a forward exchange contract or another financial instrument that is in substance a forward exchange contract, which is not intended for trading or speculation purposes, to establish the amount of the reporting currency required or available at the settlement date of a transaction. 1. The premium or discount arising at the inception of such a forward exchange contract should be amortised as expense or income over the life of the contract.

2. Exchange differences on such a contract should be recognised in the statement of profit and loss in the reporting period in which the exchange rates change. Any profit or loss arising on cancellation or renewal of such a forward exchange contract should be recognised as income or as expense for the period.

Illustration 4

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.?

1. Exp : 48.85
2. FC = 49.15
P = 0.30
$ = 100000
= 30000

2m 1m
1·2 31·3 30·4
30000 x 2/3 = 20000
30000 x 1/3 = 10000

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.

1. Exp = X
2. FC = 49·15
P/D = X

Illustration 5

→ speculation

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

1. Exp = X
2. FC = 47·10
3. P/D = X
P 0·05 x 100000 = 5000
31·12 47·15

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	₹ 47.18
Less: Contract Rate	(₹ 47.10)
Premium on Contract	₹ 0.08
Contract Amount	US$ 1,00,000
Total Profit (1,00,000 x 0.08)	₹ 8,000

1·12 31·12 31·1
Exp X
FC 47·10 0·05 47·15 0·03 47·18

P/D x 100000 $\boxed{5000}$ 100000 $\boxed{3000}$

Illustration 6

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 date 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 realizable value is translated applying exchange rate when realizable 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'.

When the reporting currency is different from the currency of the country in which the enterprise is domiciled, the reason for using a different currency should be disclosed. The reason for any change in the reporting currency should also be disclosed.

When there is a change in the classification of a significant foreign operation, an enterprise should disclose:

(a) The nature of the change in classification;

(b) The reason for the change;

(c) The impact of the change in classification on shareholders' funds; and

(d) The impact on net profit or loss for each prior period presented had the change in classification occurred at the beginning of the earliest period presented.

3.13 PRESENTATION OF FOREIGN CURRENCY MONETARY ITEM TRANSLATION DIFFERENCE ACCOUNT (FCMITDA)

In the format of Schedule III to the Companies Act, 2013, no line item has been specified for the presentation of "Foreign Currency Monetary Item Translation Difference Account (FCMITDA)". Since the balance in FCMITDA represents foreign currency translation loss, it does not meet the above definition of 'asset' as it is neither a resource nor any future economic benefit would flow to the entity therefrom. Therefore, such balance cannot be reflected as an asset. Therefore, debit or credit balance in FCMITDA should be shown on the "Equity and Liabilities" side of the balance sheet under the head 'Reserves and Surplus' as a separate line item.

LT FC MI → acq of dep Asset
↳ ED : — adjust.

Illustration 8

A Ltd. purchased fixed assets costing ₹ 3,000 lakhs on 1.1.20X1 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal instalments. Exchange rates were 1 Dollar = ₹ 40.00 and ₹ 42.50 as on 1.1.20X1 and 31.12.20X1 respectively. First instalment was paid on 31.12.20X1. The entire difference in foreign exchange has been capitalised. → asset cost +

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

Loan in \$ = $\frac{3000}{40}$ = 75lakh \$

75 lakh (42.5 - 40) = $\boxed{187.5}$

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 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:

$$\text{Foreign currency loan} = \frac{₹\ 3{,}000\ \text{lakhs}}{₹\ 40} = 75\ \text{lakhs US Dollars}$$

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

→ asset cost

Therefore, entire loss due to exchange differences amounting ₹ 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.

Illustration 9

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

} x10000 = 30000 → P&L Dr.

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. 30000 + Asset cost

(iii) The loan was taken to $\boxed{\text{finance the operations of the entity}}$ (and not to procure a depreciable asset). → $\boxed{30000}$ → FCMITD a/c : R&S ←

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

Dr.   amortise to P&L over the life/term of loan

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	Asset → record 10000×48		4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹ 51)		25,500	
	To Bank Account	↳ year end.		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)		25,500	
	To Bank Account			25,500
Mar 31	~~Foreign Exchange Difference Account~~	Dr.	30,000	
	To Foreign Loan Account [10,000 x (51-48)]			30,000
Mar 31	Property, Plant and Equipment	Dr.	30,000	
	To ~~Foreign Exchange Difference Account~~			30,000

TEST YOUR KNOWLEDGE

Multiple Choice Questions

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*

Theoretical Questions

6. *Explain "monetary item" as per Accounting Standard 11. How are foreign currency monetary items to be recognized at each Balance Sheet date?*

7. *Distinguish Non-Integral Foreign Operation (NFO) with Integral Foreign Operation (IFO) as per AS 11.*

Scenario based Questions

8. *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.

ANSWERS/SOLUTION

Answer to the Multiple Choice Questions

1.	(c)	**2.**	(b)	**3.**	(c)	**4.**	(a)	**5.**	(c)		