



10

MULTINATIONAL OPERATIONS

1. Which of the following general statements is most accurate with respect to the current rate method? Revenues:
 - (A) and operating expenses are translated at the average rate.
 - (B) and operating expenses are translated at the current rate.
 - (C) are translated at the average rate while operating expenses are translated at the current rate.

2. Regarding the different methods of consolidating foreign subsidiaries' operating results, it would be most accurate to state that:
 - (A) under the current rate method, individual components of stockholder's equity are translated at the current exchange rates.
 - (B) under the current rate method, revenues and expenses are translated at the exchange rate that existed when the underlying transaction occurred.
 - (C) under the temporal method, monetary assets and monetary liabilities are translated at a historical exchange rate.

3. The nation of Deadoa is experiencing hyperinflation. A subsidiary of a multinational operating in Deadoa will notice changes in its purchasing power and in its financial results as reported on its parent company's financial statements. Which of the following best describes the situation for a subsidiary operating in Deadoa? Purchasing power will:
 - (A) dramatically appreciate and the local currency will be rapidly appreciating against the presentation currency.
 - (B) quickly deteriorate and the local currency will be rapidly appreciating against the presentation currency.
 - (C) quickly deteriorate and the local currency will be rapidly depreciating against the presentation currency.

4. Which of the following measures is unaffected by the choice between translation under the current rate method and remeasurement under the temporal method?
 - (A) Equity
 - (B) Tax expense
 - (C) Cost of good sold

5. The Herlitzka Company, a U.S. multinational firm, has a 100% stake in a Swiss subsidiary. The Swiss franc (SF) has been determined to be the functional currency. All the common stock of the subsidiary was issued at the beginning of the year and the subsidiary uses the FIFO inventory cost-flow assumption. In addition, the value of the SF is as follows:

Beginning of Year	\$0.5902
Average throughout the year	\$0.6002
End of year	\$0.6150

The SF-based balance sheet and income statement data for the Swiss subsidiary are as follows:

Accounts receivable	=	3,000
Inventory	=	4,000
Fixed assets	=	12,000
Accounts payable	=	2,000
Long-term debt	=	5,000
Common stock	=	10,000
Retained earnings	=	2,000
Net income	=	2,000

The translated value of common stock and long-term debt respectively are:

- (A) \$5,902 and \$3,001.
(B) \$6,150 and \$3,075.
(C) \$5,902 and \$3,075.

6. (Assume U.S. GAAP for this question.) For a subsidiary in a hyperinflationary economy, the functional currency should be the:
- (A) Subsidiary's operating currency.
(B) Local currency.
(C) Parent's currency.
7. The U.S. dollar (i.e., the reporting currency) has been depreciating relative to the local currency over the past year. The use of the current rate method to translate a foreign subsidiary's financial statements to U.S. dollars will most likely have which of the following effects on return on equity (ROE) based on ending equity relative to what the ratio would have been without the effects of translation?
- (A) ROE will most likely decline.
(B) The impact of the depreciation of the US dollar on ROE is indeterminate.
(C) ROE will most likely rise.
8. Hann Company is a U.S. multinational firm with operations in several foreign countries. Hann has a 100 percent stake in a French subsidiary. The foreign subsidiary's local currency has

appreciated against the U.S. dollar over the latest financial statement reporting period. In addition, the French firm accounts for inventories using the FIFO inventory cost-flow assumption. The net profit margin as computed under the current rate method would most likely be:

- (A) higher than the same ratio computed under the temporal method.
- (B) either higher or lower than the same ratio computed under the temporal method.
- (C) lower than the same ratio computed under the temporal method.

9. Dave Iverson, CFA, is analyzing the recently released financial statement of Global Corp., a large multinational manufacturing company with production facilities across Europe and Southeast Asia. The company's choice of functional currency is not disclosed, but Iverson does notice that Global Corp. does not have any cumulative translation adjustments (CTA) on its balance sheet. Which of the following statements is most accurate based upon Iverson's observation?

- (A) The temporal method of foreign currency translation is used exclusively.
- (B) The temporal method of foreign currency translation is used for at least some of its subsidiaries.
- (C) The current rate method of foreign currency translation is used exclusively.

10. The Schuldes Company had the following reported assets in euros at historical cost for the period ending December 31, 2005.

Cash	134
Accounts receivable	270
Inventory	404
Net fixed assets	1347
Total assets	2155

The exchange rate per euro was \$0.8734 on January 1, 2005 and \$0.9896 on December 31, 2005.

The average exchange rate for the year 2005 was \$0.8925. The total assets of Schuldes using the current rate method are:

- (A) \$2,178.
- (B) \$2,133.
- (C) \$1,923.

11. An important distinction between the temporal method and the current rate method is that:

- (A) monetary assets and liabilities are remeasured (temporal method) at historical rates but translated (current rate method) at current rates.

- (B) depreciation and cost of goods sold (COGS) are a function of the current rate under translation (current rate method), but a function of the average rate under remeasurement (temporal method).
- (C) the current rate method results in an adjustment to the equity account on the balance sheet. The temporal method results in a gain or loss appearing on the income statement.
12. Gortal Inc., a U.S. company has a wholly owned subsidiary, Fortina GmbH, based in Germany. The U.S. dollar has been appreciating relative to the Euro over the past year. The use of the temporal method to translate a foreign subsidiary's financial statements to U.S. dollars will most likely have which of the following effects on the fixed-asset turnover ratio (S/FA) relative to what the ratio would have been without the effects of translation assuming no new fixed assets were purchased throughout the year?
- (A) The ratio will be higher.
- (B) The ratio will be lower.
- (C) There will be no effect on the ratio.
13. Which translation method should be used under a hyperinflationary economy when using U.S. GAAP?
- (A) All-current, because dividends are translated at the rate that applied when they were issued.
- (B) Monetary/non-monetary, because all monetary accounts are translated at the historical rate.
- (C) Temporal, because all non-monetary accounts are re-measured at the historical rate.
14. At what exchange rate are revenues and accounts receivable translated under the current rate method?
- | Revenues | Accounts receivable |
|------------------|----------------------------|
| (A) Current rate | Current rate |
| (B) Average rate | Historical rate |
| (C) Average rate | Current rate |
15. A Canadian firm owns a foreign subsidiary in the U.S. In 2002, sales were USD1,000,000 and the USD/CAD exchange rate was 0.6329. In 2003, sales were also USD1,000,000 but the exchange rate was 0.7484. What is the impact of the change in the value of the CAD on the parent company's translated sales? Sales will:
- (A) decrease by 18%.
- (B) increase by 18%.

- (C) decline by 15%.
16. A hyperinflationary economy is typically defined as one that has:
- (A) cumulative inflation that exceeds 100% over a twelve-year period.
 - (B) an inflation rate that exceeds 10% per year for three consecutive years.
 - (C) cumulative inflation that exceeds 100% over a three-year period.
17. Which of the following statements is least accurate regarding the use of the temporal method for foreign exchange accounting?
- (A) All monetary assets are translated at the current rate of exchange.
 - (B) Under the temporal method, the foreign exchange gain or loss is placed on the balance sheet in the equity section.
 - (C) All nonmonetary assets and liabilities are translated at the historical rate of exchange.
18. Which of the following ratios is unaffected by the choice between the current rate method and the temporal method?
- (A) Quick ratio.
 - (B) Inventory turnover.
 - (C) Current ratio.
19. Which of the following currency translation methods is most appropriate in a hyperinflationary economy under US GAAP? The:
- (A) temporal method because all non-monetary accounts are translated at the historical rate.
 - (B) current rate method since the translation gain or loss is shown on the income statement.
 - (C) current/non-current method since current assets and liabilities are translated at the current exchange rate.
20. Which of the following subsidiary ratios will be affected by the translation adjustment under the current rate method?
- (A) Gross margin.
 - (B) Return on equity.
 - (C) Net profit margin.
21. Which of the following statements regarding the functional currency is least accurate? The functional currency:
- (A) is the currency of the primary economic environment in which the foreign subsidiary generates and expends cash.
 - (B) is determined by management.
 - (C) is remeasured into the reporting currency under the temporal method.

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22. Where does the currency translation gain or loss appear in the financial statements under the temporal method and the current rate method?

Temporal method

Current rate method

- | | |
|----------------------|------------------|
| (A) Income statement | Balance sheet |
| (B) Balance sheet | Balance sheet |
| (C) Balance sheet | Income statement |

23. Sycamore Systems sold \$5 million worth of software on December 1, 20X1 to a Japanese company with payment denominated in Japanese yen to be received in two months. Sycamore's year end is 31st December. Payment was received on 31 Jan 20X2.

Exchange rates	(1 USD)
1 Dec 20X1	95
31 Dec 20X1	90
31 Jan 20X2	35

The amount of transaction gain/loss recorded by Sycamore on its income statement for the year ending 31 Dec 20X1 is closest to:

- (A) loss of \$300,000.
(B) gain of \$580,000.
(C) gain of \$280,000.

24. Which of the following statements regarding the foreign currency translation under US GAAP is least accurate? The functional currency is the:

- (A) parent firm's home currency if the foreign subsidiary operates in a country with high inflation.
(B) subsidiary's local currency for self-contained, independent foreign subsidiaries.
(C) parent firm's home currency for self-contained independent foreign subsidiaries.

25. Under U.S. GAAP, the temporal method is preferred to the current rate method in hyperinflationary economies because the temporal method:

- (A) provides better conversions of subsidiary revenues.
(B) is easier to perform under hyperinflation.
(C) results in non-monetary asset values that are a better proxy for the economic values of those assets.

26. Which of the following general statements is CORRECT with respect to the temporal method? Revenues and operating expenses (excluding COGS) are translated at the:

- (A) average rate.
(B) current rate.
(C) historical rate.

27. Which of the following general statements is most accurate with respect to the temporal

method?

Nonmonetary assets are translated at:

- (A) historical rates at the time of the transaction.
- (B) the average rate during the year.
- (C) the current rate.

28. Under the temporal method, the inventory and cost of goods sold (COGS) accounts are both nonmonetary accounts. Which of the following statements is least accurate regarding these accounts?

- (A) The Inventory account is remeasured using the historical rate under both LIFO and FIFO.
- (B) If the firm accounts for inventory using last in, first out (LIFO), then the beginning-of-period rate is used to remeasure COGS.
- (C) If the firm accounts for inventory using first in, first out (FIFO), then a more recent rate will be applied to the inventory account

Deborah Ortiz, CFA®, is the director of Global Research for F.E. Horton & Co. Ortiz recently hired two junior analysts, Tina Hirauye and Dominique Wilkins to assist in the financial statement analysis of global conglomerates. Hirauye and Wilkins are both Level II candidates in the CFA® Program, so Ortiz thought they would be the ideal people to work on a project dealing with consolidating the results of foreign operating units in the financial statements of the global parent.

Before starting on the project, Ortiz has a meeting with Hirauye and Wilkins to discuss the use of different currencies in a company's operations. At the meeting, Hirauye states that when analyzing multinational firms, there cannot be a difference between local and functional currencies. Wilkins disagrees with her and states that there can be a difference between local and functional currencies, but only if the parent of the subsidiary operates in a hyperinflationary environment. After another 30 minutes of discussion, Ortiz concludes the meeting by telling them to make sure they understand the different accounting rules for remeasurement and translation, under SFAS 52.

Hirauye and Wilkins are given projects involving two different firms:

- Molsan Industries is a Canadian multinational firm with a subsidiary in Japan. The subsidiary has operations in both Japan and Singapore.
- Neslarone is based in Switzerland and generates the majority of its cash in Swiss Francs (CHF). The firm issues and prepares its consolidated financial statements in U.S. dollars.

Hirauye and Wilkins spend the morning reviewing the details of their assignment and decide to take a break for lunch at a restaurant across the street from F.E. Horton & Co.'s headquarters. They agree that they have a challenging task and both are nervous about turning in their consolidated financial statements to Ortiz on the following day.

29. Regarding the statements made at the meeting:
- (A) Hirauye's statement is incorrect; Wilkins' statement is correct.
 - (B) Hirauye's statement is incorrect; Wilkins' statement is incorrect.
 - (C) Hirauye's statement is correct; Wilkins' statement is correct.
30. Hirauye is working on consolidating the financial statements of Molsan Industries' Japanese subsidiary. Under SFAS 52, regarding Foreign Currency Translation, if:
- (A) more than half of the subsidiary's revenue is from Japanese sources, then the results of the Singapore operation are translated into Japanese yen and then translated into Canadian dollars.
 - (B) management determines that the subsidiary's functional currency is the Japanese yen, the results of the Singapore operation are first remeasured into Japanese yen and then translated into Canadian dollars.
 - (C) management determines that the subsidiary's functional currency is the Singapore dollar, then the results of the Singapore operation are remeasured into Canadian dollars.
31. Ortiz had told the junior analysts to make sure they understand the different accounting rules under SFAS 52. When referring to foreign exchange rates, the difference between remeasurement and translation is that remeasurement:
- (A) refers to the conversion of local currency into the functional currency; translation is the conversion of the functional currency into the reporting currency.
 - (B) and translation refer to the same process of translating the functional currency into the reporting currency.
 - (C) is used to describe historical exchange rates while translation is used for current rates.
32. Wilkins and Hirauye are working on constructing the consolidated statements for Neslarone. They know that after they convert from Swiss Francs (CHF) to U.S. dollars (USD), they will be left with a foreign currency adjustment that needs to be included on the financial statements. To convert from CHF to USD, the analysts should use the:
- (A) current rate method and they should record the foreign currency adjustment on the balance sheet.
 - (B) current rate method and they should record the foreign currency adjustment on the income statement.
 - (C) temporal method and they should record the foreign currency adjustment on the income statement.
33. In reality, what best describes the real value of non-monetary assets and liabilities in a hyperinflationary environment?
- (A) Typically not affected because their local currency-denominated values decrease to offset the impact of inflation.
 - (B) All non-monetary accounts are re-measured at the current rate.

- (C) Typically not affected because their local currency-denominated values increase to offset the impact of inflation.
34. In a hyperinflationary economy, translation under the current rate method will most likely result in relatively:
- (A) high balance sheet values for long term assets.
(B) high translation gains.
(C) low balance sheet values for long term liabilities.
35. Which of the following situations does NOT require the use of the temporal method? The:
- (A) functional currency is some currency other than the local currency or the U.S. dollar.
(B) local currency is the functional currency.
(C) foreign subsidiary is operating in a highly inflationary economy.
36. The Herlitzka Company, a U.S. multinational firm, has a 100 percent stake in a Swiss subsidiary. The U.S. dollar (USD) has been determined to be the functional currency. All the common stock of the subsidiary was issued at the beginning of the year and the subsidiary uses the weighted-average inventory cost-flow assumption. In addition, the value of the SF is as follows:

Beginning of year	\$0.5902
Average throughout the year	\$0.6002
End of year	\$0.6150

The SF-based balance sheet and income statement data for the Swiss subsidiary are as follows:

Accounts receivable	=	3,000
Inventory	=	4,000
Fixed assets	=	12,000
Accounts payable	=	2,000
Long-term debt	=	5,000
Common stock	=	10,000
Retained earnings	=	2,000
Net income	=	2,000

The remeasured value of accounts receivable and inventory respectively are closest to:

- (A) \$1,845 and \$2,401.
(B) \$1,845 and \$2,361.
(C) \$1,771 and \$2,361.
37. Which of the following statements regarding the translation of a foreign subsidiary into the reporting currency is most accurate?
- (A) If the reporting currency is the functional currency, the temporal method is applied and exposure is equal to net monetary assets.

- (B) A multinational firm with small liability balances generally has minimal foreign currency exposure on its balance sheet.
- (C) If the functional currency is equal to the local currency, exchange gains and losses on translation will be recognized in the income statement.

38. The U.S. Deter Company operates a subsidiary in the UK, and the functional currency is the British pound. The subsidiary's 2001 income statement shows £500 of net income and a £50 dividend that was paid on December 31, when the exchange rate was \$1.50 per pound. The current exchange rate is \$1.65 per pound, and the average rate is \$1.58 per pound. What is the change in retained earnings for the period in U.S. dollars under U.S. GAAP?

- (A) \$715.
- (B) \$750.
- (C) \$725.

The Precision Screen Printers (PSP) Company has a foreign subsidiary, the Acer Tool & Die Company, located in the country of Rolivia. The currency of Rolivia is the Chad. The balance sheet and income statement of Acer Tool & Die Company for the year-ended December 31, 2005, is shown below. The balance sheet has been restated using the U.S.

Acer Tool & Die Company Balance Sheet As of December 31, 2005

	Chad (millions)	Exchange Rate (Chad/US\$)	U.S. \$ (millions)
Cash	20	0.25	\$80
Accounts receivable	30	0.25	120
Inventory	100	0.3125	320
Fixed assets (net)	500	0.3333	1,500
Total assets	650		\$2,020
Accounts payable	50	0.25	\$200
Capital stock	380	0.3333	1,140
Retained earnings	220	-	680
Total liabilities and equity	650		\$2,020

Acer Tool & Die Company Income Statement

For year ending December 31, 2005

(Amounts in millions of Chad)

Revenues	1,000
Cost of sales	700
Depreciation expense	50
Selling expense	30
Translation gain (or loss)	
Net income	220

Acer has determined that the exchange rate exposure at the beginning of 2005 is –260 Chad.

The exchange rate at the beginning of 2005 was 0.3333 Chad/US\$ and that is the historical rate applicable to beginning inventory of 90 Chad. The exchange rate at the end of 2005 was 0.25 Chad/US\$. The average rate for 2005 is 0.3125 Chad/US\$. Purchases occurred evenly throughout the year. Acer Tool & Die uses FIFO inventory valuation and depreciates fixed assets using the straight-line method. Assume that retained earnings at year end 2004 were zero, the historical exchange rate for depreciation is 0.333, and no dividends were paid during 2005.

39. What is Acer Tool & Die's cost of sales in U.S. dollars using the temporal method?
- (A) \$2,222.00
 (B) \$2,242.00
 (C) \$2,240.00
40. What is the remeasurement gain or loss for the period using the temporal method?
- (A) \$50 gain.
 (B) \$52 loss.
 (C) \$32 loss.
41. The local currency is:
- (A) the preferred functional currency for subsidiaries that are highly integrated with the parent.
 (B) translated into the functional currency under the current rate method.
 (C) the same as the functional currency under the current rate method.

South Seas Inc, a subsidiary of Seven Seas Inc., reported its most recent performance in its local currency (LC) which is the functional currency. The reporting currency of Seven Seas is the U.S. dollar (USD). South Seas also paid a dividend of 16,000LC at year end, at which time the exchange rate was 2 LC/USD. Last year, Seven Seas reported balance sheet retained earnings of 90,000 USD for its South Seas subsidiary.

Rates	LC/US\$
Current rate	2.00
Average rate	2.20
Historical rate for common stock	2.50
Historical rate for COGS	2.30
Historical rate for depreciation	2.10
Historical rate for ending inventory	2.30
Historical rate for fixed assets	2.10

	LC
Revenues	520,000
Cost of Goods Sold (COGS)	225,000
SG & A	100,000
Depreciation	80,000
Income Taxes	46,000
Net Income	69,000

The balance sheet for South Seas is given below.

	LC
Cash	25,000
Accounts Receivable	30,000
Inventory	35,000
Net Fixed Assets	500,000
Total Assets	590,000
Accounts Payable	20,000
Long term debt	100,000
Common Stock	250,000
Retained Earnings	220,000
Total Liabilities & Equity	590,000

42. What is the amount of income Seven Seas should report from its South Seas subsidiary?
- (A) 34,500 USD.
 (B) 31,400 USD.
 (C) 27,600 USD.
43. The currency translation adjustment that results from the translation of South Sea's data is closest to?
- (A) Zero because there is no currency translation adjustment under the current rate method.
 (B) -3,300 USD.
 (C) 21,600 USD.
44. If the temporal method is used, the retaining earnings is closest to:
- (A) 21,600 USD.
 (B) 120,800 USD.

(C) 90,000 USD.

45. If the functional currency is the USD, then the net income before a translation gain/loss is closest to:
- (A) 8,000 USD.
(B) 4,700 USD.
(C) 34,100 USD.
46. Which of the following statements regarding foreign currency translation are least accurate? Under the:
- (A) temporal method, sales are remeasured using the average rate.
(B) temporal method, COGS and depreciation are remeasured using the historical rate.
(C) current rate method, the foreign currency translation gain or loss appears on the parent firm's income statement.
47. Each of the following items is considered a monetary asset or liability account under the temporal method for foreign currency translation EXCEPT:
- (A) long-term debt.
(B) accounts payable.
(C) inventory.

Wasson Brothers (WB) is a large U.S. based conglomerate with many subsidiaries in both the U.S. and abroad. One of WB's wholly-owned foreign subsidiaries, Kasamatsu Industries, is based in Japan and manufactures a hugely successful line of trading cards, toys, and other related products. All of Kasamatsu's operations and sales take place in Japan, and the corresponding transactions are denominated in Japanese yen. Additionally, Kasamatsu's books and records are all maintained in yen. WB reports its earnings in U.S. dollars. The history of the exchange rate between the dollar and the yen over the last two years is presented in the following table. Figures are presented in Yen/dollars.

Yen/Dollar Exchange Rate	
December 31, 2005	150
December 31, 2004	130
2005 Average	140
2004 Average	120
Exchange rate on date that 2005 dividends were declared by Kasmatsu	145
Exchange rate on date of stock issue and acquisition of fixed assets.	100

Ashley Jameson is an analyst with Henderson-Wells, an investment banking firm in New York, and is the chief analyst covering WB. She believes that the enormous success of the trading cards has contributed greatly to WB's bottom line. However, she

believes that this effect may be misstated in the company's financial statements because of the recent volatility in exchange rates. Many analysts at other major investment banking firms have been raising their ratings on WB because of the recent earnings growth. Jameson, however, wants to be absolutely certain that these results are accurate and fully attributable to Kasamatsu's hot new product and not a result of an exchange rate fluctuation. The following are the financial statements of Kasamatsu, stated in thousands of yen.

Financial statements for Year Ending December 31, 2005 (in thousands of yen) Statement of Income and Retained Earnings	
Sales	700,000
Expenses	
Cost of Goods Sold (COGS)	280,000
Depreciation	126,000
SG&A	77,000
Total Expenses	483,000
Earnings Before Taxes (EBT)	217,000
Income Tax Expense	98,000
Net Income	119,000
Retained Earnings: December 31, 2004	250,000
	369,000
Dividends	58,000
Retained Earnings: December 31, 2005*	311,000
* Retained earnings on 12/31/2005 were US \$2million	

Balance Sheet	
Assets	
Cash and receivables	60,000
Inventory	180,000
Land	200,000
Fixed assets	346,000
Total assets	786,000
Liabilities and stockholders' equity	
Liabilities	300,000
Capital stock	175,000
Retained earnings	311,000
Total liabilities and stockholders' equity	786,000

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48. Before Jameson can perform any financial statement analysis she needs to determine which method WB uses to translate Kasamatsu's earnings into U.S. dollars (USD). Which of the following is the most appropriate method to use?
- (A) The temporal method.
 - (B) The current rate method.
 - (C) First the temporal method, followed by the current rate method.
49. Jameson must also determine how the fluctuation in the yen vs. the dollar has affected Kasamatsu's earnings in the reporting currency. Which of the following best describes the effect of changes in the yen/dollar rate has had on earnings in the reporting currency? Earnings have:
- (A) decreased because the yen is depreciating versus the USD.
 - (B) increased because the yen is depreciating versus the USD.
 - (C) increased because the yen is depreciating versus the USD.
50. Which of the following general statements is CORRECT with respect to the temporal method? Monetary assets are:
- (A) translated at the average rate.
 - (B) translated at the current rate.
 - (C) not translated.
51. Sopgate is a manufacturer of branded fast moving consumer goods having business operations in 28 countries (in each country, Sopgate has a wholly owned local subsidiary for production and/or distribution). Following information is available from Sopgate's annual report:

Region	Revenue Growth (USD)*	Growth in pre-tax profits (USD)*	Tax rate
Latin America	5%	4%	25%
North America	3%	3%	35%
Europe	2%	-1%	45%
Asia pacific	4%	6%	20%

*Growth rate indicates expected growth rate over the next five years.

Sopgate's effective tax rate is most likely expected to:

- (A) decrease.
- (B) increase.
- (C) remain unchanged.

52. A company is exposed to foreign exchange risk due the impact of changes in currency values on a:
- (A) company's assets only.
 - (B) company's assets, liabilities, and future sales.
 - (C) company's assets and liabilities only.
53. Which of the following statements describing the choice of the functional currency is least accurate? The functional currency should be the same as the parent's reporting currency if the subsidiary is:
- (A) highly integrated with the parent where the local currency, prices, and some costs are controlled or restricted.
 - (B) highly integrated with the parent where the local currency, prices, and some costs are not controlled or restricted.
 - (C) mostly independent from the parent.
54. Hann Company is a U.S. multinational firm with operations in several foreign countries. Hann has a 100% stake in a French subsidiary. The foreign subsidiary's local currency has appreciated against the U.S. dollar over the latest financial statement reporting period. In addition, the French firm accounts for inventories using the first in, first out (FIFO) inventory cost-flow assumption. The gross profit margin as computed under the current rate method would most likely be:
- (A) equal to the gross profit margin as computed under the temporal method.
 - (B) lower than the gross profit margin as computed under the temporal method.
 - (C) higher than the gross profit margin as computed under the temporal method.
55. Which of the following statements is NOT a characteristic of the current rate method of accounting for foreign currency translation?
- (A) Nonmonetary liabilities are translated at the historical rate of exchange.
 - (B) The common stock account is translated at the rate of exchange that applied when the equity was issued.
 - (C) All asset accounts are translated at the current rate of exchange as of the balance sheet date.
56. Which example least accurately describes pure balance sheet and income statement ratios?
- (A) The current ratio is a pure balance sheet ratio.
 - (B) When multiplying both the numerator and denominator by the current exchange rate, the current rate is cancelled.
 - (C) All pure balance sheet ratios are affected by the all-current translation method.

57. The Precision Screen Printers (PSP) Company has a foreign subsidiary, the Acer Tool & Die Company, located in the country of Rolivia. The currency of Rolivia is the Chad. The balance sheet and income statement of Acer Tool & Die Company for the year-ended December 31, 20X2, is shown below. The balance sheet has been restated using the U.S. dollar as the functional currency.

Acer Tool & Die Company Balance Sheet As of December 31, 20X2			
	Chad (millions)	Exchange Rate (Chad/US\$)	U.S. \$ (millions)
Cash	20	0.25	@80
Accounts receivable	30	0.25	120
Inventory	100	0.3125	320
Fixed assets (net)	500	0.3333	1,500
Total assets	650		\$2,020
Accounts payable	50	0.25	\$200
Capital stock	380	0.3333	1,140
Retained earnings	220	-	680
Total liabilities and equity	650		\$2,020

Acer Tool & Die Company Income Statement For year ending December 31, 20X2 (Amounts in millions of Chad)	
Revenues	1,000
Cost of sales	700
Depreciation expense	50
Selling expense	30
Translation gain (or loss)	
Net income	220

The exchange rate at the beginning of 20X2 was 0.3333 Chad/US\$. The exchange rate at the end of 20X2 was 0.25 Chad/US\$. The average rate for 20X2 is 0.3125 Chad/US\$. Beginning inventory is 90 Chad, which was translated to \$270 on the 20X1 balance sheet. Acer Tool & Die uses FIFO inventory valuation and depreciates fixed assets using the straight-line method.

Purchases occurred evenly throughout the year. Assume that retained earnings at year-end 20X1 were zero, the historical exchange rate for depreciation is 0.333, and no dividends were paid during 20X2.

Using the current rate method for the Acer Tool & Die Company, what is the value of total assets after translation?

- (A) \$2,600.
- (B) \$1,950.
- (C) \$2,020.

58. Which of the following statements is most accurate concerning foreign currency translation?

- (A) In the case in which a firm uses first in, first out (FIFO) inventory valuation, if the local currency depreciates the cost of good sold under the temporal method is less than the cost of goods sold using the current rate method.
 - (B) In the case of an appreciating currency, the fixed asset turnover will be lower under the temporal method, as compared to the current rate method.
 - (C) The receivables turnover ratio is identical under both the temporal method and the current rate method.
59. Which of the following statements regarding the effects of translation on financial statement items/ratios is most accurate?
- (A) Leverage is higher under the current rate method as compared to under the local currency.
 - (B) Depreciation in the reporting currency under the current rate method is higher than under the temporal method if the local currency has appreciated.
 - (C) Fixed assets are relatively overstated under the temporal method compared to the local currency if the local currency has appreciated.
60. Which of the following ratios is affected by translation under the current rate method?
- (A) Net profit margin.
 - (B) Debt/Assets ratio.
 - (C) Fixed asset turnover ratio.
61. Under the current rate method, common stock is translated by using the:
- (A) rate that existed when the equity was issued.
 - (B) present value of weighted average rate.
 - (C) exchange rate as of the balance sheet date.
62. Which of the following statements regarding the functional currency under US GAAP is least accurate?
- (A) The functional currency is defined as the primary currency of the economic environment in which the parent firm operates.
 - (B) Self-contained, independent subsidiaries whose operations are primarily located in the local market will use the local currency as the functional currency.
 - (C) If a firm operates in a country or environment which is subject to cumulative inflation of 100% or more over a three year period, that firm will use the parent's currency as the functional currency.
63. The Herlitzka Company, a U.S. multinational firm, has a 100% stake in a Swiss subsidiary. The Swiss franc (SF) has been determined to be the functional currency. All the common stock of

the subsidiary was issued at the beginning of the year and the subsidiary uses the FIFO inventory cost-flow assumption. In addition, the value of the SF is as follows:

Beginning of year	\$0.5902
Average throughout the year	\$0.6002
End of year	\$0.6150

The SF-based balance sheet and income statement data for the Swiss subsidiary are as follows:

Accounts receivable	=	3,000
Inventory	=	4,000
Fixed assets	=	12,000
Accounts payable	=	2,000
Long-term debt	=	5,000
Common stock	=	10,000
Retained earnings	=	2,000
Net income	=	2,000

The translated value of accounts receivable and inventory respectively are:

- (A) \$1,845 and \$2,460.
- (B) \$1,845 and \$2,401.
- (C) \$1,801 and \$2,401.

64. Portinta Inc, a U.S. based pharmaceutical company, has a UK based subsidiary, Medaze plc. The U.S. dollar has been appreciating relative to GBP over the past year. Using the current-rate method to translate a foreign subsidiary's financial statements to U.S. dollars will most likely have which of the following effects on the long-term debt to equity ratio relative to what the ratio would have been without the effects of translation?

- (A) The ratio will be the same.
- (B) The ratio will be higher.
- (C) The ratio will be lower.

65. The Herlitzka Company, a U.S. multinational firm, has a 100% stake in a Swiss subsidiary. The U.S. dollar (USD) has been determined to be the functional currency. All the common stock of the subsidiary was issued at the beginning of the year and the subsidiary uses the weighted-average inventory cost-flow assumption. In addition, the value of the SF is as follows:

Beginning of year	\$0.5902
Average throughout the year	\$0.6002

End of year	\$0.6150
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The SF-based balance sheet and income statement data for the Swiss subsidiary are as follows:

Accounts receivable	=	3,000
Inventory	=	4,000
Fixed assets	=	12,000
Accounts payable	=	2,000
Long-term debt	=	5,000
Common stock	=	10,000
Retained earnings	=	2,000
Net income	=	2,000

The total value of net monetary assets is equal to:

- (A) 12,000 SF.
 (B) -4,000 SF.
 (C) 3,000 SF.

Della Air Lines has recently acquired Australian Puddle Jumpers, Inc. (APJ), a small airline located in Sydney. The Australian dollar has been chosen by Della as the functional currency for APJ. The balance sheet of APJ is given below as of Dec. 31, 2011 in U.S. dollars.

Assets		Liabilities and Equity	
Cash	\$100	Accounts Payable (A/P)	\$90
Accounts Receivable (A/R)	120	Common Stock	360
Maintenance Supplies	90		
Fixed Assets	140		
Total Assets	\$450	Total Liabilities & Equity	\$450

APJ's income statement for the year ending Dec. 31, 2012 is expressed in Australian dollars as:

Sales	3,500
Total Costs	2,900
Net Income	600

The Australian dollar has steadily depreciated against the U.S. dollar. At Dec. 31, 2011, the exchange rate was A\$/US\$ 2.50, the average rate during the year was A\$/US\$ 2.75 and A\$/US\$ 3.0 on Dec. 31, 2012.

The Dec. 31, 2012 Balance Sheet for APJ is given in Australian dollars as follows:

Assets		Liabilities and Equity	
Cash	441	Accounts Payable (A/P)	210
Accounts Receivable (A/R)	330	Common Stock	720
Supplies	291	Retained Earnings	600
Fixed Assets	468		
Total Assets	1,530	Total Liabilities & Equity	1,530

66. On APJ's 2012 income statement, the level of sales in U.S. dollars would be closest to:
- (A) \$1,985.
 (B) \$1,272.
 (C) \$1,377.
67. On APJ's 2012 balance sheet, the level of accounts receivable in U.S. dollars would be closest to:
- (A) \$110.
 (B) \$132.
 (C) \$330.
68. For APJ, the conversion to US\$ is most likely to result in:
- (A) remeasurement gain.
 (B) cumulative translation adjustment loss.
 (C) cumulative translation adjustment gain.
69. If the functional currency is the reporting currency, the exposure and the foreign currency movements are most likely to result in a:
- (A) remeasurement loss.
 (B) cumulative translation adjustment loss.
 (C) remeasurement gain.
70. A U.S. firm owns a foreign subsidiary in France. In 2002, sales were EUR 1,000,000 and the USD/EUR exchange rate was 1.0620. In 2003, sales were EUR 1,100,000 and the exchange rate was 1.1417. What is the impact of the change in the value of the USD on the parent company's translated sales?
- (A) Sales will increase by 7.5%.
 (B) Sales will increase by 18.25%.
 (C) Sales will decrease by 7.5%.
71. Organic growth in sales is most accurately defined as growth in sales excluding the effects of:
- (A) acquisitions/divestitures only.

- (B) acquisitions/divestitures and currency value fluctuations.
 (C) currency value fluctuations.

72. A German company (reporting currency = Euro) owns a foreign subsidiary in the U.S. If the results below are reported in local currency (USD), after translation what is the effect of the change in the exchange rate on revenues? Round to the nearest dollar and/or percent.

Year	Sales	\$ per 1 Euro avg. Exchange Rate
2001	\$10,000	0.9
2002	\$10,000	0.8

- (A) The company shows a 0.1% decline in revenues in 2002.
 (B) The company shows a 12.5% growth in revenues in 2002.
 (C) There is no change in revenue growth between 2001 and 2002.

Wasson Brothers (WB) is a large U.S. based conglomerate with many subsidiaries in both the U.S. and abroad. One of WB's wholly-owned foreign subsidiaries, Kasamatsu Industries, is based in Japan. Kasamatsu manufactures a hugely successful line of trading cards, toys, and related products. All of Kasamatsu's operations and sales take place in Japan, and the corresponding transactions are denominated in Japanese yen. Additionally, Kasamatsu's books and records are all maintained in yen. WB reports its earnings in U.S. dollars. The history of the exchange rate between the dollar and the yen over the last two years is presented in the following table. Figures are presented in yen/\$.

Yen/Dollar Exchange Rate	
December 31, 2013	150
December 31, 2012	130
2013 Average	140
2012 Average	120
Exchange rate on date that 2013 dividends were declared by Kasamatsu	145
Exchange rate on date of stock issue and acquisition of fixed assets.	100

Shelly Jameson is an analyst with Henderson-Wells, an investment banking firm in New York, and is the chief analyst covering WB. She believes that the enormous success of the trading cards has contributed greatly to WB's bottom line. However, Jameson believes that this effect may be overstated in the company's financial statements because of the recent volatility in exchange rates. Many analysts at other investment banking firms have been raising their ratings on WB because of the recent earnings growth. Jameson, however, wants to be absolutely certain that these results are accurate and fully attributable to Kasamatsu's hot new product and not a result of an

exchange rate fluctuation. The following are the financial statements of Kasamatsu, stated in thousands of yen.

Financial Statements for Year Ending December 31, 2013 (in thousands of yen) Statement of Income and Retained Earnings	
Sales	700,000
Expenses	
Cost of Goods Sold (COGS)	280,000
Depreciation	126,000
SG & A	77,000
Total Expenses	483,000
Earnings Before Taxes (EBT)	217,000
Income Tax Expense	98,000
Net Income	119,000
Retained Earnings: December 31, 2012	250,000
	369,000
Dividends	58,000
Retained Earnings: December 31, 2013*	311,000
*Retained earnings on 12/31/2013 were US \$2 million	

Balance Sheet	
Assets	
Cash and receivables	60,000
Inventory	180,000
Land	200,000
Fixed assets	346,000
Total assets	786,000
Liabilities and stockholder's equity	
Liabilities	300,000
Capital Stock	175,000
Retained Earnings	311,000
Total liabilities and stockholders' equity	786,000

73. Jameson would like to examine WB's group accounts. What is the most appropriate exchange rate (yen/\$) to use in translating Kasamatsu's reported dividends into U.S. dollars?

- (A) 150.
- (B) 140.
- (C) 145.

74. If Jameson wishes to convert any of the figures on Kasamatsu's Income Statement from yen to dollars, she should most appropriately use which of the following exchange rates (yen/\$)?
- (A) 140.
 - (B) 145.
 - (C) 150.
75. Before Jameson can perform any financial statement analysis, she wants to determine which method WB uses to translate Kasamatsu's earnings into U.S. dollars (USD). Which of the following is the most accurate translation method and reasoning? WB should translate Kasamatsu's earnings using the:
- (A) current rate method because the local currency is the USD.
 - (B) temporal method because the local currency differs from the functional currency.
 - (C) current rate method because the functional currency is the yen.
76. Which of the following asset or liability values is likely to be the most understated in a hyperinflationary economy if translation occurs under the current rate method?
- (A) Accounts receivable.
 - (B) A plant purchased several years ago.
 - (C) Dividends payable.
77. The U.S. dollar has been depreciating relative to the local currency over the past year. The use of the current rate method to translate a foreign subsidiary's financial statements to U.S. dollars will most likely have which of the following effects on the operating profit margin (EBIT/S) relative to what the ratio would have been without the effects of translation?
- (A) There will be no effect on the ratio.
 - (B) The ratio will rise.
 - (C) The ratio will fall.
78. Which of the following statements concerning the translation of a subsidiary's financial statement and the subsidiary's ratios is least accurate?
- (A) The subsidiary's ratios in the local currency will differ from ratios calculated after translation.
 - (B) The statement of cash flows is not affected by the choice of translation.
 - (C) Ratios calculated under the current rate method will not differ from those calculated under the temporal method.

79. Edmonton Oilfield Supply has made an equipment sale in Venezuela in the amount of VEF 15,000,000. On the day of the sale, the exchange rate is 1.7519 VEF per 1 Canadian dollar. 90 days later, when the Venezuelan firm pays for the equipment, the exchange rate is 1.6326. As a result of the change in the exchange rate, Edmonton will recognize a:
- (A) gain of \$1,096,104.
 - (B) gain of \$625,666.
 - (C) loss of \$1,789,500.
80. Global International Corp. (GIC) has three subsidiaries: GIC Europe whose local currency is the euro and whose functional currency is the euro; GIC China whose local currency is the yuan and whose functional currency is the Hong Kong dollar; and GIC Bahamas whose local currency is the Bahamian dollar and whose functional currency is the U.S. dollar. GIC's reporting currency is the U.S. dollar. Which conversion methods should be used by GIC for each of its subsidiaries?
- (A) GIC Europe's data should be translated under the current rate method; GIC China data should be remeasured under the temporal method into Hong Kong dollars, and then translated under the current rate method into U.S. dollars; and GIC Bahamas data should be remeasured under the temporal method into U.S. dollars.
 - (B) The financial data for all three subsidiaries should be remeasured under the temporal method.
 - (C) GIC Europe's data should be remeasured under the temporal method; GIC China's data should be remeasured under the temporal method into Hong Kong dollars, and then translated under the current rate method into U.S. dollars; and GIC Bahamas' data should be translated under the current rate method into U.S. dollars.
81. Jameson has finally completed translating all the necessary figures into dollars and now wants to compute by how much WB's reported sales in dollars will change due to Kasamatsu's sales. Which of the following is closest to the amount of sales that WB will report as a result of Kasamatsu's to operations (in thousands of dollars)?
- (A) \$4,828.
 - (B) \$5,000.
 - (C) \$4,667.
82. Which of the following statements is least accurate regarding accounting for foreign currency translations? The:
- (A) current rate method applies the current exchange rate to all balance sheet accounts.
 - (B) temporal method uses the historical exchange rate to translate non-monetary assets and liabilities into the currency of the country of the parent company.
 - (C) current rate method applies the average exchange rate to all income statement accounts.



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