Statement of Financial Accounting Standards No. 89

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Financial Reporting and Changing Prices

December 1986

Financial Accounting Standards Board
of the Financial Accounting Foundation
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Statement of Financial Accounting Standards No. 89

Financial Reporting and Changing Prices

December 1986

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Paragraph Numbers

FAS 89: Financial Reporting and Changing Prices

FAS 89 Summary

This Statement supersedes FASB Statement No. 33, *Financial Reporting and Changing Prices*, and its subsequent amendments, and makes voluntary the supplementary disclosure of current cost/constant purchasing power information.

The Statement is effective for financial reports issued after December 2, 1986.

INTRODUCTION AND SCOPE

1. In 1979, FASB Statement No. 33, *Financial Reporting and Changing Prices*, was issued as an experiment in requiring supplementary information on the effects of inflation and changes in specific prices. At that time the Board committed itself to review the results of the requirements within five years. The Board has completed that review and has concluded that further supplementary disclosures should be encouraged, but not required.

2. This Statement supersedes the following pronouncements:

a. FASB Statement No. 33, *Financial Reporting and Changing Prices*
b. FASB Statement No. 39, *Financial Reporting and Changing Prices: Specialized Assets—Mining and Oil and Gas*
c. FASB Statement No. 40, *Financial Reporting and Changing Prices: Specialized Assets—Timberlands and Growing Timber*
d. FASB Statement No. 41, *Financial Reporting and Changing Prices: Specialized Assets—Income-Producing Real Estate*
e. FASB Statement No. 46, *Financial Reporting and Changing Prices: Motion Picture Films*
f. FASB Statement No. 54, *Financial Reporting and Changing Prices: Investment Companies*
g. FASB Statement No. 69, *Disclosures about Oil and Gas Producing Activities, paragraphs 35-38*
h. FASB Statement No. 70, *Financial Reporting and Changing Prices: Foreign Currency*

Translation

i. FASB Statement No. 82, *Financial Reporting and Changing Prices: Elimination of Certain Disclosures*

j. FASB Technical Bulletin No. 81-4, *Classification as Monetary or Nonmonetary Items*.

FASB Technical Bulletin No. 79-8, *Applicability of FASB Statements 21 and 33 to Certain Brokers and Dealers in Securities*, is amended to delete any reference to Statement 33.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Disclosure

3. A business enterprise that prepares its financial statements in U.S. dollars and in accordance with U.S. generally accepted accounting principles is encouraged, but not required, to disclose supplementary information on the effects of changing prices. Appendix A provides measurement and presentation guidelines for disclosure. Entities are not discouraged from experimenting with other forms of disclosure.

Effective Date

4. This Statement is effective for financial reports issued after December 2, 1986.

This Statement was adopted by the affirmative vote of four members of the Financial Accounting Standards Board. Messrs. Lauver, Mosso, and Swieringa dissented.

Mr. Mosso dissented to the issuance of Statement 33 and he dissents to its rescission, both for the same reason. He believes that accounting for the interrelated effects of general and specific price changes is the most critical set of issues that the Board will face in this century. It is too important either to be dealt with inconclusively as in the original Statement 33 or to be written off as a lost cause as in this Statement.

The basic proposition underlying Statement 33—that inflation causes historical cost financial statements to show illusory profits and mask erosion of capital—is virtually undisputed. Specific price changes are inextricably linked to general inflation, and the combination of general and specific price changes seriously reduces the relevance, the representational faithfulness, and the comparability of historical cost financial statements.

Although the current inflation rate in the United States is relatively low in the context of recent history, its compound effect through time is still highly significant. High inflation rates prevail in many countries where United States corporations operate. Rates from country to country vary from time to time. Those distortive influences on financial statements will now go unmeasured and undisclosed.

Although Statement 33 had obvious shortcomings, it was a base on which to build. It represented years of due process—research, debate, deliberations, decisions—and application experience. As last amended, it had made significant progress in eliminating alternative concepts and methodologies. Its recision means that much of that due process and application experience will have to be repeated in response to a future inflation crisis. That will entail great cost in terms of time, money, and creative talent and, because due process does not permit quick reaction to crises, it risks loss of credibility for the Board and loss of initiative in private sector standard setting.

Mr. Lauver shares the views expressed by Mr. Mosso. He believes that instead of rescinding Statement 33, a continuing effort should be undertaken to complete what was only begun by that Statement.

Statement 33 was not a completed product. First, it required adjustment of only two of the items known to be affected by price changes, cost of sales and depreciation. Second, two adjusted amounts for cost of sales and depreciation were required to be reported, one on a constant purchasing power basis and one on a specific price basis. Third, the adjusted amounts together with two new items required to be disclosed, gain or loss on monetary items and certain holding gains, were not required to be reported in an articulating set of adjusted statements of financial position and performance. Indeed, no determination was made about how those supplemental disclosures could or should be integrated into an alternate measure of enterprise performance.

Relative to most changes in financial reporting, the changes required by Statement 33 were monumental. Because most accountants and users of financial statements have been inculcated with a model of financial reporting that assumes stability of the monetary unit, accepting a change of this consequence would take a lengthy period of time under the best of circumstances. Given the incomplete and complex nature of the disclosures described in the preceding paragraph, Mr. Lauver believes that there is no reason to be concerned about or surprised by comments that the Statement 33 disclosures were not widely used after a period as short as five years. He acknowledges that improvement of disclosures about the effects of changing prices requires a number of complex and difficult decisions. However, the importance of those effects requires that the Statement 33 effort be continued to complete the development of an alternate measure of enterprise performance and that the disclosures based on that measure be evaluated for a reasonable period of years before deciding to end the experiment.

Mr. Swieringa shares the views of Mr. Mosso and Mr. Lauver. In addition, he believes that Statement 33 should not be rescinded because an important opportunity exists now to reconsider the Statement 33 disclosures. Systems and data continuity will be lost by making these disclosures voluntary, and reinstating requirements to disclose the effects of changing prices on business enterprises when inflation rates increase will be difficult, time consuming, and costly.

The Statement 33 disclosures were developed in the late 1970s when double-digit inflation rates created considerable pressure for information about the effects of changing prices on enterprise financial position and performance. Since Statement 33 was issued, inflation rates have decreased dramatically and evidence has been obtained about the limited use of this information. Lower inflation rates and evidence of limited use are not independent events, but they provide a context in which a reconsideration of the Statement 33 disclosures can take place without the crisis atmosphere of the late 1970s. Mr. Swieringa believes that such a reconsideration could be based on the comments received on the December 1984 Exposure Draft and on evidence presented in several published articles and monographs.

Mr. Swieringa also believes that systems and data continuity will be lost by issuing this Statement. Statement 33 initially applied only to very large public enterprises, but the number of those enterprises increased over time because of growth and inflation. Those enterprises implemented systems to capture and report Statement 33 data. One concern is that those enterprises will remove their systems, thereby limiting their ability and inclination to provide the data when inflation rates increase. Another concern is that Statement 33 data will no longer be readily available from data service organizations in machine-readable form. In recent years, analysts and researchers have used those data for trend analysis and for model estimation and testing. The loss of those data may limit the ability and inclination of users and researchers to continue to assess the effects of changing prices on enterprise financial position and performance.

Finally, Mr. Swieringa believes that reinstating requirements to disclose the effects of changing prices on business enterprises when inflation rates increase will be as difficult, time consuming, and costly as the initial implementation of Statement 33 disclosures in 1979. The alternative approaches described in paragraph 120 and the criteria described in paragraphs 123-126 will have to be considered anew in any future project that considers reinstating those requirements.

Members of the Financial Accounting Standards Board:

Donald J. Kirk, *Chairman*
Victor H. Brown
Raymond C. Lauver
David Mosso
C. Arthur Northrop
Robert J. Swieringa
Arthur R. Wyatt

Appendix A

GUIDANCE FOR THE MEASUREMENT AND PRESENTATION OF SUPPLEMENTARY INFORMATION ON EFFECTS OF CHANGING PRICES

CONTENTS

Paragraph Numbers

Appendix A: GUIDANCE FOR THE MEASUREMENT AND PRESENTATION OF SUPPLEMENTARY INFORMATION ON EFFECTS OF CHANGING PRICES

Introduction

5. The Board and others expended considerable effort to develop the supplementary disclosures on the effects of changing prices required by Statement 33, as amended. The Board believes that those requirements are the best method devised to date for the presentation of those disclosures. Accordingly, those requirements have been combined [1] in this appendix for the benefit of those enterprises that wish to continue making those disclosures.

6. Although the U.S. economy is experiencing little inflation at the present time, that condition may not continue. If it does not, the Board again may need to require disclosure of the effects of changing prices. If so, this appendix is likely to serve as a starting point for the development of a standard on reporting the effects of changing prices.

Presentation

Five-Year Summary of Selected Financial Data

7. An enterprise shall disclose the following information [2] for each of the five most recent years [3] (paragraphs 36 and 37):

a. Net sales and other operating revenues
b. **Income from continuing operations** [4] on a current cost basis (paragraphs 32 and 33)
c. **Purchasing power gain or loss** on net monetary items (paragraphs 40-43)
d. Increase or decrease in the current cost or lower **recoverable amount** of inventory and property, plant, and equipment,[5] net of inflation (paragraphs 34 and 35)
e. The aggregate foreign currency **translation adjustment** on a current cost basis, if applicable (paragraphs 9, 38, and 39)
f. Net assets at year-end on a current cost basis (paragraphs 27 and 28)
g. Income per common share from continuing operations on a current cost basis
h. Cash dividends declared per common share
i. Market price per common share at year-end.

8. The information presented in the five-year summary shall be stated either of the following:

a. In average-for-the-year or end-of-year units of constant purchasing power
b. In dollars [6] having a purchasing power equal to that of dollars of the base period used by the Bureau of Labor Statistics in calculating the Consumer Price Index for All Urban Consumers (CPI-U) [7] (currently 1967).

An enterprise shall disclose the level of the CPI-U used for each of the five most recent years.

9. If the enterprise has a significant foreign operation measured in a functional currency other than the U.S. dollar (dollar), it shall disclose whether adjustments to the current cost information to reflect the effects of general inflation are based on the U.S. general price level index (the **translate-restate** method, paragraph 38) or on a functional currency general price level index (the **restate-translate** method, paragraph 39).

10. The enterprise shall provide an explanation of the disclosures required by this appendix and a discussion of their significance in the circumstances of the enterprise. Disclosure and discussion of additional information to help users of the financial report understand the effects of changing prices on the activities of the enterprise are encouraged.

Additional Disclosures for the Current Year

11. In addition to the information required by paragraphs 7-10, an enterprise shall provide the information specified in paragraphs 12 and 13 if income from continuing operations on a **current cost/constant purchasing power** basis would differ significantly from income from continuing operations in the primary financial statements.

12. An enterprise shall disclose certain components of income from continuing operations for the current year on a current cost basis (paragraphs 32 and 33) applying the same constant purchasing power option used for presentation of the five-year summary. The information may be presented in a *statement format* (disclosing revenues, expenses, gains, and losses), in a *reconciliation format* (disclosing adjustments to the income from continuing operations that is shown in the primary income statement), or in notes to the five-year summary required by paragraph 7. Formats for presenting the supplementary information are illustrated in paragraph 45. Whichever format is used, the presentation shall disclose (for example, in a reconciliation format) or allow the reader to determine (for example, in a statement format) the difference between the amount in the primary statements and the current cost amount of the following items: cost of goods sold and depreciation, depletion, and amortization expense. If depreciation has been allocated among various expense categories in the supplementary computations of income from continuing operations (for example, among cost of goods sold and other functional expenses), the aggregate amount of depreciation on a current cost basis shall be included in the notes to the supplementary information. In addition to information about income from continuing operations, the enterprise may include the following items in a schedule of current year information: (a) the purchasing power gain or loss on net monetary items, (b) the increase or decrease in the current cost or lower recoverable amount of inventory and property, plant, and

equipment, net of inflation, and (c) the translation adjustment. As illustrated in paragraph 45 and defined in the glossary in paragraph 44, income from continuing operations does not include items (a), (b), or (c).

13. An enterprise shall also disclose:

a. Separate amounts for the current cost or lower recoverable amount at the end of the current year of inventory and property, plant, and equipment (paragraphs 16-26 and 29-31)
b. The increase or decrease in current cost or lower recoverable amount before and after adjusting for the effects of inflation of inventory and property, plant, and equipment for the current year (paragraphs 34 and 35)
c. The principal types of information used to calculate the current cost of inventory; property, plant, and equipment; cost of goods sold; and depreciation, depletion, and amortization expense (paragraphs 19-26)
d. Any differences between (1) the depreciation methods, estimates of useful lives, and salvage values of assets used for calculations of current cost/constant purchasing power depreciation and (2) the methods and estimates used for calculations of depreciation in the primary financial statements (paragraph 22).

Additional Disclosures by Enterprises with Mineral Resource Assets

14. For its mineral reserves other than oil and gas, an enterprise shall disclose the following additional information for each of its five most recent fiscal years:

a. Estimates of significant quantities of **proved mineral reserves** or proved and **probable mineral reserves** (whichever is used for cost amortization purposes) at the end of the year or at the most recent date during the year for which estimates can be made (If estimates are not made as of the end of the year, the disclosures shall indicate the dates of the estimates.)
b. The estimated quantity, expressed in physical units or in percentages of reserves, of each mineral product that is recoverable in significant commercial quantities if the mineral reserves included under subparagraph (a) include deposits containing one or more significant mineral products
c. The quantities of each significant mineral produced during the year (If the mineral reserves included under subparagraph (a) are ones that are milled or similarly processed, the quantity of each significant mineral product produced by the milling or similar process shall also be disclosed.)
d. The quantity of significant proved, or proved and probable, mineral reserves purchased or sold in place during the year
e. For each significant mineral product, the average market price or, for mineral products transferred within the enterprise, the equivalent market price prior to use in a manufacturing process.

15. In determining the quantities to be reported in conformity with paragraph 14:

a. If the enterprise issues consolidated financial statements, 100 percent of the quantities attributable to the parent company and 100 percent of the quantities attributable to its consolidated subsidiaries (whether or not wholly owned) shall be included.
b. If the enterprise's financial statements include investments that are proportionately consolidated, the enterprise's quantities shall include its proportionate share of the investee's quantities.
c. If the enterprise's financial statements include investments that are accounted for by the equity method, the investee's quantities shall not be included in the disclosures of the enterprise's quantities. However, the enterprise's (investor's) share of the investee's quantities of reserves shall be reported separately, if significant.

Measurement

Inventory and Property, Plant, and Equipment

16. Current cost amounts of inventory and property, plant, and equipment are measured as follows:

a. Inventory at current cost or lower recoverable amount at the measurement date
b. Property, plant, and equipment at the current cost or lower recoverable amount of the assets' remaining service potential at the measurement date
c. Resources used on a partly completed contract at current cost or lower recoverable amount at the date of use on or commitment to the contract.

17. The current cost of inventory owned by an enterprise is the current cost of purchasing the goods concerned or the current cost of the resources required to produce the goods concerned (including an allowance for the current overhead costs according to the allocation bases used under generally accepted accounting principles), whichever would be applicable in the circumstances of the enterprise.

18. The current cost of property, plant, and equipment owned by an enterprise is the current cost of acquiring the same service potential (indicated by operating costs and physical output capacity) as embodied by the asset owned; the information used to measure current cost reflects whatever method of acquisition would currently be appropriate in the circumstances of the enterprise. The current cost of a used asset may be calculated:

a. By measuring the current cost of a new asset that has the same service potential as the used asset had when it was new (the current cost of the asset as if it were new) and deducting an allowance for depreciation
b. By measuring the current cost of a used asset of the same age and in the same condition as the asset owned
c. By measuring the current cost of a new asset with a different service potential and adjusting

that cost for the value of the difference in service potential due to differences in life, output capacity, nature of service, and operating costs.

19. Various types of information may be used in the measurement methods described in paragraphs 17 and 18 to determine the current cost of inventory; property, plant, and equipment; cost of goods sold;[8] and depreciation, depletion, and amortization expense. The information may be applied to single items or broad categories, as appropriate in the circumstances. The following types of information are listed as examples of the information that may be used but are not listed in any order of preferability. The enterprise is expected to select types of information appropriate to its particular circumstances, giving due consideration to their availability, reliability, and cost:

a. Indexation
   (1) Externally generated price indexes for the class of goods or services being measured
   (2) Internally generated price indexes for the class of goods or services being measured
b. Direct pricing
   (1) Current invoice prices
   (2) Vendors' price lists or other quotations or estimates
   (3) Standard manufacturing costs that reflect current costs.

20. An enterprise may substitute **historical cost** amounts adjusted by an externally generated price index of a broad-based measure of general purchasing power (that is, **historical cost/constant purchasing power** amounts) for current cost amounts if that substitution would not result in a significantly different number for income from continuing operations than other means of estimating current cost amounts described in this appendix. For example, an enterprise with small amounts of inventory and property, plant, and equipment apart from certain specialized assets (paragraphs 23-26) may be able to report historical cost/constant purchasing power information. In such circumstances, disclosure of the increase or decrease in the current cost or lower recoverable amount of inventory and property, plant, and equipment, net of inflation (paragraphs 7(d) and 13(b)), is not required, but the discussions described in paragraphs 10 and 13(a), (c), and (d) are required.

21. Current cost measurements are to be based on production or purchase of the asset in whatever location or market would minimize total cost including transportation cost. For a U.S. operation, either (a) the purchase would be made in the United States and current cost would be estimated directly in dollars or (b) the purchase would be made in a foreign market and the current cost in that market would be translated into dollars at the current exchange rate. An enterprise may need to measure the current cost of inventory and property, plant, and equipment located outside the United States. That may be difficult depending upon the availability of information in the country concerned, and, accordingly, reasonable approximations are acceptable. If a foreign operation first measures current cost in a currency other than its functional currency, that amount is then translated into the functional currency at the current exchange rate.

22. There is a presumption that depreciation methods, estimates of useful lives, and salvage values of assets for purposes of the supplementary information are the same as the methods and estimates used for calculations in the primary financial statements. However, if the primary financial statements are based on methods and estimates that partly allow for price changes, different methods and estimates may be used for purposes of the supplementary information.

Specialized Assets

23. The current cost of **mineral resource assets** is determined by current market buying prices or by the current cost of finding and developing mineral reserves. The Board recognizes that no generally accepted approach exists for measuring the current finding cost of mineral reserves. To indicate the effects of changes in current costs, it may be impracticable to do more than adjust historical costs by an index of the changes in specific prices of the inputs concerned. That approach may fail to yield a close approximation of the current cost of finding and developing new reserves. In recognition of that difficulty, the requirements of this appendix are flexible regarding the approach used to measure current cost of mineral resource assets. The approach may include use of specific price indexes, direct information about market buying prices, and other statistical evidence of the cost of acquisitions.

24. Because Statement 69 requires an enterprise to disclose a standardized measure of discounted future net cash flows relating to proved oil and gas reserve quantities, the enterprise may follow the approach in paragraph 23 or in paragraph 25 for its oil and gas mineral resource assets. Paragraph 13(c) requires disclosure of the types of information that have been used to measure current costs.

25. Timberlands and growing timber, **income-producing real estate**, and **motion picture films** have certain special features that raise doubts about the applicability of the current cost measurement methods required for other assets. Accordingly, an enterprise may disclose historical cost amounts adjusted by an externally generated index of a broad-based measure of general purchasing power as substitutes for current cost amounts for such assets and their related expenses.

26. If an enterprise estimates the current cost of growing timber and timber harvested by adjusting historical cost for the changes in specific prices, those historical costs may either (a) be limited to the costs that are capitalized in the primary financial statements or (b) include all costs that are directly related to reforestation and forest management, such as planting, fertilization, fire protection, property taxes, and nursery stock, whether or not those costs are capitalized in the primary financial statements.

Net Assets

27. If the enterprise presents the minimum information required by this appendix, the amount of net assets (that is, shareholders' equity) is the amount of net assets reported in the primary

financial statements, adjusted for the difference between the historical cost amounts and the current cost or lower recoverable amounts of inventory and property, plant, and equipment.

28. If the enterprise elects to present comprehensive current cost/constant purchasing power financial statements as supplementary information, the amount of net assets in the five-year summary is the amount reported in the supplementary balance sheet.

Recoverable Amount

29. Recoverable amount is the current worth of the net amount of cash expected to be recoverable from the use or sale of an asset. It may be measured by considering the **value in use** or **current market value** of the asset concerned. Value in use is used to determine recoverable amount of an asset if immediate sale of the asset is not intended. Current market value is used to determine recoverable amount only if the asset is about to be sold.

30. If the recoverable amount for a group of assets is judged to be materially and permanently lower than the current cost amount, the *recoverable amount* is used as a measure of the assets and of the expense associated with the use or sale of the assets. Decisions on the measurement of assets at their recoverable amounts need not be made by considering assets individually unless they are used independently of other assets.

31. An enterprise that is subject to rate regulation or another form of price control may be limited to a maximum recovery through its selling prices, based on the nominal currency amount of the historical cost of its assets. In that situation, historical costs measured in nominal currency may represent an appropriate basis for the measurement of the recoverable amounts associated with those assets. Recoverable amounts may also be lower than historical costs. Nevertheless, cost of goods sold and depreciation, depletion, and amortization expense are to be measured at current cost/constant purchasing power amounts provided that replacement of the service potential of the related assets would be undertaken, if necessary, in current economic conditions; if replacement would not be undertaken, those expenses are to be measured at recoverable amounts.

Income from Continuing Operations

32. An enterprise that presents the minimum information required by this appendix shall measure income from continuing operations on a current cost basis as follows:

a. Cost of goods sold at current cost or lower recoverable amount at the date of sale or at the date on which resources are used on or committed to a specific contract
b. Depreciation, depletion, and amortization expense of property, plant, and equipment on the basis of the average current cost of the assets' service potential or lower recoverable amount during the period of use.

Other revenues, expenses, gains, and losses may be measured at the amounts included in the primary income statement. (Refer to paragraphs 16-26 and 29-31 for discussions of current cost or lower recoverable amount measurements.)

33. The amount of income tax expense in computations of current cost/constant purchasing power income from continuing operations is the same as the amount of income tax expense charged against income from continuing operations in the primary financial statements. No adjustments are to be made to income tax expense for any timing differences that might be deemed to arise as a result of the use of current cost accounting methods. Income tax expense is not to be allocated between income from continuing operations and the increases or decreases in current cost amounts of inventory and property, plant, and equipment.

Increase or Decrease in the Current Cost Amounts of Inventory and Property, Plant, and Equipment, Net of Inflation

34. The increase or decrease in the current cost amounts of inventory and property, plant, and equipment represents the difference between the measures of the assets at their *entry dates* for the year and the measures of the assets at their *exit dates* for the year. Entry dates means the beginning of the year or the dates of acquisition, whichever is applicable; *exit dates* means the end of the year or the dates of use, sale, or commitment to a specific contract, whichever is applicable. For the purposes of this paragraph, assets are measured in accordance with the provisions of paragraphs 16-26 and 29-31.

35. For the current year, the increase or decrease in current cost amounts of inventory and property, plant, and equipment is reported both before and after eliminating the effects of general inflation (paragraph 13(b)). In the five-year summary, the increase or decrease is reported after elimination of the effects of each year's general inflation (paragraph 7(d)). An acceptable approximate method of calculating the increase or decrease in current cost amounts and the inflation adjustment is illustrated in paragraphs 67-70.

Restatement of Current Cost Information into Units of Constant Purchasing Power

36. Enterprises that do not have significant foreign operations or that use the dollar as the functional currency for all significant foreign operations are to use the CPI-U to restate current costs into units of constant purchasing power. Acceptable approximate methods are illustrated in paragraph 82.

37. The effects of general inflation on current cost information for operations measured in a foreign functional currency are measured either (a) after translation and based upon the CPI-U (the translate-restate method) or (b) before translation and based on a broad-based measure of the change in the general purchasing power of the functional currency (the restate-translate method).[9] The same method is to be used for all operations measured in functional currencies other than the dollar and for all periods presented. Acceptable approximate methods are illustrated in paragraphs 82, 83, 90, and 91.

Translation Adjustment

38. If current cost information for operations measured in functional currencies other than the dollar is based on the translate-restate method, the aggregate translation adjustment on the current cost basis is stated net of any income taxes allocated to the aggregate translation adjustment in the primary financial statements (FASB Statement No. 52, *Foreign Currency Translation*, paragraph 31(c)).

39. If current cost information for operations measured in functional currencies other than the dollar is based on the restate-translate method, the aggregate translation adjustment on the current cost basis is stated net of both any income taxes allocated to the aggregate translation adjustment in the primary financial statements and the aggregate **parity adjustment**. The parity adjustment is the amount needed to measure end-of-year net assets in (a) average-for-the-year dollars, if income from continuing operations is measured in average-for-the-year functional currency units, or (b) end-of-year dollars, if income from continuing operations is measured in end-of-year functional currency units.

Purchasing Power Gain or Loss on Net Monetary Items

40. The purchasing power gain or loss on net monetary items is the net gain or loss determined by restating in units of constant purchasing power the opening and closing balances of, and transactions in, **monetary assets** and **monetary liabilities**. Acceptable approximate methods of calculating the purchasing power gain or loss on net monetary items are illustrated in paragraphs 66, 83, and 90.

41. The economic significance of monetary assets and liabilities depends heavily on the general purchasing power of money, although other factors, such as creditworthiness of debtors, may affect their significance. The economic significance of nonmonetary items depends heavily on the value of specific goods and services. Nonmonetary assets include (a) goods held primarily for resale or assets held primarily for direct use in providing services for the business of the enterprise, (b) claims to cash in amounts dependent on future prices of specific goods or services, and (c) residual rights such as goodwill or equity interests. Nonmonetary liabilities include (a) obligations to furnish goods or services in quantities that are fixed or determinable without reference to changes in prices and (b) obligations to pay cash in amounts dependent on future prices of specific goods or services. Guidance on the classification of balance sheet items as monetary or nonmonetary is set forth in paragraphs 96-108.

42. If inflation-adjusted current cost information is based on the translate-restate method, the purchasing power gain or loss on net monetary items is equal to the net gain or loss determined by restating the opening and closing balances of, and transactions in, monetary assets and liabilities in units of constant purchasing power as measured by the CPI-U.

43. If inflation-adjusted current cost information is based on the restate-translate method, the purchasing power gain or loss on net monetary items is equal to the net gain or loss determined by restating the opening and closing balances of, and transactions in, monetary assets and liabilities in units of constant purchasing power as measured by the change in the general purchasing power of the functional currency. The purchasing power gain or loss computed in that manner is translated into its dollar equivalent at the average exchange rate for the period.

Glossary

44. This paragraph defines certain terms that are used in this appendix.

Current cost/constant purchasing power accounting

A method of accounting based on measures of current cost or lower recoverable amount in units of currency, each of which has the same general purchasing power. For operations in which the dollar is the functional currency, the general purchasing power of the dollar is used and the CPI-U is the required measure of purchasing power (paragraph 36). For operations in which the functional currency is other than the dollar, the general purchasing power of either the dollar or the functional currency is used (paragraph 37).

Current market value

The amount of cash, or its equivalent, expected to be derived from the sale of an asset net of costs required to be incurred as a result of the sale.

Historical cost accounting

The generally accepted method of accounting used in the primary financial statements that is based on measures of historical prices without restatement into units, each of which has the same general purchasing power.

Historical cost/constant purchasing power accounting

A method of accounting based on measures of historical prices in units of a currency, each of which has the same general purchasing power.

Income from continuing operations

Income after applicable income taxes but excluding the results of discontinued operations, extraordinary items, the cumulative effect of accounting changes, translation adjustments, purchasing power gains and losses on monetary items, and increases and decreases in the current cost or lower recoverable amount of nonmonetary assets and liabilities.

Income-producing real estate

Properties that meet all of the following criteria:

a. Cash flows can be directly associated with a long-term leasing agreement with

unaffiliated parties.
b. The property is being operated. (It is not in a construction phase.)
c. Future cash flows from the property are reasonably estimable.
d. Ancillary services are not a significant part of the lease agreement.

Hotels, which have occupancy rates and related cash flows that may fluctuate to a relatively large extent, do not meet the criteria for income-producing real estate.

Mineral resource assets

Assets that are directly associated with and derive value from all minerals that are extracted from the earth. Such minerals include oil and gas, ores containing ferrous and nonferrous metals, coal, shale, geothermal steam, sulphur, salt, stone, phosphate, sand, and gravel. Mineral resource assets include mineral interests in properties, completed and uncompleted wells, and related equipment and facilities and other facilities required for purposes of extraction (FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies*, paragraph 11). This definition does not cover support equipment because that equipment is included in the property, plant, and equipment for which current cost measurements are required by this appendix.

Monetary asset

Money or a claim to receive a sum of money the amount of which is fixed or determinable without reference to future prices of specific goods or services.

Monetary liability

An obligation to pay a sum of money the amount of which is fixed or determinable without reference to future prices of specific goods and services.

Motion picture films

All types of films and videotapes and disks, including features, television specials, series, and cartoons that meet one of the following criteria:

a. Exhibited in theaters
b. Licensed for exhibition by individual television stations, groups of stations, networks, cable television systems, or other means
c. Licensed for commercial reproduction (for example, for the home viewing market).

Parity adjustment

The effect of the difference between local and U.S. inflation for the year on net assets (that is, shareholders' equity) measured in nominal dollars. If only the differential rates of U.S. and local inflation are reflected in the exchange rates (parity), the parity adjustment and the translation adjustment net to zero. Therefore, the sum of the parity adjustment and the translation adjustment represents the effect of exchange rate changes in excess of (or less than) that needed to maintain purchasing power parity between the functional currency and the dollar.

Probable mineral reserves

In extractive industries other than oil and gas, the estimated quantities of commercially recoverable reserves that are less well defined than proved.

Proved mineral reserves

In extractive industries other than oil and gas, the estimated quantities of commercially recoverable reserves that, on the basis of geological, geophysical, and engineering data, can be demonstrated with a reasonably high degree of certainty to be recoverable in the future from known mineral deposits by either primary or improved recovery methods.

Purchasing power gain or loss on net monetary items

The net gain or loss determined by restating in units of constant purchasing power the opening and closing balances of, and transactions in, monetary assets and liabilities.

Recoverable amount

Current worth of the net amount of cash expected to be recoverable from the use or sale of an asset (paragraphs 29-31).

Restate-translate

An approach to converting current cost/nominal functional currency data of a foreign operation into units of constant purchasing power expressed in dollars. Using this approach, the current cost/nominal functional currency data are restated into units of constant purchasing power using a general price index for the foreign currency. After restatement into units of constant functional currency purchasing power, the current cost data are translated into dollars. This approach often necessitates a parity adjustment.

Translate-restate

An approach to converting current cost/nominal functional currency data of a foreign operation into units of constant purchasing power expressed in dollars. Using this approach, the current cost/nominal functional currency data are first translated into dollars and then restated into units of constant purchasing power using the CPI-U.

Translation adjustment

The effect that results from the process of translating an entity's financial statements from its functional currency into the dollar (paragraphs 38 and 39).

Value in use

The amount determined by discounting the future cash flows (including the ultimate proceeds of disposal) expected to be derived from the use of an asset at an appropriate rate that allows for the risk of the activities concerned.

Illustrations of Disclosures

45. This paragraph illustrates formats that may be used to disclose the information required by this appendix for a manufacturing enterprise. An enterprise may choose to disclose the information required by paragraphs 7-13 of this appendix (a) in a schedule of annual information (for example, Schedule 1 or Schedule 2), in a five-year summary (for example, Schedule 3 or Schedule 4), and notes to those schedules or (b) in a five-year summary and notes to that summary (for example, Schedule 5). Many enterprises have included amounts reported in the primary statements alongside current cost/constant purchasing power amounts in the five-year summary. The Board encourages enterprises to continue to adapt the disclosure formats to enhance such comparisons. Schedule 4 illustrates a five-year summary with comparative data from the primary financial statements. The Board also encourages enterprises to provide more detailed discussions than the illustrative notes in this paragraph—especially discussion of the significance of the information in the circumstances of the enterprise (required by paragraph 10) and the principal types of information used to calculate current cost amounts (required by paragraph 13(c)). Illustrative calculations are given in paragraphs 46-95. In the schedules that follow, the CPI-U is expressed in average dollars.

Schedule 1

Statement of Income from Continuing Operations
Adjusted for Changing Prices [a]

For the Year Ended December 31, 19X6
In Thousands of Average 19X6 Dollars

Income from continuing operations, as reported in the primary income statement	$22,995
Adjustments to reflect current costs	
Cost of goods sold	(8,408)
Depreciation expense	(9,748)
Income from continuing operations adjusted for changes in specific prices	$ 4,839
Gain from decline in purchasing power of net amounts owed [b]	$ 2,449
Increase in specific prices (current cost) of inventory and property, plant, and equipment held during the year [c]	$25,846
Effect of increase in general price level	5,388
Excess of increase in specific prices over increase in the general price level	$20,458
Foreign currency translation adjustment [d]	$ (624)

Schedule 2

Statement of Income from Continuing Operations Adjusted for Changing Prices [a]

For the Year Ended December 31, 19X6
In Thousands of Dollars

	As Reported in the Primary Statements	Adjusted for Changes in Specific Prices (Current Cost)
Net sales and other operating revenues	$275,500	$275,500
Cost of goods sold	197,000	205,408
Depreciation expense	10,275	20,023
Other operating expenses	14,685	14,685
Interest expense	7,550	7,550
Income tax expense	22,995	22,995
	252,505	270,661
Income from continuing operations	$ 22,995	$ 4,839
Gain from decline in purchasing power of net amounts owed [b]		$ 2,449
Increase in specific prices (current cost) of inventory and property, plant, and equipment held during the year [c]		$ 25,846
Effect of increase in general price level		5,388
Excess of increase in specific prices over increase in the general price level		$ 20,458
Foreign currency translation adjustment [d]	$ (295)	$ (624)

Schedule 3

Five-Year Comparison of Selected Financial Data Adjusted for Effects of Changing Prices

In Thousands of Average 19X6 Dollars, except for Per Share Amounts

	Year Ended December 31,				
	19X6	19X5	19X4	19X3	19X2
Net sales and other operating revenues	$275,500	$247,500	$240,000	$235,500	$265,000
Income (loss) from continuing operations	4,839	1,660	(2,102)	(4,663)	1,261
Gain from decline in purchasing power of net amounts owed	2,449	7,027	5,432	1,247	6,375
Excess of increase in specific prices of inventory and property, plant, and equipment over increase in the general price level	20,458	2,292	3,853	8,597	3,777
Foreign currency translation adjustment	(624)	(386)	(454)	(293)	127
Net assets at year-end [a]	92,027	67,905	60,409	56,966	55,705
Per share information:					
Income (loss) from continuing operations	$ 3.23	$ 1.11	$ (1.40)	$ (3.11)	$ .84
Cash dividends declared	2.00	2.06	2.19	2.42	2.75
Market price at year-end	35	39	43	27	32
Average consumer price index [b]	298.4	289.1	272.4	246.8	217.4

Schedule 4

Five-Year Comparison of Selected Financial Data

In Thousands of Dollars,
except for Per Share Amounts

	Year Ended December 31,				
	19X6	**19X5**	**19X4**	**19X3**	**19X2**
Total revenue					
As reported	$275,500	$239,800	$219,100	$194,800	$193,100
Adjusted for general inflation [a]	275,500	247,500	240,000	235,500	265,000
Income (loss) from operations					
As reported	22,995	11,097	4,756	9,977	11,847
Adjusted for specific price changes [a]	4,839	1,660	(2,102)	(4,663)	1,261
Purchasing power gain from holding net monetary liabilities [a]	2,449	7,027	5,432	1,247	6,375
Excess of increase in specific price of assets over increase in the general price level [a]	20,458	2,292	3,853	8,597	3,777
Foreign currency translation adjustment					
As reported	(295)	(276)	(396)	(138)	76
Adjusted for specific price changes [a]	(624)	(386)	(454)	(293)	127
Net assets at year-end					
As reported	47,700	28,000	20,179	18,819	11,980
Adjusted for specific price changes [b]	92,027	67,905	60,409	56,966	55,705
Per share information:					
Income (loss) from operations					
As reported	$15.33	$ 7.40	$ 3.17	$6.65	$ 7.90
Adjusted for specific price changes [a]	3.23	1.11	(1.40)	(3.11)	.84
Cash dividends declared					
As reported	2.00	2.00	2.00	2.00	2.00
Adjusted for general inflation [a]	2.00	2.06	2.19	2.42	2.75
Market price at year-end					
As reported	36	38	41	23	25
Adjusted for general inflation [a]	35	39	43	27	32
Average consumer price index [c]	298.4	289.1	272.4	246.8	217.4

Schedule 5
Five-Year Comparison of Selected Financial Data
Adjusted for Effects of Changing Prices [a]

In Thousands of Average 19X6 Dollars,
except for Per Share Amounts

	Year Ended December 31,				
	19X6	19X5	19X4	19X3	19X2
Net sales and other operating revenues	$275,500	$247,500	$240,000	$235,500	$265,000
Income (loss) from continuing operations [b]	4,839	1,660	(2,102)	(4,663)	1,261
Gain from decline in purchasing power of net amounts owed [c]	2,449	7,027	5,432	1,247	6,375
Increase in specific prices of inventory and property, plant, and equipment [d]	20,458	2,292	3,853	8,597	3,777
Foreign currency translation adjustment [e]	(624)	(386)	(454)	(293)	127
Net assets at year-end [d]	92,027	67,905	60,409	56,966	55,705
Per share information:					
Income (loss) from continuing operations	$3.23	$1.11	$ (1.40)	$ (3.11)	$ .84
Cash dividends declared	2.00	2.06	2.19	2.42	2.75
Market price at year-end	35	39	43	27	32
Average consumer price index [f]	298.4	289.1	272.4	246.8	217.4

Illustrative Calculations of Current Cost/Constant Purchasing Power Information

Introduction

46. Paragraphs 47-95 illustrate the methodology that might be used in calculating the disclosures in paragraph 45.

47. Computation of current cost information should be based on a detailed analysis of all transactions; however, the costs of preparing the information can be reduced with little loss of usefulness by simplifying the methods of calculation. Therefore, only cost of sales and depreciation expense need to be adjusted from the amounts shown in the primary income statement. Revenues, other expenses, and gains and losses need not be adjusted. Approximate methods of computation are acceptable for adjusting cost of sales and depreciation expense. The

measurement of current cost is not illustrated.

48. The objective in making these calculations is to obtain a *reasonable degree* of accuracy—complete precision is not required. Preparers are encouraged to devise short-cut methods of calculation, appropriate to their individual circumstances.

49. If inventories and cost of sales are accounted for under the LIFO method in the primary financial statements, the only adjustment normally required in computing income from continuing operations would be to eliminate the effect of changing prices on any prior-period LIFO layer liquidation.

50. Seven basic steps to restate historical cost information into current cost/constant purchasing power information are illustrated in paragraphs 47-95:

a. Analyze inventory (at the beginning and end of the year) and cost of goods sold to determine when the costs were incurred
b. Restate inventory and cost of goods sold into current cost
c. Analyze property, plant, and equipment to determine when the related assets were acquired
d. Restate property, plant, and equipment and depreciation, depletion, and amortization expense into current cost
e. Identify the amount of net monetary items (paragraphs 96-108) at the beginning and end of the period and changes during the period
f. Compute the purchasing power gain or loss on net monetary items
g. Compute the change in current cost of inventory and property, plant, and equipment and the related effect of the increase in the general price level.

51. The methodology illustrated in paragraphs 47-95 has been developed for the hypothetical enterprise, Parent Company. Parent Company has a wholly owned foreign subsidiary, Sub Company. Sub Company measures its operations in a functional currency other than the dollar. The changing prices disclosures for Parent Company and Sub Company are developed separately. Merging the amounts calculated for each entity results in a consolidated disclosure:

a. Paragraphs 59-71 illustrate the minimum recommended calculations for the domestic operations of Parent Company. A method of checking the arithmetic accuracy of the calculations is included in paragraph 72.
b. Paragraphs 79-86 illustrate the translate-restate method for Sub Company, a foreign subsidiary that does not use the dollar as a functional currency. A method of checking the arithmetic accuracy of the calculations is included in paragraph 84.
c. The results of the calculations described in (a) and (b) are summarized in paragraph 87 and are reflected in the illustrative disclosures in paragraph 45.

52. Paragraphs 88-95 illustrate the restate-translate method for Sub Company. A method of checking the arithmetic accuracy of the calculations is included in paragraphs 92 and 93.

53. Throughout this appendix, $ indicates nominal dollars, C$ indicates average 19X6 constant dollars, FC indicates nominal functional currency, C$E indicates dollar equivalents of FC amounts using the translate-restate method, CFC indicates average 19X6 constant functional currency, and CFC$ indicates the translated dollar equivalents of CFC amounts using the restate-translate method.

Parent Company Information

54. Historical cost/nominal financial statements

Parent Company
Balance Sheet (Unconsolidated)
As of December 31, 19X6 and 19X5
(000s)

	19X6	19X5		19X6	19X5
Current assets:			Current liabilities:		
Cash	$ 1,000	$ 2,000	Accounts payable and accrued expenses	$ 47,000	$ 32,000
Accounts receivable	36,000	16,500	Income taxes payable	6,000	6,000
Inventories, at FIFO cost	63,000	56,000	Current portion of long-term debt	5,000	5,000
Total current assets	100,000	74,500	Total current liabilities	58,000	43,000
Property, plant, and equipment, at cost	100,000	85,000	Deferred income taxes	6,000	5,000
Less accumulated depreciation	56,000	46,000	Long-term debt	34,000	39,000
	44,000	39,000	Total liabilities	98,000	87,000
			Capital stock †	10,000	10,000
Investment in Sub Company *	1,500	1,500	Retained earnings	37,500	18,000
	$145,500	$115,000		$145,500	$115,000

Parent Company (Unconsolidated)
Statement of Earnings and Retained Earnings
For the Year Ended December 31, 19X6

	(000s)
Sales	$270,000
Cost of goods sold, exclusive of depreciation	197,000
Selling, general, and administrative expenses	10,835
Depreciation	10,000
Interest	7,165
	225,000
Earnings before taxes	45,000
Income taxes	22,500
Net income	22,500
Retained earnings at beginning of year	18,000
	40,500
Dividends	3,000
Retained earnings at end of year	$ 37,500
Net income per share	$ 15

55. Inventory and production:

a. Inventory is accounted for on a first-in, first-out (FIFO) basis and turns over four times per year. There is no significant amount of work in progress or raw materials.
b. At December 31, 19X6 and 19X5 inventory consisted of 900,000 units and 1,000,000 units respectively—representing production of the immediately preceding quarter. Management has measured the current cost of inventory at $73 per unit at December 31, 19X6 ($65,700,000) and $58 per unit at December 31, 19X5 ($58,000,000).
c. Costs were incurred and goods produced as follows:

	(000s)					
	19X5	19X6				
	4th	1st	2nd	3rd	4th	Total
Historical costs	$56,000	$39,560	$59,400	$42,040	$63,000	$204,000
Units produced	1,000	618	900	618	900	3,036
Units sold		1,000	618	900	618	3,136

d. At December 31, 19X6 the selling price per unit was $85.
e. There were no write-downs or disposals of inventory.

56. Property, plant, and equipment:

a. Details of fixed assets at December 31, 19X6 are as follows:

		(000s)	
Date Acquired	**Percent Depreciated**	**Historical Cost**	**Accumulated Depreciation**
19W9	80	$ 50,000	$ 40,000
19X0	70	5,000	3,500
19X1	60	5,000	3,000
19X2	50	5,000	2,500
19X3	40	5,000	2,000
19X4	30	5,000	1,500
19X5	20	10,000	2,000
19X6	10	15,000	1,500
		$ 100,000	$ 56,000

b. Depreciation is calculated at 10 percent per annum, straight line. A full year's depreciation is charged in the year of acquisition.

c. There were no disposals.

d. Management has measured the current cost of property, plant, and equipment at December 31, 19X6 and 19X5 as follows:

	(000s)			
	December 31, 19X6		**December 31, 19X5**	
Date Acquired	**Current Cost**	**Accumulated Depreciation**	**Current Cost**	**Accumulated Depreciation**
19W9	$ 120,000	$ 96,000	$ 110,000	$ 77,000
19X0	10,000	7,000	6,000	3,600
19X1	15,000	9,000	7,000	3,500
19X2	18,000	9,000	12,000	4,800
19X3	12,000	4,800	10,000	3,000
19X4	17,000	5,100	15,000	3,000
19X5	12,000	2,400	10,000	1,000
19X6	16,000	1,600	–	–
	220,000	$ 134,900	170,000	$ 95,900
Accumulated depreciation	134,900		95,900	
Net current cost	$ 85,100		$ 74,100	

e. The recoverable amount has been determined by management to be in excess of current cost, net of accumulated depreciation.

57. Dividends were paid at the rate of $750,000 per quarter.

58. Consumer Price Index for All Urban Consumers (from the *Survey of Current Business*, U.S. Department of Commerce, Bureau of Economic Analysis, January 19X7):

December 19X5	292.4
Average 19X6	298.4
December 19X6	303.5

Parent Company Calculations

59. The objective is to express the supplementary information in average 19X6 dollars. As indicated in paragraph 27, nominal dollar measurements may be used for all elements of net assets other than inventory and property, plant, and equipment. As indicated in paragraph 32, nominal dollar measurements may be used for all elements of income from continuing operations other than cost of sales and depreciation.

Step 1: Analysis of Inventory and Cost of Goods Sold

60. Inventory is assumed to turn over four times per year. Therefore, inventory with a historical cost of $63,000,000 at December 31, 19X6 is assumed to have been acquired during the fourth quarter of 19X6, and inventory with a historical cost of $56,000,000 at December 31, 19X5 is assumed to have been acquired in the fourth quarter of 19X5.

Step 2: Current Cost of Inventory and Cost of Goods Sold

61. Cost of goods sold, current cost:

Current cost at the beginning of year	$ 58/unit
Current cost at the end of year	73/unit
	$131/unit
Average current cost ($131 ÷ 2)	$65.5/unit
Units sold during the year (000s) (par. 55(c))	× 3,136
Average current cost of goods sold (000s)	$205,408

62. The current cost amounts should be compared with the recoverable amount. This is

illustrated below:

Market price per unit at end of year	$85
Current cost per unit of inventory on hand at end of year	73
Excess—no write-down required	$12

Step 3: Analysis of Property, Plant, and Equipment and Depreciation

63. An analysis of property, plant, and equipment was given in paragraph 56.

Step 4: Current Cost of Property, Plant, and Equipment and Depreciation

64. It will usually be appropriate to calculate current cost depreciation, depletion, and amortization expense by reference to average current cost of the related assets (current cost of assets at beginning of year + current cost of assets at end of year ÷ 2).

	(000s) Current Cost
Current cost—12/31/X5 (par. 56(d))	$ 170,000
Current cost—12/31/X6 (par. 56(d))	220,000
	390,000
	÷ 2
Average current cost	$ 195,000
Current cost depreciation: 10%, straight line	$ 19,500

In this example, management has determined that the recoverable amount is greater than net current cost of property, plant, and equipment and there is no write-down.

Step 5: Identification of Net Monetary Items

65. Net monetary items (par. 54):

	(000s)	
	Dec. 31, 19X6	**Dec. 31, 19X5**
Cash	$ 1,000	$ 2,000
Accounts receivable	36,000	16,500
Accounts payable and accrued expenses	(47,000)	(32,000)
Income taxes payable	(6,000)	(6,000)
Current portion of long-term debt	(5,000)	(5,000)
Deferred income taxes	(6,000)	(5,000)
Long-term debt	(34,000)	(39,000)
Net monetary liabilities	($61,000)	($68,500)

Step 6: Computation of the Purchasing Power Gain or Loss on Net Monetary Items

66. The amount of net monetary items at the beginning of the year, changes in the net monetary items, and the amount at the end of the year are restated into average 19X6 dollars. The purchasing power gain or loss on net monetary items is then the balancing item as illustrated below:

	(000s) Nominal Dollars	Conversion Factor	(000s) Avg. 19X6 Dollars
Balance—1/1/X6	$ 68,500	298.4 (avg. 19X6) / 292.4 (Dec.19X5)	C$ 69,906
Decrease in net monetary liabilities during the year	(7,500)	*	(7,500)
Balance—12/31/X6	$ 61,000	298.4 (avg. 19X6) / 303.5 (Dec.19X6)	(59,975)
Purchasing power gain on net monetary items			C$ 2,431

Step 7: Computation of the Change in Current Cost of Inventory and Property, Plant, and Equipment and the Effect of General Price-Level Changes

67. The increase in current cost of inventories:

	(000s) Current Cost/ Nominal Dollars	Conversion Factor	(000s) Current Cost/ Avg. 19X6 Dollars
Balance—1/1/X6 (par. 55(b))	$58,000	298.4 (avg. 19X6) / 292.4 (Dec. 19X5)	C$ 59,190
Production (par. 55(c))	204,000	*	204,000
Cost of goods sold (par. 61)	(205,408)	*	(205,408)

Balance—12/31/X6 (par. 55(b))	(65,700)	298.4 (avg. 19X6) / 303.5 (Dec. 19X6)	(64,596)
Increase in current cost of inventories	$ 9,108		C$ 6,814

68. The inflation component of the increase in current cost amount is the difference between the nominal dollar and constant dollar measures. Using the numbers from paragraph 67:

	(000s)
Increase in current cost (nominal dollars)	$ 9,108
Increase in current cost (constant dollars)	C$ 6,814
Inflation component	2,294

69. The increase in current cost of property, plant, and equipment:

	(000s) Current Cost/ Nominal Dollars	Conversion Factor	(000s) Current Cost/ Avg. 19X6 Dollars
Balance—1/1/X6 (par. 56(d))	$74,100	298.4 (avg. 19X6) / 292.4 (Dec. 19X5)	C$ 75,621
Additions (par. 56(a))	15,000	*	15,000
Depreciation (par. 64)	(19,500)	*	(19,500)
Balance—12/31/X6 (par. 56(d))	(85,100)	298.4 (avg. 19X6) / 303.5 (Dec. 19X6)	(83,670)
Increase in current cost of property, plant, and equipment	$ 15,500		C$ 12,549

70. The inflation component of the increase in current cost amount is the difference between the nominal dollar and constant dollar measures. Using the numbers from paragraph 69:

	(000s)
Increase in current cost (nominal dollars)	$15,500
Increase in current cost (constant dollars)	C$12,549
Inflation component	2,951

Summary of Increase in Current Cost Amounts

71. Summarizing paragraphs 68 and 70 above:

	(000s)		
	Increase in Current Cost	**Inflation Component**	**Increase Net of Inflation**
Inventory	$ 9,108	2,294	C$ 6,814
Property, plant, and equipment	15,500	2,951	12,549
Total	$24,608	5,245	C$19,363

Check of Calculations

72. A reconciliation of shareholders' equity [10] (net assets) on a current cost/constant purchasing power basis acts as a check on the arithmetic accuracy of the calculations. Changes in shareholders' equity during 19X6 in average 19X6 dollars appear below:

	Source Paragraph	**(000s) Current Cost/ Average 19X6 Dollars**
Equity at January 1, 19X6		
Inventory	67	C$ 59,190
Property, plant, and equipment—net	69	75,621
Net monetary items	66	(69,906)
		64,905
Income from continuing operations	87	4,592
Dividends	57	(3,000)
Gain from decline in purchasing power of net monetary liabilities	66	2,431

Excess of increase in specific prices over increase in the general price level	71	19,363
		C$ 88,291
Equity at December 31, 19X6		
Inventory	67	C$ 64,596
Property, plant, and equipment—net	69	83,670
Net monetary items	66	(59,975)
		C$ 88,291

Sub Company Information

73. The functional currency financial statements of Sub Company [11] appear below:

Sub Company
Historical Cost/Nominal FC Balance Sheets

	(000s) December 31, 19X6	19X5
Cash	FC2,550	FC1,250
Equipment	2,500	2,500
Accumulated depreciation	750	500
Net equipment	1,750	2,000
Total assets	FC4,300	FC3,250
Accounts payable	FC 600	FC 500
Long-term debt	2,000	1,500
Total liabilities	2,600	2,000
Capital stock	500	500
Retained earnings	1,200	750
Total equity	1,700	1,250
Total liabilities and equity	FC4,300	FC3,250

Sub Company
Historical Cost/Nominal FC Statement of Income and Retained Earnings
For the Year Ended December 31, 19X6

	(000s)
Revenue	FC5,000
General and administrative expenses	3,500
Depreciation	250
Interest	350
	4,100
Income before taxes	900
Income taxes	450
Net income	450
Retained earnings—beginning of year	750
Retained earnings—end of year	FC1,200

74. The fixed asset was acquired on December 31, 19X4. It is depreciated on a straight-line basis over 10 years and is expected to have no salvage value. There were no acquisitions or disposals of assets during the year.

75. Exchange rates between the functional currency and the dollar are:

December 31, 19X5	FC1 = $1.20
Average 19X6	FC1 = $1.10
December 31, 19X6	FC1 = $1.00

76. Management has measured the current cost of equipment at December 31, 19X6 and 19X5 as follows:

	(000s)	
	19X6	**19X5**
Current cost	FC5,500	FC4,000
Accumulated depreciation	(1,650)	(800)
Net current cost	FC3,850	FC3,200

The recoverable amount has been determined to be in excess of net current cost at both dates.

77. Current cost equity in nominal FC at the beginning and end of the year may be computed by adding net monetary items and net property, plant, and equipment at current cost. To determine current cost equity in nominal dollars, those FC amounts are translated at the appropriate exchange rate:

	December 31					
	19X6			19X5		
	(000s) FC	Exchange Rate	(000s) $	(000s) FC	Exchange Rate	(000s) $
Monetary items (par. 73):						
Cash	FC2,550	$1	$ 2,550	FC1,250	$1.20	$ 1,500
Current liabilities	(600)	$1	(600)	(500)	$1.20	(600)
Long-term debt	(2,000)	$1	(2,000)	(1,500)	$1.20	(1,800)
Net monetary liabilities	FC (50)		$ (50)	FC (750)		$ (900)
Equipment—net (par. 76)	FC 3,850	$1	$ 3,850	FC3,200	$1.20	$ 3,840
Equity at current cost	FC 3,800		$ 3,800	FC2,450		$ 2,940

78. The U.S. and local general price level indexes are:

	Local	U.S.
December 19X5	144	292.4
Average 19X6	158	298.4
December 19X6	173	303.5

Sub Company Calculations: Translate-Restate Method

79. To apply the translate-restate method, amounts measured in nominal FC are first translated into their dollar equivalents. Changes in those dollar equivalent amounts are then restated to reflect the effects of U.S. inflation.

Current Cost Depreciation and Income from Continuing Operations

80. The first step is to determine current cost depreciation for the year as follows:

	(000s)
Current cost—beginning of year (par. 76)	FC4,000
Current cost—end of year (par. 76)	5,500
	9,500
	÷ 2
Average current cost, gross	FC4,750

Current cost depreciation expense for the year is FC475,000 (FC4,750,000 × 10%). Computation of current cost depreciation and income from continuing operations does not involve use of a general price level index if measurements are made in average-for-the-year currency units. Accordingly, reported current cost depreciation under the translate-restate method is C$E523,000 (FC475,000 x $1.10).

81. Income from continuing operations on a current cost basis is computed by simply replacing historical cost depreciation in income from continuing operations in the primary financial statements with the current cost amount. Accordingly, current cost income from continuing operations is:

Net income + historical cost depreciation – current cost depreciation

= FC450,000 (par. 73) + FC250,000 (par. 73) – FC475,000 (par. 80)

= FC225,000.

Reported current cost income from continuing operations under the translate-restate method is C$E247,000 [12] (FC225,000 × $1.10).

Excess of Increase in Specific Prices over Increase in General Price Level

82. The second step is to compute the change in the current cost of equipment and the effect of the increase in the general price level. To measure the increase in current cost of equipment in nominal FC dollar equivalents, the effect of the exchange rate change must be excluded. One way to accomplish this is to translate the December 31, 19X5 and 19X6 FC current cost amounts to dollar equivalents at the average exchange rate and then restate those dollar amounts to average 19X6 constant dollar equivalents:

	(000s) Current Cost/FC	Exchange Rate	(000s) Current Cost/$	Conversion Factor	(000s) Current Cost/C$E
Current cost, net—12/31/X5 (par. 76)	FC3,200	$1.10	$3,520	298.4 (avg.19X6) / 292.4 (Dec. 19X5)	C$E3,592
Depreciation (par. 80)	(475)	$1.10	(523)	*	(523)
Current cost, net—12/31/X6 (par. 76)	(3,850)	$1.10	(4,235)	298.4 (avg. 19X6) / 303.5 (Dec. 19X6)	(4,164)
Increase in current cost	FC1,125		$1,238		C$E1,095

The inflation component of the increase in current cost amount is the difference between the nominal dollar and the constant dollar equivalent amounts:

	(000s)
Increase in current cost (nominal dollars)	$ 1,238
Increase in current cost (constant dollars)	C$E1,095
Inflation component	143

Purchasing Power Gain or Loss on Net Monetary Items

83. The third step is to compute the purchasing power gain or loss on net monetary items. Under the translate-restate method, the translated beginning and ending net monetary liabilities are restated to average 19X6 dollars. The U.S. purchasing power gain is then the balancing amount:

	(000s) FC	Exchange Rate	(000s) $
Net monetary liabilities—12/31/X5 (par. 77)	FC750	$1.20	$900
Net monetary liabilities—12/31/X6 (par. 77)	50	$1.00	50
Decrease during the year	FC700		$850

	(000s) $	Conversion Factor	(000s) C$E
Net monetary liabilities—12/31/X5	$ 900	298.4 (avg. 19X6) / 292.4 (Dec. 19X5)	C$E918
Decrease during the year	(850)	*	(850)
Net monetary liabilities—12/31/X6	$ 50	298.4 (avg. 19X6) / 303.5 (Dec. 19X6)	(49)
Purchasing power gain			C$E 19

In some circumstances, the above procedure will include a part of the effect of exchange rate changes on net monetary items in the purchasing power gain or loss. A more precise computation that would completely exclude the effect of exchange rate changes would be to compute a separate purchasing power gain or loss for each functional currency operation in a manner similar to that illustrated in paragraph 82 for the increase in specific prices. For Sub Company, that alternative method produces a purchasing power gain of C$E18:

	(000s) FC	Average Exchange Rate	(000s) $	Conversion Factor	(000s) C$E
Net monetary liabilities—12/31/X5 (par. 77)	FC750	$1.10	$825	298.4 (avg.19X6) / 292.4 (Dec. 19X5)	C$E842
Decrease during the year	(700)	$1.10	(770)	*	(770)
Net monetary liabilities—12/31/X6 (par. 77)	FC 50	$1.10	55	298.4 (avg. 19X6) / 303.5 (Dec. 19X6)	(54)
Purchasing power gain					C$E 18

The first procedure illustrated is less costly because it can be applied on a consolidated basis, and it generally provides a reasonable approximation. Accordingly, that method is acceptable. For this exercise, the more precise computation is used.

Check of Calculations

84. A reconciliation of equity serves as a check of the calculations and is a convenient way to compute the translation adjustment:

	(000s)	
Equity at 12/31/X5 in average 19X6 C$—$2,940 (par. 77) × 298.4 / 292.4		C$ 3,000
Income from continuing operations (par. 81)	C$E247	
Purchasing power gain (par. 83)	18	
Excess of increase in specific prices over increase in general price level (par. 82)	1,095	
Translation adjustment (par. 85)	(624)	
Increase in equity in terms of U.S. purchasing power		736
		C$ 3,736
Equity at 12/31/X6 in average 19X6 C$—$3,800 (par. 77) × 298.4 / 303.5		C$ 3,736

Translation Adjustment

85. The preceding paragraph shows that the translation adjustment is the amount needed to balance the reconciliation of equity. The translation adjustment may be checked by computing the effect of changes in the exchange rate on beginning-of-year equity and on the increase or decrease in equity during the year. To check the translation adjustment determined under the translate-restate method: (a) translate the beginning- and end-of-year equity on a C$ basis into FC amounts and (b) use those FC amounts to compute the effect on equity of changes in the exchange rate.

	(000s) C$	Exchange Rate	(000s) FC
Equity at 12/31/X5 in average 19X6 C$ (par. 84)	C$3,000	$0.833 *	FC2,499
Equity at 12/31/X6 in average 19X6 C$ (par. 84)	3,736	$1.00	3,736
Increase in equity	C$ 736		FC1,237

	(000s)	
Beginning-of-year equity	FC2,499	
Exchange rate change during 19X6 ($1.20–$1.00)	× (.20)	$ (500)
Increase in equity	FC1,237	
Difference between ending exchange rate and average rate for 19X6 ($1.10–$1.00)	× (.10)	
		$ (124)
Translation adjustment		$ (624)

If the short-cut method for determining the purchasing power gain or loss described in paragraph 83 were followed, the translation adjustment would be $(625).

Consolidation: Translate-Restate Method

86. Parent Company prepares its changing prices disclosures on a consolidated basis and complies with the minimum requirements in determining current cost income from continuing operations (paragraph 32). Accordingly, revenue, general and administrative expenses, interest, and income taxes (paragraph 33) are shown at amounts reported in the historical cost financial statements. For Sub Company, those amounts are translated into dollars as follows:

	(000s) FC Amount (Par. 73)	Exchange Rate	(000s) U.S. Dollars
Revenue	FC5,000	1.10	$ 5,500
General and administrative expenses	FC3,500	1.10	$ 3,850
Interest	FC 350	1.10	$ 385
Income taxes	FC 450	1.10	$ 495

87. The "Total" column of the following schedule provides the figures in Schedule 2 of paragraph 45, "Illustrations of Disclosures."

	Source Par.	(000s) Parent Company	Source Par.	(000s) Sub Company	Total
Average 19X6 Units of Purchasing Power					
Net sales & other revenues	54	$270,000	86	$ 5,500	$275,500
Cost of goods sold	61	205,408			205,408
Depreciation expense	64	19,500	80	523	20,023
Selling, general, and administrative expenses	54	10,835	86	3,850	14,685
Interest expense	54	7,165	86	385	7,550
Provision for taxes	54	22,500	86	495	22,995
		265,408		5,253	270,661
Income (loss) from operations		$ 4,592		$ 247	$ 4,839
Purchasing power gain (loss)	66	$ 2,431		$ 18	$ 2,449
Increase in specific prices					
Inventory	71	$ 9,108	83		$ 9,108
Property, plant, and equipment	71	15,500	82	$ 1,238	16,738
		24,608		1,238	25,846
Effect of increase in general price level	71	5,245	82	143	$ 5,388
Increase in specific prices—net of inflation	71	$ 19,363	82	$1 ,095	$ 20,458
Translation adjustment			85	$ (624)	$ (624)
Net assets	72	$ 88,291	84	$ 3,736	$ 92,027
December 31, 19X6 Units of Purchasing Power					
Inventory	55	$ 65,700			$ 65,700
Property, plant, and equipment—net of accumulated depreciation	56(d)	$ 85,100	82	$ 4,235	$ 89,335

Sub Company Calculations: Restate-Translate Method

88. To apply the restate-translate method, the steps illustrated in paragraphs 79-85 are followed except that all restatements to reflect the effects of general inflation are made using the local general price level index before translation to dollar equivalents.

Current Cost Depreciation and Income from Continuing Operations

89. Current cost depreciation and income from continuing operations are FC475,000 and FC225,000, respectively, as determined in paragraphs 80 and 81.

Purchasing Power Gain or Loss on Net Monetary Items

90. To apply the restate-translate method, the FC amount of net monetary items at the

beginning of the year, changes in the net monetary items, and the amount at the end of the year are restated into average 19X6 CFC. The purchasing power gain or loss on net monetary items is then the balancing item:

	(000s) FC	Conversion Factor	(000s) CFC
Net monetary liabilities—12/31/X5 (par. 77)	FC750	158 (avg. 19X6) / 144 (Dec. 19X5)	CFC823
Decrease during the year	(700)	*	(700)
Net monetary liabilities—12/31/X6 (par. 77)	FC 50	158 (avg. 19X6) / 173 (Dec. 19X6)	(46)
Purchasing power gain			CFC 77

Excess of Increase in Specific Prices over Increase in General Price Level

91. Under the restate-translate method, the local index is used to restate the beginning and ending current cost FC amounts into average 19X6 CFC:

	(000s) Current Cost/FC	Conversion Factor	(000s) Current Cost/CFC
Current Cost net—12/31/X5 (par. 76)	FC3,200	158 (avg. 19X6) / 144 (Dec. 19X5)	CFC3,511
Depreciation (par. 89)	(475)	*	(475)
Current Cost, net—12/31/X6 (par. 76)	(3,850)	158 (avg. 19X6) / 173 (Dec. 19X6)	(3,516)
Increase in current cost	FC1,125		CFC 480

The inflation component of the increase in current cost amount is the difference between the nominal functional currency and constant functional currency amounts:

	(000s)
Increase in current cost (FC)	FC 1,125
Increase in current cost (CFC)	CFC 480
Inflation component	645

Check of Calculations

92. As with the translate-restate method, a reconciliation of equity acts as a check of the

calculations. A reconciliation of equity also is a convenient point at which to translate the functional currency amounts determined in the preceding paragraphs into dollar equivalents and is a convenient way to compute the translation and parity adjustments.

93. If beginning and ending equity are restated to average 19X6 CFC using the local index, the reconciliation of equity under the restate-translate method would be:

	(000s) CFC	Exchange Rate	(000s) CFC$
Equity at 12/31/X5 in average 19X6 CFC (FC2,450 (par. 77) × 158/144)	CFC2,688	1.20	CFC$3,226
Income from continuing operations (par. 89)	225	1.10	247
Purchasing power gain (par. 90)	77	1.10	85
Excess of increase in specific prices over increase in general price level (par. 91)	480	1.10	528
Translation adjustment (par. 94)	–		(616)
	CFC3,470		CFC$3,470
Equity at 12/31/X6 in average 19X6 CFC (FC3,800 (par. 77) × 158/173)	CFC3,470	1.00	CFC$3,470

Translation Adjustment

94. The translation adjustment is the amount needed to balance the CFC$ reconciliation of equity. The adjustment may be computed as (a) the change in exchange rates during the period multiplied by the restated amount of net assets at the beginning of the period plus (b) the difference between the average exchange rate for the period and the end-of-period exchange rate multiplied by the increase or decrease in restated net assets for the period. Accordingly, the translation adjustment under the restate-translate method is:

	(000s)	
Beginning-of-year equity (par. 93)	CFC2,688	
Exchange rate change during 19X6 ($1.20–$1.00)	× .20	
		$ (538)
Increase in equity (3,470–2,688)	CFC 782	
Difference between ending exchange rate and average rate for 19X6 ($1.10–$1.00)	× .10	
Translation adjustment		(78)
		$ (616)

Parity Adjustment

95. The reconciliation of equity in paragraph 93, in which beginning-of-year and end-of-year equity are stated in average 19X6 CFC, is needed to calculate the translation adjustment in CFC$. However, beginning- and end-of-year equity and the increase in equity must be stated in average 19X6 constant dollars in the supplementary current cost information. Beginning and end-of-year equity in average 19X6 constant dollars are C$3,000,000 and C$3,736,000, respectively, as computed in paragraph 84. Thus, the overall increase in U.S. purchasing power for the year is C$3,736,000 - C$3,000,000 = C$736,000. However, the reconciliation of equity in paragraph 93 indicates that the increase in equity for the year is CFC$244,000 (CFC$3,470,000 - CFC$3,226,000). The difference between C$736,000 and CFC$244,000 is the parity adjustment needed to adjust the ending net investment and the increase in the net investment to measures in average 19X6 constant dollars. Accordingly, the parity adjustment is C$736,000 - CFC$244,000 = $492,000. That amount represents (a) the effect of the difference between local and U.S. inflation from December 31, 19X5 average for 19X6 on the restatement of opening equity to average units plus (b) the effect of the difference between local and U.S. inflation from average for 19X6 to December 31, 19X6 the restatement of ending nominal dollar equity to average units:

	(000s)	
Beginning-of-year equity (par. 77)	$ 2.940	
Difference between local and U.S. inflation from 12/31/X5 to average 19X6 (158/144–298.4/292.4)	× 0.0767	
		$225
Equity at 12/31/X6 (par. 77)	3,800	
Difference between local and U.S. inflation from average 19X6 to 12/31/X6 (158/173–298.4/303.5)	× 0.0699	
		266
		491
Rounding difference		1
Parity adjustment		$492

For display purposes, the parity adjustment be combined with the $(616,000) translation adjustment (paragraph 94). Accordingly, the net translation adjustment disclosed in the supplementary current cost information prepared using the restate-translate method would be $(616,000) + $492,000 = $(124,000). The components of current cost information based on the restate-translate method thus would be:

		(000s)
Beginning-of-year equity—\$2,940 (par. 77) × 298.4/292.4		C\$3,000
Income from continuing operation—CFC225 (par. 89) × 1.10	CFC\$247	
Purchasing power gain—CFC77 (par. 90) × 1.10	85	
Excess of increase in specific prices over increase in general price level—CFC480 (par. 91) × 1.10	528	
Translation and parity adjustments	(124)	
Increase in equity in terms of U.S. purchasing power		736
End-of-year equity—\$3,800 (par. 77) × 298.4/303.5		C\$3,736

Monetary and Nonmonetary Items

96. Paragraphs 96-108 provide guidance on the interpretation of paragraphs 40-43 for the classification of certain asset and liability items as monetary or nonmonetary. The following table illustrates the application of the definitions to common cases under typical circumstances. In other circumstances the classification should be resolved by reference to the definitions. Paragraphs 96-108 are not intended to provide answers that should be followed regardless of the circumstances of the case. (Footnote reference is at the end of the table.)

	Monetary	Nonmonetary
Assets		
Cash on hand and demand bank deposits (dollars)	X	
Time deposits (dollars)	X	
Foreign currency on hand and claims to foreign currency [a]	X	
Securities:		
Common stocks (not accounted for on the equity method) Common stocks represent residual interests in the underlying net assets and earnings of the issuer.		X
Preferred stock (convertible or participating)	Circumstances may indicate that such stock is either monetary or nonmonetary. Refer to convertible bonds.	
Preferred stock (nonconvertible, nonparticipating) Future cash receipts are likely to be substantially unaffected by changes in specific prices.	X	
Convertible bonds	If the market values the security primarily as a bond, it is monetary; if it values the security primarily as stock, it is nonmonetary.	

Bonds (other than convertibles)	X		
Trading account investments in fixed-income securities owned by banks, investment brokers, and others (paragraphs 97 and 98)		X	
Accounts and notes receivable	X		
Allowance for doubtful accounts and notes receivable	X		
Variable-rate mortgage loans The terms of such loans do not link them directly to the rate of inflation. Also, there are practical reasons for classify ing all loans as monetary.	X		
Inventories used on contracts			They are, in substance, right to receive sums of money if the future cash receipts on the contracts will not vary due to future changes in specific prices. Goods used on contracts to be priced at market upon delivery are nonmonetary.
Inventories (other than inventories used on contracts) and commodity inventories (other than those described below)		X	
Commodity inventories whose values are hedged by futures contracts whose contract amounts have not been recorded in the financial statements			Refer to paragraphs 99 and 100.
Loans to employees	X		
Prepaid insurance, advertising, rent,and other prepayments			Claims to future services are nonmonetary. Prepayments that are deposits, advance payments, or receivables are monetary because the prepay ment does not obtain a given quantity of future services, but rather is a fixed-money offset.
Long-term receivables	X		
Refundable deposits	X		
Advances to unconsolidated subsidiaries	X		

Equity investment in unconsolidated subsidiaries or other investees		X
Pension, sinking, and other funds under an enterprise's control	The specific assets in the fund should be classified as monetary or nonmonetary. Refer to listings under securities above.	
Property, plant, and equipment		X
Accumulated depreciation of property, plant, and equipment		X
The unguaranteed residual value of property owned by a lessor and leased under direct financing, sales-type, and leveraged leases	Refer to paragraphs 101and 102.	
Investment tax credits that are deferred by a lessor as part of the unearned income of a leveraged lease	Refer to paragraphs 103 and 104.	
Portion of the carrying amount of lessors' assets leased under noncancellable operating leases that represent claims to fixed sums of money (paragraphs 105 and 106)		X
Cash surrender value of life insurance	X	
Purchase commitments—portion paid on fixed-price contracts An advance on a fixed-price contract is the portion of the purchaser's claim to nonmonetary goods or services that is recognized in the accounts; it is not a right to receive money.		X
Advances to supplier—not on a fixed-price contract Such advances are rights to receive credit for a sum of money, not claims to a specified quantity of goods or services.	X	
Deferred income tax charges [a] Offsets to prospective monetary liabilities	X	
Patents, trademarks, licenses, and formulas		X
Goodwill		X
Deferred life insurance policy acquisition costs [a] Such costs represent the portion of future cash receipts for premiums that is recognized in the accounts and are sometimes viewed as an offset to the policy reserve.	X	
Deferred property and casualty insurance policy acquisition costs related to unearned premiums		X

Other intangible assets and deferred charges		X
Liabilities		
Accounts and notes payable	X	
Accrued expenses payable (wages and so forth)	X	
Accrued vacation pay	If to be paid at the wage rates as of the vacationdates and if those rates may vary, accrued vacation payis nonmonetary.	
Cash dividends payable	X	
Obligations payable in foreign currency	X	
Sales commitments—portion collected on fixed-price contracts An advance received on a fixed-price contract is the portion of the seller's obligation to deliver goods or services that is recognized in the accounts; it is not an obligation to pay money.		X
Advances from customers—not on a fixed-price contract Such advances are equivalent to loans from customers and are not obligations to furnish specified quantities of goods or services.	X	
Accrued losses on firm purchase commitments	X	
In essence, these are accounts payable.	X	
Deferred revenue	If an obligation to furnish goods or services is in involved, deferred revenue isnonmonetary. Certain "deferred income" items ofsavings and loan associations are monetary.	
Refundable deposits	X	
Bonds payable and other long-term debt	X	
Unamortized premium or discount and prepaid interest on bonds or notes payable Such items are inseparable from the debt to which they relate—a monetary item.	X	

Convertible bonds payable Until converted, these are obligations to pay sums of money.	X	
Accrued pension obligations	Fixed amounts payable to a fund are monetary; all other amounts are nonmonetary.	
Obligations under warranties These are nonmonetary because they oblige the enterprise to furnish goods or services or their future price.		X
Deferred income tax credits [a] Cash requirements will not vary materially due to changes in specific prices.	X	
Deferred investment tax credits These are not to be settled by payment of cash and are related to nonmonetary assets.		X
Life insurance policy reserves These represent portions of policies' face values that are now deemed liabilities.	X	
Property and casualty insurance loss reserves	X	
Unearned property and casualty insurance premiums These are nonmonetary because they are principally obligations to furnish insurance coverage. The dollar amount of payments to be made under that coverage might vary materially due to changes in specific prices.		X
Deposit liabilities of financial institutions	X	
Minority interests in consolidated subsidiaries (paragraph 107)		X
Equity		
Capital stock of the enterprise or of its consolidated subsidiaries subject to mandatory redemption at fixed amounts (paragraph 108)	X	

97. *Trading account investments in fixed-income securities owned by banks, investment brokers, and others*. Trading account securities are securities of all types carried in a dealer trading account that are held principally for resale to customers. The predominant practice by banks is to carry these securities at market value. Trading account investments include both fixed-income securities (for example, nonconvertible preferred stock, convertible bonds, and other bonds) and other securities (for example, common stock). Usually, trading account

securities are held for extremely short periods of time—sometimes for only a few hours. Frequently, the enterprise buys and sells the securities expecting to make a profit on the difference between dealer and retail, or bid and ask, prices rather than on price changes during the period securities are held. However, the prices of the securities change with market forces.

98. Trading account investments in fixed-income securities are not claims to receive sums of money that are fixed or determinable. The market prices of the securities might and frequently do change while the securities are held. Generally, nonconvertible and nonparticipating preferred stock, convertible bonds that the market values primarily as bonds rather than as stocks, and nonconvertible bonds should be classified as monetary items. However, those classifications are based, in part, on the assumption that those securities would be held for long periods, if not to maturity. Trading account investments, on the other hand, are held for shorter periods and their value depends much less heavily on the general purchasing power of money and more on the specific values of the securities. Therefore, trading account investments in fixed-income securities should be classified as nonmonetary.

99. *Commodity inventories whose values are hedged by futures contracts*. Many enterprises hedge commodity inventories (such as grain or metals). *Short hedges* are designed to provide a degree of assurance that a decline in the price of the commodity would be offset by an increase in the value of the hedge contract. Short hedges thus tend to reduce the effects of price changes on the inventory that is hedged.

100. There are certain similarities between inventories that are hedged and inventories that are used on or committed to a fixed-price contract. In each case, the risk of gain or loss due to price changes before the inventory is sold is largely or entirely eliminated. To the extent that hedges fix the value of an inventory in dollars (or units of foreign functional currency, if appropriate), the inventory effectively becomes a monetary item.

101. *The unguaranteed residual value of property owned by a lessor and leased under direct financing, sales-type, and leveraged leases*. The unguaranteed residual value is included with the minimum lease payments, at present value, in the net investment in the lease.

102. The minimum lease payments are monetary items because they are claims to fixed sums of money. The residual value is not a claim to a fixed sum of money, so it is a nonmonetary item. Some assets and liabilities, of which the net investment in the lease is a good example, are combinations of claims to (or obligations of) fixed amounts and claims to (or obligations of) variable amounts. Ideally, those claims should be separated for purposes of classifying them as monetary and nonmonetary. However, if the information necessary to make the separation is not available or is impracticable to obtain, such items need not be divided into monetary and nonmonetary components and would be classified according to their dominant element. If the net investment in leases is principally claims to fixed amounts, it would be classified as monetary; it would be classified as nonmonetary if it is principally claims to residuals.

103. *Investment tax credits that are deferred by a lessor as part of the unearned income of a leveraged lease*. Under FASB Statement No. 13, *Accounting for Leases*, the deferred investment tax credit related to the leased asset is subtracted from rentals receivable and estimated residual value as part of the calculation of the lessor's investment in the leveraged lease. The investment, including the deferred investment tax credit related to the leveraged lease, is presented as one amount in the balance sheet. As indicated in paragraph 102, the investment in a leveraged lease would be classified as monetary or nonmonetary according to its dominant element.

104. As indicated in the table in paragraph 96, a deferred investment tax credit should be classified as nonmonetary but, if it is part of an investment in a leveraged lease and if the information necessary to separate its elements is not available or is impracticable to obtain, the investment would be classified according to its dominant element.

105. *Portion of the carrying amount of lessors' assets leased under noncancellable operating leases that represent claims to fixed sums of money*. These assets are carried at depreciated historical cost under generally accepted accounting principles and are classified with or near property, plant, and equipment, which are nonmonetary.

106. The classification of a lease as an operating lease under Statement 13 indicates that the lease has not transferred substantially all of the benefits and risks incident to ownership to the lessee. Thus, the economic significance of the asset continues to depend heavily on the value of the future lease rentals, residual values, and associated costs. Therefore, an asset subject to an operating lease should be classified as nonmonetary.

107. *Minority interests in consolidated subsidiaries*. The interests of minority shareholders in the earnings and equity of subsidiaries are, from the consolidated entity's point of view, claims that are not fixed. Rather, they are residuals that will vary based on the subsidiary's earnings, dividends, and other transactions affecting its equity and so are nonmonetary. (Refer to paragraph 108 as to classification of capital stock of the enterprise or of its consolidated subsidiaries subject to mandatory redemption at fixed amounts.)

108. *Capital stock of the enterprise or of its consolidated subsidiaries subject to mandatory redemption at fixed amounts*. Such securities are claims of the stockholders to a fixed sum of money and therefore are monetary. Classification as a monetary item called for in paragraphs 96-108 is only for purposes of determining a purchasing power gain or loss. Paragraphs 96-108 do not address how such securities should be classified in balance sheets or the accounting for dividends on those securities.

Appendix B

BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

CONTENTS

Paragraph Numbers

Appendix B: BACKGROUND INFORMATION AND BASIS FOR CONCLUSION

Introduction

109. This appendix summarizes considerations that were deemed significant by members of the Board in reaching the conclusions in this Statement. It includes reasons for accepting certain views and rejecting others. Individual Board members gave greater weight to some factors than to others.

Statement 33

110. In September 1979, the FASB issued Statement 33 in response to a perceived need for information on effects of changing prices on the reported results of operations and on selected assets of business enterprises. The Board recognized that two methods of providing the information had been advocated by a significant number of preparers, users, and auditors, that no clear preference existed for one method, and that neither method had been used extensively enough to judge its relevance or reliability. Accordingly, the Board required certain large publicly held companies to provide on an experimental basis certain financial information based on each of those methods. The methods required were restatements of information from the primary financial statements to reflect changes in (a) general price levels (historical cost/constant purchasing power information) and (b) both specific prices and general price levels (current cost/constant purchasing power information).

111. The Basis for Conclusions of Statement 33 discusses (a) why the primary financial statements provide only a limited view of effects of changing prices, (b) why those effects may not be understood adequately unless they are directly reflected in financial reports, (c) how information on those effects might be used, and (d) why the current cost/constant purchasing power and the historical cost/constant purchasing power methods were selected over alternative measurement methods as the basis for an experiment in reporting certain effects of changing prices. Because the Board concluded that alternative measures of enterprise performance could be helpful in assessing the ability of an enterprise to maintain its operating capability and its financial capital, Statement 33 required a minimum set of disclosures that reflected effects of changing prices and provided users with sufficient information to assess alternative performance measures.

112. To enhance experimentation and learning by preparers, users, and the Board, Statement 33 permitted alternative methods for measuring and displaying the effects of specific and general price changes. To limit the cost of implementing the requirements, Statement 33 required

information about only certain financial statement items that, for most of the enterprises covered, were likely to be most affected by changing prices. The Statement, therefore, required only selected data to be restated by the two methods.

Review of Statement 33

113. The Board committed itself to a comprehensive review of the experiment after a period of five years subsequent to the issuance date of Statement 33. In preparation for that review, the Board encouraged a wide range of research studies to learn about the experiences of preparers, users, and auditors with both historical cost/constant purchasing power information and current cost/constant purchasing power information. In July 1983, a task force was appointed to assist the Board in evaluating whether to continue the requirements after the initial five-year period and, if continued, what changes should be considered. The task force assisted in the preparation of an FASB Invitation to Comment, *Supplementary Disclosures about the Effects of Changing Prices*, which was designed to supplement the research studies by soliciting the advice of users, preparers, and auditors. The Board received approximately 400 responses to that document.

114. The research studies and responses to the Invitation to Comment indicated that the Statement 33 information was not widely used. Both the number of users and the extent of use were limited. A large number of responses to the Invitation to Comment suggested that the costs of preparing the disclosures had outweighed the benefits. Some respondents stated that although inflation is considered in assessing the results of operations, mandatory disclosure requirements were unnecessary because users have developed their own methods for making those assessments. Others advocated alternative disclosures and criticized the methods but not the objectives adopted in Statement 33. Still others supported either historical cost/constant purchasing power or current cost/constant purchasing power disclosures but argued that the presentation of the data, especially using two methods, had discouraged and confused some users.

115. With the knowledge gained from the experiment, the Board concluded that reducing the number of disclosures and simplifying the remaining requirements might enhance the usefulness of the information. The Board decided to eliminate the historical cost/constant purchasing power disclosure requirements of Statement 33 because of evidence that reporting effects of changing prices using two different methods detracted from the usefulness of the information and that the historical cost/constant purchasing power information was less useful than the current cost/constant purchasing power information. Statement 70, issued in 1982, eliminated the requirement to disclose historical cost/constant purchasing power information for enterprises that did not use the dollar as the functional currency for all significant operations. Statement 82, issued in 1984, eliminated the requirement for other enterprises.

The Current Cost Exposure Draft

116. In December 1984, the Board issued an Exposure Draft, *Financial Reporting and*

Changing Prices: Current Cost Information, that would have combined without significant changes all existing FASB pronouncements relating to reporting supplementary information on the effects of changing prices. Thus, it would have continued the disclosure of current cost information expressed in terms of constant monetary units. Certain disclosures related to mineral resource assets also would have been continued. Although the requirements for historical cost/constant purchasing power information were previously eliminated, such information could have been substituted for current cost/constant purchasing power information in certain circumstances. That proposed Statement would have differed from existing requirements in two respects. The five-year summary of selected financial data would have been stated in average-for-the-current-year units of purchasing power. The option in Statement 33 to use base-year dollars or the end-of-the-current-year U.S. Consumer Price Index would have been eliminated. In addition, a gain or loss on disposal or write-down of inventory or property, plant, and equipment that was included in income from continuing operations in the primary statements would have been adjusted to reflect the current cost basis of the item prior to its disposal or write-down when included in income from continuing operations on a current cost basis. The Board received comments from more than 100 respondents.

117. A large majority of respondents recommended that the Board discontinue the existing requirements. Many commented that the data did not appear to have been used by the institutional investment community, bankers, or investors in general. Numerous reasons were cited for nonuse. Some respondents believed that the data were not relevant or reliable (for reasons discussed further in paragraph 124). Others thought that comparisons of data between enterprises had been inhibited by the flexibility in methods of application, by differences in the quality of the raw data used to prepare the changing prices information, and by failure to disclose the assumptions used in preparing the data. Still other respondents expressed the view that the disclosures were overly complex and therefore difficult to understand. Some respondents commented that the manner of disclosing the information discouraged its use—the data were placed at the end of the financial information in annual reports, were labeled as supplementary and unaudited, were not adequately explained, and were not comprehensive. Further, some commented that the components of income adjusted for changing prices were not aggregated in a useful way. In addition to those views, the most frequently cited reason for discontinuing the supplementary disclosures was that the benefits derived from presenting that data had not been sufficient to justify the costs incurred. Although the Board is not persuaded that the cost of the disclosures required by Statement 33, as amended, *considered in isolation* was unduly burdensome, nevertheless, at the present time, the Board acknowledges that those disclosures did not achieve the cost-benefit relationship that had been anticipated for them.

118. Many respondents suggested that even an improved set of disclosures might not be useful because managements and investors had information better than or different from that required by Statement 33. Many respondents commented that the inflation rate had diminished and, therefore, interest in disclosures about the effects of inflation had decreased. Some commented that other factors were more important in investment decisions than information on changing prices, for example, the opportunity and ability to raise capital from outside sources to finance

replacements of productive capacity or the effects of interest rates on monetary assets and liabilities.

119. A minority of respondents said that the supplementary disclosures required by Statement 33, as amended, should be continued. The central theme of supporters of those disclosures was the need to overcome the inherent weaknesses of historical cost financial statements in and following periods of changing prices. In their view, those financial statements must be adjusted for the effects of inflation to report performance in real terms to help in assessing an enterprise's ability to maintain its financial capital. The effects of past inflation carry over into current and future financial statements; therefore, even at the present low levels of inflation, a large cumulative effect remains. Also, higher levels of inflation may return. Some commented that it was too early to abandon the experiment. They believed that users had not had enough time to adapt their methods to the data, that more years of data would increase the utility of the data for trend analysis, and that the experimental label, dual disclosures, and temporary availability of the data had discouraged use. They suggested that changes in those areas should be made.

Alternative Approaches Considered

More Limited Disclosures

120. During the second and third quarters of 1985, the Board addressed the issue of whether to continue the disclosure requirements. It considered a number of alternatives suggested by respondents. The Board concluded that adoption of any of those alternatives, such as a current cost/nominal dollar approach, a condensed current cost approach, or a replacement cost approach based on ASR No. 190, *Notice of Adoption of Amendments to Regulation S-X Requiring Disclosure of Certain Replacement Cost Data* (now rescinded), would not significantly reduce the cost to prepare the data. A few respondents recommended that the Board retain only a modest statistical display of changing prices information, for example, a requirement to disclose in average-for-the-year or end-of-year units of constant purchasing power (a) net sales and other operating revenues, (b) cash dividends declared per common share, and (c) market price per common share at year-end. Those respondents said that approach would provide some limited data at a reasonable cost, warning readers about the effects of changing prices. The Board recognizes that a limited display of data could result in substantial cost savings, but it doubts whether users would gain much from such limited data. Further, most users could develop those data independently. Other respondents suggested that the Board rescind the requirements and urge preparers to disclose on a voluntary, experimental basis information thought to be useful for a particular enterprise.

A Continuing Project to Develop Improved Disclosures

121. In October 1985, the Board decided to continue (a) a project to develop more effective and useful disclosures of the effects of general inflation and specific price changes on enterprise performance, resources, obligations, and equity and (b) the requirements of Statement 33, as

amended. Thus, enterprises were required to provide disclosures for 1985 pursuant to the same requirements that were in effect for 1984.

122. The principal goals of the project described in paragraph 121 would have been (a) to develop a comprehensive changing prices model that reflects both current price and general price-level adjustments of financial statement items and (b) to decide which aspects of that model were sufficiently relevant and reliable to be included as supplementary disclosures in financial reports. During early 1986, the Board considered the appropriate objectives, scope, and approach for that project in light of the four factors the Board generally considers in deciding whether to undertake a major technical project.

123. The first factor considered is the pervasiveness of the problem to be addressed. A determination is made concerning (a) the extent to which an issue is troublesome to users, preparers, auditors, or others, (b) the extent to which practice is diverse, and (c) the likely duration of the problem (that is, is it transitory or will it persist). The Board believes that the problems created by changing prices are pervasive. It is widely accepted that, in inflationary periods, historical cost financial statements for most capital-intensive enterprises show illusory profits, mask erosion of capital, and invalidate trend analysis. Although the Board believes current cost/constant purchasing power information may be useful, based on comment letters received, the information is of little interest at present, whether the problems are pervasive or not. Prior to the issuance of Statement 33, little information was disclosed about the effects of specific and general price changes on reported results of operations. During the period that pronouncement was effective, enterprises generally provided only the minimum disclosures required. In addition, since Statement 33 was designed as an experiment and permitted considerable flexibility, to some extent, diversity of practice was expected and accepted. Finally, interest in disclosures of the effects of changing prices on enterprise performance seems to build and to ebb depending on the severity of inflation. Despite the long-term effects of previous high inflation, during a period of low inflation, as exists now, the public has evidenced relatively little interest in the subject. As discussed previously in paragraphs 117 and 118, some respondents stated that the lack of interest in the supplementary disclosures stemmed from the inadequacies of the current cost disclosures and from preparers' and investors' ability to otherwise assess the effects of changing prices.

124. The second factor considered is the potential for developing an alternative solution—whether one or more alternatives that will improve the relevance, reliability, and comparability of financial reporting are likely to be developed. The Board believes a reason for the low level of acceptance of the current cost/constant purchasing power disclosures related to the perception that those disclosures were not sufficiently relevant or reliable for some or all enterprises. Some believe that the concept underlying current costs, that is, the cost of replacing existing service potential, is not relevant because many enterprises do not intend to, or physically cannot, replace an existing asset's service potential with another asset of comparable service potential. For example, an enterprise producing motion picture films or an enterprise exploring for oil and gas reserves could not duplicate its existing assets that have resulted from past

successful efforts. In addition, some believe that applying a specific price index to a historical cost number to compute the current cost of inventory and property, plant, and equipment may not produce a reliable measure of current cost because of technological or other changes over time that affect particular assets but that may not affect or have a significantly different effect on the basket of goods or services on which a specific price index is based. Although Statement 33, as amended, provided for adjusting current costs for such changes, the difficulty of accomplishing that adjustment is acknowledged. Likewise, in the absence of specific guidelines, the determination that current cost did not exceed the lower recoverable amount of a unit of property, plant, and equipment required the application of considerable judgment. In some cases, enterprises reported current cost holding gains during periods in which losses from continuing operations on a current cost basis were incurred. Some have questioned the reliability of such results. Developing specific guidelines on how to determine the lower recoverable amount of a unit of property, plant, and equipment used in a production process is a complex technical issue and would be a principal consideration in any project that addresses impairment of assets in the context of the primary financial statements. To date, there is no acknowledged solution. The difficulties described above were acknowledged in Statement 33. Their existence is not the only reason for the Board's decision. Even though there is a wide range of views, even among Board members, on what changes might improve the relevance and reliability of the disclosures that were required by Statement 33, as amended, it is possible that a technical solution eventually could be developed notwithstanding the fact that research and investigation already performed both in the U.S. and abroad has not identified a solution generally acknowledged to be both relevant and reliable. However, the effort necessary to develop a solution would take significant time and significant Board resources and its results likely would be more costly for preparers to implement than were the requirements of Statement 33, as amended. Further, as noted in paragraph 126, there is sufficient uncertainty about whether the eventual technical solution would receive general acceptance among preparers, users, and auditors. Accordingly, it is the Board's belief that attempting to solve the existing problems at this time would not meet any reasonable cost-benefit test.

125. The third factor addresses the technical feasibility of a project, that is, the extent to which a technically sound solution can be developed or whether the project under consideration should await completion of other projects. Statement 33 required presentation of an intermediate measure of performance (income from continuing operations) adjusted for certain effects of changing prices. It also required certain other disclosures (holding gains or losses and purchasing power gains or losses) that a user might consider in assessing aggregate enterprise performance. However, it did not require presentation of a "bottom line" alternative to net income. The further refinement of Statement 33 to require disclosure of an alternative "bottom line" measure of performance as envisioned by the project described in paragraph 122 would likely require the Board to readdress many complex issues of recognition and measurement that were considered as part of the conceptual framework, but that remain contentious and unresolved.

126. The last factor considers practical consequences, namely, whether an improved accounting

solution is likely to be generally acceptable and whether not addressing a particular subject might cause others to act, that is, the SEC or Congress. Without a clearer indication of what the alternative accounting solution might be, it is difficult to assess its likely acceptability. However, as noted earlier, it is probable that the solution would be more costly for preparers to apply and, therefore, would likely be resisted by them, given their experience with, and assessment of, Statement 33. At present, governmental interest in any requirement to continue the disclosures required by Statement 33, as amended, seems to have diminished.

127. Based on the assessments discussed in paragraphs 123-126, the Board decided, in June 1986, not to proceed with a project to develop a comprehensive changing prices model that reflects both current price and general price-level adjustments of financial statement items and concluded that the supplementary disclosures required by Statement 33, as amended, should not be required. The Board expects to address (as it has in the past) the relevance of current prices of assets or liabilities as part of its deliberations on major accounting issues. Those projects may result in Statements that require measurement or disclosure in the primary financial statements of assets or liabilities based on current prices and the effects of changes in those prices. The Board's consideration of the complex issues surrounding the broad issue of specific price changes does not cease with the issuance of this Statement.

Voluntary Disclosure

128. An FASB Exposure Draft, *Financial Reporting and Changing Prices*, was issued on September 30, 1986 that proposed making voluntary the disclosure of supplementary information on the effects of inflation and changes in specific prices. The Board received over 200 letters of comment in response to the Exposure Draft. Reiterating many of the comments made in response to the 1983 Invitation to Comment and 1984 Exposure Draft, a substantial majority of the respondents to the most recent Exposure Draft supported the elimination of the requirement for supplementary disclosure of information on the effects of changing prices. A large number of the respondents reasserted that although inflation is considered in assessing the results of operations, mandatory disclosure requirements are unnecessary because users have developed their own methods of adjusting information in the primary financial statements for changing prices. A large majority of respondents also suggested that the costs of preparing the disclosures have outweighed the benefits to date.

129. A small minority of respondents disagreed with the Exposure Draft's recommendation to rescind Statement 33 for reasons similar to those previously discussed in paragraph 119. Some respondents believed that insufficient time had been allowed for information on the effects of changing prices to be incorporated into user evaluations and that additional years of data were needed to allow for the assimilation of this information into user methods. Other respondents stated that the effects of past high inflation carry over into future financial statements even in times of relatively low inflation and therefore affect such statements. Some noted that the experimental label and short-term availability of the data had discouraged use. Still other respondents believed that if inflation returns, the Board will need to reimplement the

requirement. In that event, data comparison will be hampered by the lack on information on the effects of changing prices in the interim years. In addition, some respondents reiterated the view that one reason that the data were not used relates to the deficiencies of the current cost method.

130. The Board agrees with many of the concerns expressed by those few respondents that support continuance of a changing prices disclosure requirement. However, those concerns are not persuasive when considered in the light of what a large majority of respondents have stated about the general nonuse of the data. Further, the Board believes that any attempt to correct the deficiencies of the present changing prices disclosure requirements identified by many respondents would be so time-consuming and expensive that no reasonable cost-benefit relationship could be attained. That is especially true in view of the poor prospects that the Board believes now exist for increased use of supplementary changing prices data.

Footnotes

FAS89, Appendix A, Footnote 1--The combining of prior requirements retains the editorial style of the relevant FASB Statements, for example, the use of "shall" is retained even though the presentations and measurements described are now voluntary.

FAS89, Appendix A, Footnote 2--An enterprise that presents consolidated financial statements shall present the information required by this appendix on the same consolidated basis. The information required by this appendix need not be presented for a parent company, an investee company, or other enterprise in a financial report that includes the results for that enterprise in consolidated financial statements.

FAS89, Appendix A, Footnote 3--The information required by this appendix shall be presented as supplementary information in any published annual report that contains the primary financial statements of the enterprise except that the information need not be presented in an interim financial report. The information required by this appendix need not be presented for segments of a business enterprise although such presentations are encouraged.

FAS89, Appendix A, Footnote 4--Terms defined in paragraph 44 of this appendix are in **boldface type** the first time they appear in this appendix.

FAS89, Appendix A, Footnote 5--For the purposes of this appendix, except where otherwise provided, "inventory" and "property, plant, and equipment" shall include land and other natural resources and capitalized leasehold interests but *not* goodwill or other intangible assets.

FAS89, Appendix A, Footnote 6--As a practical matter, this option is not available to enterprises that measure a significant part of their operations in one or more functional currencies other than the U.S. dollar and that elect to use the restate-translate method (paragraph 39) for measuring inflation-adjusted current cost information.

FAS89, Appendix A, Footnote 7--The index is published in *Monthly Labor Review*. Those desiring prompt and direct information may subscribe to the Consumer Price Index press release mailing list of the Department of Labor. If the level of the Consumer Price Index at the end of the year and the data required to compute the average level of the index over the year have not been published in time for preparation of the annual report, they may be estimated by referring to published forecasts based on economic statistics or by extrapolation based on recently reported changes in the index.

FAS89, Appendix A, Footnote 8--If turnover is rapid and material amounts of depreciation are not allocated to inventory, cost of goods sold measured on a Last-In, First-Out (LIFO) basis may provide an acceptable approximation of cost of goods sold, measured at current cost, provided that the effect of any LIFO inventory liquidations (that is, any decreases in earlier years' LIFO layers) is excluded.

FAS89, Appendix A, Footnote 9--The choice of a measure of functional currency purchasing power should take into account the availability, reliability, and timeliness of a general price level index and the frequency with which it is adjusted. It is anticipated that an appropriate index of the change in the general price level will be available for most functional currencies. Indexes are published in most countries, and some indexes are published periodically by organizations such as the International Monetary Fund, the Organisation for Economic Co-Operation and Development, and the United Nations. However, in some cases indexes may not be available on a timely basis or may not be sufficiently reliable. In those circumstances, management should estimate the change in the general price level.

FAS89, Par. 45, Schedule 1, Footnote a--The condensed financial information in this exhibit compares selected information from the primary financial statements with information that reflects effects of changes in the specific prices (current cost) of inventory and property, plant, and equipment expressed in units of constant purchasing power. The current cost amounts for inventory and cost of goods sold reflect actual manufacturing costs incurred in 19X6. The current cost amounts for major components of property, plant, and equipment were determined by applying specific price indexes to the applicable historical costs. For assets used in U.S. operations, Producer Price Indexes and Factory Mutual Building Indexes were used; for assets used in foreign operations, appropriate indexes for each country were used. The current cost information is expressed in average 19X6 dollars as measured by the CPI-U.

FAS89, Par. 45, Schedule 1, Footnote b--The purchasing power gain on net amounts owed is an economic benefit to the enterprise that results from being able to repay those amounts with cheaper dollars.

FAS89, Par. 45, Schedule 1, Footnote c--During 19X6, the specific prices (current cost) of inventory increased by $9,108 and of property, plant, and equipment by $16,738. The total increase of $25,846 exceeded the increase necessary to keep pace with general inflation. At December 31, 19X6, the current cost of inventory was $65,700 and of property, plant, and equipment, net of accumulated depreciation, was $89,335 (both measured in December 31, 19X6 units of purchasing power). Those amounts are higher than the amounts in the primary statements of $63,000 for inventory and $45,750 for property, plant, and equipment, net of accumulated depreciation; therefore, it is reasonable to expect income from continuing operations on a current cost basis for 19X7 to remain significantly below that reported in the primary statements.

FAS89, Par. 45, Schedule 1, Footnote d--Current cost amounts for foreign operations are measured in their functional currencies, translated into dollar equivalents using the average exchange rate for the year, and restated into constant units of purchasing power using the CPI-U. Essentially, the foreign currency translation adjustment is the effect of changes in exchange rates during the year on shareholders' equity. The negative translation adjustment indicates that, overall, the dollar has increased in value relative to the functional currencies used to measure the foreign operations of the enterprise.

FAS89, Par. 45, Schedule 2, Footnote a--The condensed financial information in this exhibit compares selected information from the primary financial statements with information that reflects effects of changes in the specific prices (current cost) of inventory and property, plant, and equipment expressed in units of constant purchasing power. The current cost amounts for inventory and cost of goods sold reflect actual manufacturing costs incurred in 19X6. The current cost amounts for major components of property, plant, and equipment were determined by applying specific price indexes to the applicable historical costs. For assets used in U.S. operations, Producer Price Indexes and Factory Mutual Building Indexes were used; for assets used in foreign operations, appropriate indexes for each country were used. The current cost information is expressed in average 19X6 dollars as measured by the CPI-U.

FAS89, Par. 45, Schedule 2, Footnote b--The purchasing power gain on net amounts owed is an economic benefit to the enterprise that results from being able to repay those amounts with cheaper dollars.

FAS89, Par. 45, Schedule 2, Footnote c--During 19X6, the specific prices (current cost) of inventory increased by $9,108 and of property, plant, and equipment by $16,738. The total increase of $25,846 exceeded the increase necessary to keep pace with general inflation. At December 31, 19X6, the current cost of inventory was $65,700 and of property, plant, and equipment, net of accumulated depreciation, was $89,335 (both measured in December 31, 19X6 units of purchasing power). Those amounts are higher than the amounts in the primary statements of $63,000 for inventory and $45,750 for property, plant, and equipment, net of accumulated depreciation; therefore, it is reasonable to expect income from continuing operations on a current cost basis for 19X7 to remain significantly below that reported in the primary statements.

FAS89, Par. 45, Schedule 2, Footnote d--Current cost amounts for foreign operations are measured in their functional currencies, translated into dollar equivalents using the average exchange rate for the year, and restated into constant units of purchasing power using the CPI-U. Essentially, the foreign currency translation adjustment is the effect of changes in exchange rates during the year on shareholders' equity. The negative translation adjustment indicates that, overall, the dollar has increased in value relative to the functional currencies used to measure the foreign operations of the enterprise.

FAS89, Par. 45, Schedule 3, Footnote a--Net assets include inventory and property, plant, and equipment at current cost and all other items as they are reported in the primary financial statements. No adjustment has been made for the lower tax basis applicable to the current cost amounts included in net assets.

FAS89, Par. 45, Schedule 3, Footnote b--For purposes of this illustration, although the years for which information has been provided are nonspecific, the actual 1979-1983 average index numbers have been applied.

FAS89, Par. 45, Schedule 4, Footnote a--In average 19X6 dollars.

FAS89, Par. 45, Schedule 4, Footnote b--Net assets adjusted for specific price changes include inventory and property, plant, and equipment at current cost and all other items as they are reported in the primary financial statements. No adjustment has been made for the lower tax basis applicable to the current cost amounts included in net assets.

FAS89, Par. 45, Schedule 4, Footnote c--For purposes of this exhibit, although the years for which information has been provided are nonspecific, the actual 1979-1983 average index numbers have been applied.

FAS89, Par. 45, Schedule 5, Footnote a--The condensed financial information in this exhibit presents selected information that reflects effects of changes in the specific prices (current cost) of inventory and property, plant, and equipment expressed in units of constant purchasing power. The current cost amounts for inventory and cost of goods sold reflect actual manufacturing costs incurred in 19X6. The current cost amounts for major components of property, plant, and equipment were determined by applying specific price indexes to the applicable historical costs. For assets used in U.S. operations, Producer Price Indexes and Factory Mutual Building Indexes were used; for assets used in foreign operations, appropriate indexes for each country were used. The current cost information is expressed in average 19X6 dollars as measured by the CPI-U.

FAS89, Par. 45, Schedule 5, Footnote b-- Income from continuing operations reported in the primary financial statements was $22,995 for 19X6. Current cost income reported in the five-year summary was only $4,839 because depreciation expense on a current cost basis exceeded depreciation expense in the primary statements by $9,748 and current cost of goods sold was $8,408 greater than the amount reported in the primary statements.

FAS89, Par. 45, Schedule 5, Footnote c--The purchasing power gain on net amounts owed is an economic benefit to the enterprise that results from being able to repay those amounts with cheaper dollars.

FAS89, Par. 45, Schedule 5, Footnote d--During 19X6, the specific prices (current cost) of inventory increased by $9,108 and of property, plant, and equipment by $16,738. The total increase exceeded the increase necessary to keep pace with general inflation by $20,458. Net assets include inventory and property, plant, and equipment at current cost and all other items as reported in the primary financial statements (restated into average-for-19X6 dollars). No adjustment has been made for the lower tax basis applicable to the current cost amounts included in net assets. At December 31, 19X6, the current cost of inventory was $65,700 and of property, plant, and equipment, net of accumulated depreciation, was $89,335 (both measured in December 31, 19X6 units of purchasing power). Those amounts are higher than the amounts in the primary statements of $63,000 for inventory and $45,750 for property, plant, and equipment, net of accumulated depreciation; therefore, it is reasonable to expect income from continuing operations on a current cost basis for 19X7 to remain significantly below that reported in the primary statements.

FAS89, Par. 45, Schedule 5, Footnote e--Current cost amounts for foreign operations are measured in their functional currencies, translated into dollar equivalents using the average exchange rate for the year, and restated into constant units of purchasing power using the CPI-U. Essentially, the foreign currency translation adjustment is the effect of changes in exchange rates during the year on shareholders' equity. A negative (positive) translation adjustment indicates that, overall, the dollar increased (decreased) in value relative to the functional currencies used to measure the foreign operations of the enterprise.

FAS89, Par. 45, Schedule 5, Footnote f--For purposes of this exhibit, although the years for which information has been provided are nonspecific, the actual 1979-1983 average index numbers have been applied.

FAS89, Par. 54, Footnote †—1,500,000 shares outstanding.

FAS89, Par. 54, Footnote *—Investments in Sub Company is recorded at cost and is eliminated in consolidation. Parent Company does not issue separate unconsolidated statements.

FAS89, Par. 66, Appendix A, Footnote *--Assumed to be in average 19X6 dollars.

FAS89, Par. 67, Appendix A, Footnote *--Assumed to be in average 19X6 dollars.

FAS89, Par. 69, Appendix A, Footnote *--Assumed to be in average 19X6 dollars.

FAS89, Appendix A, Footnote 10--To facilitate the illustration of consolidated amounts in paragraph 87, investment in Sub Company has been excluded from net assets of Parent Company in this paragraph.

FAS89, Appendix A, Footnote 11--For simplicity, Sub Company is assumed to have a fixed asset but no inventory. The mechanics of restating inventory and cost of goods sold on a current cost basis are essentially the same as those illustrated for property, plant, and equipment.

FAS89, Appendix A, Footnote 12--Current cost income has been rounded down from $247,500 to $247,000. This is necessary because current cost depreciation was rounded up to $523,000 from $522,500 and current cost income is a remainder of this number.

FAS89, Par. 82, Appendix A, Footnote *—Assumed to be in average 19X6 C$E.

FAS89, Par. 83, Appendix A, Footnote *—Assumed to be in average 19X6 C$E.

FAS89, Par. 85, Appendix A, Footnote *— FC1 – $1.20 = $0.833

FAS89, Par. 90, Appendix A, Footnote*—Assumed to be in average 19X6 C$E.

FAS89, Par. 91, Appendix A, Footnote*—Assumed to be in average 19X6 C$E.

FAS89, Par. 96, Appendix A, Footnote a--Although classification of this item as nonmonetary may be technically preferable, the monetary classification provides a more practical solution for the purposes of computing the purchasing power gain or loss on a consolidated basis.