



USAID
FROM THE AMERICAN PEOPLE



New Partners Initiative Technical Assistance Project (NuPITA)

Foreign Currency Translation Guidelines

Background

Local procurement clauses of the '**Required as Applicable**' **Standard Provision #8** for non-US organizations; and **22CFR 228.40** for US-based organizations require that payments for goods and services supplied by local businesses, dealers, or producers be made in the local currency of the cooperating country.

USG-funded organizations may engage in foreign currency operations in two main ways:

- a) Firstly, recipients may enter into business transactions that are denominated in foreign currencies; the results of these transactions will need to be translated into the currency in which they report to the awarding agency (US dollars).
- b) Secondly, foreign operations may be conducted through a foreign sub-recipient which maintains its accounting records in a currency other than that of the prime recipient; in order to prepare consolidated financial reports, there is a need to translate the sub-recipient 's transactions into the currency used for reporting purposes of the prime.

Managing foreign exchange risk is a fundamental component in the safe and sound management of all organizations that have exposures in foreign currencies. It involves prudently managing foreign currency positions in order to control, within set parameters, the impact of changes in exchange rates on the financial position of the organizations.

Objectives of translation

Poor understanding of the impact of exchange rates on accounting and reporting can create additional losses and gains.

The translation of foreign currency transactions and financial statements should produce results which are generally compatible with the effects of rate changes on an organizations cash flows and its award; and also ensure that the financial statements present a true and fair view of the results of management actions.

Consolidated statements should reflect the financial results and relationships as measured in the foreign currency financial statements prior to the translation.

Procedures

The accounting policies for the organization's foreign currency management should be clearly documented so that they can be consistently and accurately applied in the various field offices.

The procedures which should be adopted when accounting for exchange rates are considered in two stages, namely:

- a) The preparation of the financial statements of an individual organization in the cooperating country; and
- b) The preparation of consolidated financial statements by the prime recipient's headquarters offices.

Prime Recipient

It is important that the prime recipient of the USG funds has a multi-currency accounting system which will allow for:

- Recording of transactions in the original/local currency (ie, the actual currency paid or received)
- Maintaining of non-USD currency balances in the ledger for all assets and liability accounts
- Generation of reports in original/local currency, USD equivalent or a reporting currency

During implementation, organizations enter into transactions which are denominated in local currencies of the cooperating country. The result of each transaction should normally be translated into US dollars at the exchange rate ruling at the time of transaction; other options may be:

- i) To use the actual rates, on a '**First-in first-out (FIFO)**' basis, given by the bank whenever a transfer is made to move funds from the dollar account to the local currency account. For example, a transfer is made of USD 10,000 at an exchange rate of 40 USH – all expenditures up to 400,000 USH are converted using the exchange rate of 40.
- ii) To use an **average** rate, preferably computed for the month, where the different rates of exchange for the period are added together and divided by the number of different rates for the same period. For example, rates of 40, 42, and 38 are added together and divided by 3 for an average monthly rate of 40. This is often used when rates do not fluctuate significantly.
- iii) To use a **weighted average** rate, where the different rates of exchange for the period are averaged with consideration of the USD amounts being transferred each exchange. For example, rates of 45, 50, and 65 for amounts of USD 15,000, 5,000, and 10,000 respectively for a weighted average of 52.5 (calculated by multiplying each rate by the USD amount transferred at that rate, adding the three subtotals together, and dividing by 30,000, the total USD transferred). This provides a more realistic rate for the translations, particularly if rates fluctuate significantly in a month.
- iv) To use a **certified weighted average** exchange rate from the organization's bank or other reliable source.

For scenarios ii-iv, exchange gains/losses will result during a reporting period. Recipients and contractors are required to separately account for any gains or losses on foreign currency exchange. An account code should be set up in the income section of the Chart of Accounts for Exchange Gains/Losses. At the end of each month, this account should be debited (for losses) or credited (for gains). Depending on the

stability of the US dollar and local currency, this account will fluctuate throughout the grantee's fiscal year. At the end of the fiscal year, the account balance will appear on the grantee's audited financial statements. Any gain on the currency exchange process must either be returned to USAID or reported to USAID then approval sought for it to be utilized to further program activities.

Sub-agreements

It is recommended that budgets in the sub-agreements with sub-recipients are drawn up in the local currency of the cooperating country. The benefits of doing this are:

- The sub-recipients can manage and monitor the progress of their budget since both the budget and the actual expenditure is denominated in the same currency.
- The sub-recipient does not have to deal with the complications of exchange losses and gains.

Consolidated financial statements

Financial reports for consolidation purposes should reflect the same method (s) used by the field offices that are operating in local currency. The consolidation process is a compilation transactions that reflect the activities of the in-country programs, whether the compilation is done on a quarterly or annual basis.

Quarterly and annual financial reports to USAID must be reported in US dollars. Therefore the prime recipients must convert local currency transactions for the time period back into US dollars. The following guidelines are recommended for the process:

- When converting local currency month end transactions into US dollars, use the same currency exchange rate used for converting US dollars into local currency for each month contained in the report (by using the same rate, there will not be an additional gain/loss).
- After converting each month back to US dollars, add all months together to obtain a total for the reporting period. It is not necessary to obtain an average for the three month or 12 month period.

Conclusion

US NGOs, per **Mandatory Standard Provision # 16**, must consult and receive guidance in writing from the USAID Mission Director in the cooperating country on the methodology for foreign currency conversions. If the mission is unable to provide guidance, it is recommended that an official letter is sent by the organization to the mission director with a copy to the AOTR and activity manager detailing how exchange rate conversions will be done and a copy of the letter is retained in the organization's files.

Non-US NGOs may also request guidance from the USAID and/or use organizational policy which needs to be well documented in the organization's financial manual.