

Guidelines for exchange rate management

Introduction

This document provides guidance to ForumCiv's cooperation partners on how to manage exchange rates in initiatives financed by the Swedish Partnership Program (SPP). It is important to have good routines and principles for exchange rate management in place to ensure a more cost-efficient use of development aid, facilitate compliance with agreements, and decrease the risk of unexpected currency losses.

These guidelines are aligned with ForumCiv's General Conditions Article 5 and Sida's guiding document "[Guidelines on the handling of Currency Exchange Gains and Losses](#)" with an increased focus on exchange rate effects when forwarding funds to partners in subsequent step.

The basics

Exchange rate = The value relation between two currencies. It is the current market price to buy one currency in exchange for another.

Exchange rate difference = Occurs when the relative value between two currencies changes.

Example:

Your organization has a bank account with 10 000 EUR.

If you sold the Euro on May 1st you would get 112 968 SEK with a rate of 11.2968. Your 10 000 EUR is therefore worth 112 968 SEK on May 1st.

If you sold the Euro on June 1st instead, you would get 116 365 SEK with an exchange rate of 11.6365. The same 10 000 EUR increase in value since May 1st and is now worth 3 397 SEK more.

In this example the relative value between EUR and SEK changed between May 1st and June 1st resulting in an exchange rate difference.

Differentiate exchange rate effects from gains and losses

It's important to differentiate "exchange rate effects" in subsequent step from "exchange rate gains and losses". In previous program periods under the Swedish Partnership Programme, ForumCiv has not differentiated clearly between these concepts. Instead, the terms exchange rate gains and losses have also been used for exchange rate effects. Further, ForumCiv's reporting requirements focused mainly on exchange rate effects.

Starting with the Swedish Partnership Program 2023-2027, cooperation partners must report both exchange rate effects as well as exchange rate gains and losses in ForumCiv-financed initiatives.

Exchange rate effect = Occurs when the budgeted income in a local currency is more or less than the actual amount received in local currency. This happens when the actual exchange rate differs from the budgeted reference rate. These effects can also be referred to as "unrealized" exchange rate gains/losses since they occur in relation to a budget estimate.

Exchange rate gain/loss = A "realized" gain or loss that is booked in the accounting system of an organization. Exchange rate gains and losses can arise in a number of different situations and are also handled differently depending on the accounting method used.

Examples:

Exchange rate effect

A Swedish organization is entering into a one-year agreement with their partner organization in Bolivia. The agreement stipulates a total granted amount of 500 000 SEK to the Bolivian partner organization.

At the time of preparing the agreement, the exchange rate between SEK and BOB (Bolivian Bolivianos) is 1.57. Thus 1.57 is used as the budgeted reference rate and the Bolivian organization sets a budget based on the assumption that they will receive 318 471 BOB.

However, when the funds are transferred to the partner in Bolivia, the exchange rate is 1.59 and the partner only receives 314 465 BOB. In other words, the partner in subsequent step has a negative exchange rate effect of 4 006 BOB (318 471 – 314 465). Consequently, the Bolivian partner will have to reduce their budget in BOB by 4 006. The budget in SEK is still the same (500 000 SEK).

In their financial report to ForumCiv, the Swedish organization reports this negative exchange rate effect. To convert the effect into SEK, the Swedish organization uses the actual exchange rate of the transfer date (1.59). Hence, -4 006 BOB converts into -6 370 SEK.

Exchange rate gains/losses

The Swedish organization gets an invoice of 1 000 EUR that they pay directly from their Swedish bank account.

Since the Swedish organization uses accrual-based accounting they book the cost on the date that they receive the invoice. The exchange rate on that date is 11.64. Hence, 1 000 EUR converts into 11 640 SEK.

But when the Swedish organization pays the invoice a few weeks later, the exchange rate is 11.44 so they pay only 11 440 SEK and has consequently made an **exchange rate gain** of 200 SEK. The gain will be booked in the organizations accounting system.

In their financial report to ForumCiv, the Swedish organization reports the exchange rate gain of 200 SEK.

How to manage exchange rate effects

As described in the example above, an exchange rate “effect” (in subsequent step) will occur when the budgeted income in a local currency is more or less than the actual amount received in local currency. Since exchange rates fluctuate daily, initiatives are very likely to have exchange rate effects.

Exchange rate effects are “unrealized” gains/losses and are usually not booked in any accounting system. Even though they are referred to as unrealized, exchange rate effects can have significant impact on the operations of partners in subsequent step. For example, if a partner in subsequent step receives less income than planned, they may have to reduce the size or number of planned activities. And if they receive more funds than planned, they may have to adapt the initiative as well.

This section goes through how to manage exchange rate effects (in subsequent step) in SPP-financed initiatives – from budgeting and signing agreements to transferring funds and reporting to ForumCiv.

When preparing the application budget

- Before the application is submitted to ForumCiv, the partner in subsequent step(s) prepares a budget in local currency. This is then converted into SEK before adding the costs of the Cooperation partner in Sweden.
- When setting the budget, discuss the difference between fixed and variable costs. Fixed costs cannot be adjusted that easily. If the budget contains only budget lines with fixed costs, the possibility to adapt is more difficult.
- Have a dialogue with your partner about possible exchange rate effects on the project.
- As the application process takes time, monitor possible currency fluctuations between SEK and the local currency. If currency fluctuations impact the application budget, contact your handling Programme Officer.

Before signing agreement with partner in subsequent step

- Discuss how to prioritize if the amount received will be higher or lower than planned. It's good to discuss different scenarios when entering into an agreement.
- Make sure that you sign the agreement in SEK so that you do not risk having to pay your partner more funds than you have if the SEK loses value against the local currency.
- Attach a budget in both SEK and local currency, using a budget reference rate. (See tips in the box below on setting and updating the budget reference rate).

Budget reference rate – Tips of routines and good practices

The budget reference rate is the exchange rate included in the agreement budget with the partner in subsequent step. It is the rate used to convert the budget in local currency into SEK.

The budget reference rate has a big impact on the exchange rate effect. If the rate is far off track it will result in large exchange rate effects. Therefore, it's important to have good routines when setting and updating the budget reference rate, for example:

- Use a reliable currency converter such as www.xe.com and www.Oanda.com.
- Compare the rate on more than one currency converter.
- Have a systemized routine for setting the budget reference rate (e.g. the average rate for the latest month or the rate from the first day of the month when the agreement is signed).
- Include reference rate decimals, for example use 7.66 rather than rounding off to 8.
- Update the rate if it takes more than a month between the preparation of the budget and the signing of the agreement. If such updates impact the agreement budget with ForumCiv, contact your handling Programme Officer.
- If the budget covers several years, update the budget in local currency annually with a revised budget reference rate. If such updates have an impact on your agreement budget with ForumCiv, then ForumCiv's written approval is needed.

Example: Budget reference rate

A Swedish organization is entering into a two-year agreement with their partner organization in Kenya. The agreement stipulates a total granted amount of **846 461 SEK**.

At the time of preparing the agreement, the exchange rate between SEK and KES is 0.077. Thus, **0.077** is used as the **budgeted reference rate** and based on this, the organization in Kenya sets a

budget based on the assumption that they will receive 5 065 000 KES during the first year and 5 928 000 KES during the second year.

BUDGET	YEAR 1			YEAR 2			TOTAL	
	Budget (SEK)	(budget reference rate)	Budget (KES)	Budget (SEK)	(budget reference rate)	Budget (KES)	Budget (SEK)	Budget (KES)
Annual Conference	169,400	0.077	2,200,000	169,400	0.077	2,200,000	338,800	4,400,000
Networking meetings*3	17,325	0.077	225,000	17,325	0.077	225,000	34,650	450,000
Project coordinator	92,400	0.077	1,200,000	95,172	0.077	1,236,000	187,572	2,436,000
Project assistant	69,300	0.077	900,000	71,379	0.077	927,000	140,679	1,827,000
Office costs	41,580	0.077	540,000	41,580	0.077	540,000	83,160	1,080,000
Evaluation				61,600	0.077	800,000	61,600	800,000
Total	390,005		5,065,000	456,456		5,928,000	846,461	10,993,000

Transferring funds to partner in subsequent step

When transferring funds to your partner:

- Use the international banking system or national bank unless an alternative method has been approved by ForumCiv.
- Always confirm the amount received with a bank statement from your partner.
- Any bank fees that are charged during the transfer should be booked as costs and should not affect the calculation of the actual exchange rate.
- Save documentation of transfers so that you can follow up and report on sums transferred and received, exchange rates and exchange rate effects.
- Do not transfer more funds than needed. If, at the end of the initiative, your partner has unused funds, you risk making a realized exchange loss that you will have to reimburse through own means.

Example: Transferring funds

Continuing the example from above, when the Swedish organization transfers the first disbursement to their Kenyan partner, the exchange rate between the currencies has changed from the budget reference rate (0.077) to 0,075.

After the second disbursement during Year 1, the partner organization has received more money in KES than what they planned for ($5\,271\,301 - 5\,065\,000 = 206\,301$ KES). The currency fluctuations between KES and SEK have resulted in a positive “exchange rate effect” for the organization in Kenya.

TRANSFER OF FUNDS Y1	Transferred (SEK)	Received (KES)	Exchange rate (actual rate)	Budget (KES)	Difference: Received-Budget (KES)
First disbursement Y1	195,002	2,600,027	0.075	2,532,494	67,533
Second disbursement	195,003	2,671,274	0.073	2,532,506	138,768
Subtotal Y1	390,005	5,271,301	0.074	5,065,000	206,301

After the second disbursement Year 2 the organization has received less money in KES than what they originally planned for ($5\,706\,592 - 5\,928\,000 = -221\,408$ KES), resulting in a negative “exchange rate effect”.

TRANSFER OF FUNDS Y2	Transferred (SEK)	Received (KES)	Exchange rate (actual rate)	Budget (KES)	Difference: Received-Budget (KES)
First disbursement Y2	228,228	2,817,630	0.081	2,964,000	-146,370
Second disbursement	228,228	2,888,962	0.079	2,964,000	-75,038
Subtotal Y2	456,456	5,706,592	0.080	5,928,000	-221,408

After the final transfer each year: Update the budget in local currency

After the final disbursement of each year, remember to ask your partner for an updated budget in local currency that equals the total amount received for that year (including any carry-over funds from previous years).

Each budget update needs your written approval. If a budget update in your agreement with the Partner in subsequent step impacts the agreed budget with ForumCiv, ForumCiv's written approval is needed. Please refer to the SPP Procedures Manual for information on budget changes.

Example: Updating the budget

The partner organization in Kenya received an additional 206 301 KES during year 1, compared to their budget (a positive exchange rate effect). Now, the organization needs to specify how they want to use the funds and update the budget accordingly.

REVISED BUDGET	YEAR 1				
	Original budget (SEK)	Original budget (KES)	Revised budget (KES)	Variance (KES)	Comment
Annual Conference	169,400	2,200,000	2,200,000	0	
Networking meetings*3	17,325	225,000	331,301	106,301	One additional networking meeting
Project coordinator	92,400	1,200,000	1,200,000	0	
Project assistant	69,300	900,000	900,000	0	
Office costs	41,580	540,000	540,000	0	
Peace conference preparations			100,000	100,000	Conference including local travel costs
Evaluation				0	
Total	390,005	5,065,000	5,271,301	206,301	

Report actual costs (converted into SEK)

When it's time to prepare the financial report to ForumCiv, you must convert the actual costs in local currency into SEK and report them to ForumCiv.

If there is an outgoing balance in an ongoing initiative, discuss with your partner if and how that can be used in the following year and ask for a budget update.

If there is an outgoing balance after the last year of the initiative, it should be repaid to ForumCiv according to the agreement.

Different methods to convert actual costs into SEK

There are several different methods to convert actual costs in local currency into SEK. Depending on the method, the outcome in SEK might differ slightly. ForumCiv recommends that you use either the "Weighted Average Rate" or the "First in, First out"-method.

In the examples below you can see that the outcome in SEK varies slightly depending on which conversion method is used.

Weighted average annual rate

The weighted average annual rate is calculated by dividing the total sum transferred in SEK by the total sum received in KES during the reported period. The actual average annual exchange rate for the total amount transferred to the partner in Kenya is 0.074 for year 1 (390 005 / 5 271 301).

The total outcome in SEK using the weighted average method is 387 612 SEK.

WEIGHTED AVERAGE	Transferred (SEK)	Received (KES)	Exchange rate	Outcome (KES)	Outcome (SEK)
First disbursement Y1	195,002	2,600,027	0.075		
Second disbursement Y1	195,003	2,671,274	0.073		
Total sums and average rate Y1	390,005	5,271,301	0.074	5,238,006	387,612

First in, First out (FiFo)

With the FiFO method, the exchange rate for each transfer is used to convert costs into SEK until the whole transferred amount is spent.

Costs up to the amount of 2 600 027 KES is converted to SEK with the rate from the first disbursement 0,075. The remaining costs from the first year (2 637 979 KES) are converted to SEK with rate 0.073. The total outcome in SEK using the FiFo method is 387 574 SEK.

First in First out (FiFo)	Transferred (SEK)	Received (KES)	Exchange rate	Outcome (KES)	Outcome (SEK)
First disbursement Y1	195,002	2,600,027	0.075	2,600,027	195,002
Second disbursement Y1	195,003	2,671,274	0.073	2,637,979	192,572
Total sums and average rate Y1	390,005	5,271,301	0.074	5,238,006	387,574

Example: Weighted average annual rate

The Swedish organization decides to use the weighted average annual rate (0,074) to convert the total outcome in KES into SEK. The total outcome of 5 238 006 KES converts to 387 612 SEK.

COSTS YEAR 1	YEAR 1					
	Revised budget (KES)	Outcome (KES)	Variance %	Comment to variances over 10%	Exchange rate (weighted average)	Outcome (SEK)
Annual Conference	2,200,000	2,200,000	0.00%		0.074	162,800
Networking meetings*3	331301	302,506	-8.69%		0.074	22,385
Project coordinator	1,200,000	1,140,500	-4.96%		0.074	84,397
Project assistant	900,000	950,000	5.56%		0.074	70,300
Office costs	540,000	525,000	-2.78%		0.074	38,850
Peace conference reparations	100,000	120,000	20.00%	Forgot to include VAT	0.074	8,880
Total	5,271,301	5,238,006	-0.63%			387,612
Outgoing balance		33,295 KES				

Since the partner organization in Kenya has an outgoing balance of 33 295 KES, they hand in an updated budget for the second year to their Swedish partner, showing how they wish to spend this balance.

Report exchange rate effects

It's important that cooperation partners report exchange rate effects (in subsequent step) in their annual financial reports, since it helps ForumCiv evaluate the initiative.

You should report the exchange rate effect converted into SEK in the financial report to ForumCiv.

Example: Reporting exchange rate effects

In the financial report for year 1, the Swedish organization reports an exchange rate effect of +15 195 SEK and in the financial report for year 2, they report an exchange rate effect of -17 784 SEK.

The effects are calculated against the original budget in KES. To convert the exchange rate effect from KES to SEK, the organization uses the weighted average annual rate.

EXCHANGE RATE EFFECTS	Transferred (SEK)	Received (KES)	Exchange rate (weighted average)	Original Budget (KES)	Difference: Received-Budget (KES)	Difference: Received-Budget (SEK)
YEAR 1	390,005	5,271,301	0.074	5,065,000	206,301	15,195
YEAR 2	456,456	5,706,592	0.080	5,928,000	-221,408	-17,784

How to manage exchange rate gains and losses

The risk that the Cooperation Partner in Sweden will be greatly affected by “realized” exchange rate gains and losses is rather limited for ForumCiv-financed initiatives as the agreement with ForumCiv uses the same currency as your accounting currency, SEK.

Exchange rate gains and losses are referred to as “realized” gains and losses and they should be booked in your accounting system. They can arise in a number of different situations and are handled differently depending on which accounting method you use. The most common accounting methods are:

- Accrual-based accounting method (Revenues are recorded when earned and expenses are recorded when incurred – regardless if they have been received or paid.)
- Cash-based accounting method (Revenues and expenses are recorded when cash is received and paid.)

- Modified cash-based accounting method (a hybrid between accrual and cash-based).

Gains and losses can for example arise when:

- Revaluating assets and liabilities in foreign currency
- Invoices in foreign currency are booked and paid on two different dates.

Examples:

Revalue assets:

Your organization has an EU-funded program and you receive an income of 10 000 EUR on May 1st.

The amount will be booked in the accounting system with the rate from that day (10,35) 103 500 SEK.

Unfortunately, the project implementation is delayed and by December 31st you still have the amount of 10 000 EUR on your bank account.

You will now revalue the asset with the rate for December 31st (11.14). The asset amounts to 111 400 SEK and you book an exchange rate gain of 7 900 SEK.

Invoices in foreign currency:

Your organization gets an invoice of 1 000 EUR that you pay directly from your Swedish bank account.

Since you use accrual-based accounting you book the cost on the date that you receive the invoice. The exchange rate on that date is 11.64. Hence, 1 000 EUR converts into 11 640 SEK.

But when you pay the invoice a few weeks later, the exchange rate is 11.44 so you only pay 11 440 SEK and has consequently made an **exchange rate gain** of 200 SEK. You book the gain in your accounting system.

Basic accounting principles

When booking exchange rate differences into the accounts, follow these basic accounting principles:

International Accounting Standard (IAS) 21:

- Transactions shall be booked in the organization's "accounting currency". An organization's "*accounting currency*" is the currency used in the accounts. This means that an organization's income and expenses in currencies other than the accounting currency must be converted to the accounting currency.
- Exchange rate transactions must be recorded at the transaction date.
- Exchange rate differences should be recognized directly as a gain or loss in the income statement.
- Exchange rate gains and losses should be recorded as they occur during the agreement period.

General Accounting Principles:

- Currency exchange gains and losses should be reported on separate income and loss accounts.
- Currency exchange rate differences should be recognized and reported on in the accounting records in the period in which they arise.

- The value of assets and liabilities at the end of the financial year shall be re-evaluated using the closing rate of exchange.

Report exchange rate gains and losses

You must report the balance of exchange rate gains and losses annually in the financial report to ForumCiv. You may offset exchange rate gains against losses *during* the implementation of an initiative. If the balance represents an exchange rate gain at the end of the initiative period, you should include it in the closing balance and reimburse it to ForumCiv along with any other unused funds. However, ForumCiv will not cover any exchange losses in the event that the closing balance is negative at the end of the Initiative Period.

Example: Exchange rate gains/losses

Let's say that the partner organization in Kenya in the example above is at the end of the two-year initiative. They have an outgoing balance of **484 856 KES**, which converts to **38 447 SEK** when using the weighted average rate.

The outgoing balance in KES is the sum that the local organization must transfer to the Swedish organization who then will repay the sum to ForumCiv.

TOTAL INCOME AND COSTS	KES	Exchange rate (weighted average)	SEK
Total income Y1	5,271,301	0.074	390,005
Total income Y2	5,706,592	0.080	456,456
Total income	10,977,893		846,461
Total costs Y1	5,238,006	0.074	387,612
Total costs Y2	5,255,031	0.080	420,402
Total costs	10,493,037		808,014
Outgoing balance	484,856		38,447

However, when the Kenyan organization transfers the amount of 484 856 KES to their Swedish partner, the exchange rate has changed again, and the amount received in the Swedish organizations bank account is only 27 637 SEK. As a result. the Swedish organization has made an exchange rate loss of 10 810 SEK, which they will have to pay for through own means.

TRANSFER OF BALANCE	Transferred (KES)	Budgeted repayment (SEK)	Actual repayment (SEK)	Exchange rate loss/gain (SEK)
	484,856	38,447	27,637	-10,810

Fraud risks in exchange rate management

As mentioned in this Guideline, many risks are linked to exchange rate management. Some may even involve serious forms of fraudulent behavior.

It is therefore very important that all transactions can be linked to the implementation of the initiative and thus be deemed necessary.

Fraud risks that may arise in currency contexts may, for example, be linked to unnecessary currency exchanges, counterfeit bank statements, improper use due to differences between official and unofficial exchange rates, where changes in official currency are stated in the accounts while the actual exchange takes place using the more favorable unofficial, and non-verifiable, rate. If this continues during a longer period, considerable amounts may be misappropriated. It is therefore important to pay due attention to abnormal events and to be able to make reasonable assessments related to currency management on an ongoing basis.

Agreement conditions

Agreement conditions related to exchange rate fluctuations are found in FomCiv's General Conditions Article 5.

5.1 If the Grant is exchanged into a currency other than the currency of the Agreement, the currency exchange shall be made through the international banking system or national bank, unless otherwise approved by ForumCiv.

5.2 Currency exchanges shall be systematic and reasonable, based on the context of the Project activity. Transactions must be necessary for the implementation of the Project.

5.3 If exchange rate fluctuations diminish the value of the Grant to such an extent that it affects the implementation of the Project, the cooperation partner shall inform ForumCiv as soon as possible.

5.4 Exchange gains may be offset against exchange losses during the implementation of the Project. However, a balance shall be established for each year in the financial report. If the balance represents exchange gains at the end of the Project Period, this part shall be included in the closing balance and thus be part of the unused funds to be reimbursed to ForumCiv in accordance with Article 17.1 of these General Conditions. However, ForumCiv shall not cover any exchange losses in the event the closing balance is negative at the end of the Project Period.

5.5 The balance of exchange gains/losses detailed in the financial report shall be audited annually in accordance with the audit instructions for the Agreement.

FAQ (Frequently asked questions)

Why must our partner set the budget in local currency, when the agreement is in SEK?

The budget should be based on information, experience and price comparison from the country and context where the activities will take place. The budget should be presented in a format that enables your analysis; is the annual budget reasonable in relation to the expected results? If the budget is not presented in local currency, it's difficult to assess if the costs are reasonable for the country and context.

Why do we have to report exchange rate effects?

When evaluating if an initiative turned out as planned, the actual amount available is vital. If your partner received less funds than planned, were they able to implement all activities? If your partner received more funds than planned, were they able to adapt and spend it in a good way? Lessons learned and strategic decisions can be drawn if we see that an initiative is very affected by exchange rate fluctuations.