19.1 Foreign Currency Translation

Policy Statement

It is the policy of the Province of Nova Scotia to report the accounts of the province in Canadian dollars. The effects of transactions, expenses, assets, and liabilities that are denominated in foreign currencies are translated to Canadian dollars.

Policy Objectives

The objective of this policy is to express foreign currency transactions in a manner that is consistent with domestic transactions (Canadian dollar basis).

The policy will conform to generally accepted accounting principles (GAAP) for the Public Sector for foreign currency translations.

This policy supports the following corporate objectives:

- consistency of currency used
- flexibility to incur foreign currency transactions
- fiscal responsibility
- accountability
- compliance with Public Sector GAAP
- need to manage foreign currency transactions
- enhanced measurement of cost of foreign transactions
- improved information to support long-term planning

Application

This policy applies to all transactions throughout the departments and public service votes, but primarily to the Capital Markets Administration Group and the Liability Management and Treasury Services (LMTS) group.

All other public sector entities related to the Province of Nova Scotia are encouraged to adopt a GAAP-compliant foreign currency translation policy and apply it as soon as is practical.

It is recognized that many entities may already have an appropriate policy in place.

All areas/entities to which this policy is applicable are responsible for implementation and operation of an internal control system that ensures that foreign currency transactions are accounted for in accordance with this policy.

Policy Directives

INCLUSIONS

The policy applies to the following:

- debt denominated in a foreign currency
- sinking fund assets and earnings held in same currency as the related debt
- sinking fund assets and earnings held in Canadian dollars for debt of foreign currencies
- foreign currency denominated fund assets and earnings of the Public Debt Retirement Fund (PDRF)

EXCLUSIONS

The following transactions are excluded:

- foreign currency effects of swaps.

ACCOUNTING

Debt

Foreign currency debt is originally converted to Canadian dollars at the currency translation rate in effect on the date of issue, the historical rate.

The balance of foreign currency debt is translated to Canadian dollars at year-end using the current rate, the rate in effect as at the balance sheet date. The gain/loss caused by the change in the current rate is deferred and amortized over the remaining life of the debt on a straight-line basis.

Where a swap is attached to the debt, the final foreign currency translation gains/ losses are essentially fixed at the swap rate. At each year-end, the swap rate, not the current rate, is the translation rate used to translate the foreign debt into Canadian dollars. Any gains/losses are amortized over the remaining life or until settlement of the debt.

Sinking Funds Held in Foreign Currency

Foreign currency sinking funds are established to provide funds for foreign currency—denominated debt retirement/settlement.

Instalments to sinking funds are recorded in Canadian dollars, translated at the currency translation rate in effect on the date of payment.

The foreign currency value of all sinking fund instalments and withdrawals are translated to Canadian dollars at the current rate at each year-end date. Sinking fund earnings are earned throughout the year and therefore are translated to Canadian dollars using an average rate for the year. The gain/loss caused by changes in the current rate is deferred and amortized over the remaining life of the sinking fund investments on a straight-line basis.

Sinking fund income is recorded at the currency translation rate in effect when earnings are allocated.

Sinking Funds Held in Canadian Dollars for Foreign Currency Debt
Since the transactions for these sinking funds are already recorded in Canadian dollars, no translation is required. No exchange gains/losses are generated by these funds.

Amortization of foreign exchange ceases when the monetary item is settled. Any unamortized amounts would be recognized into net income immediately.

In the case of replacement debt, any unamortized foreign exchange gains/losses are not fully recognized into net income immediately but continue to be amortized over the remaining life of the replacement debt.

Policy Guidelines

Debt management decisions will have significant impact on future operations in the form of amortization charges. LMTS considers the impact that any refinancing or changes to existing debt structures may have on annual amortization costs. Given that future foreign currency translation rates are not easily predicted or controllable, amortization charges represent a non-discretionary cost once debt decisions are made. Amortization charges for foreign exchange gains and losses extend to future years.

Budgeting should reflect the multi-year nature of foreign currency translation amortization charges.

Accountability

CAPITAL MARKETS ADMINISTRATION, DEPARTMENT OF FINANCE
Capital Markets Administration is responsible to

- account for foreign currency transactions and monetary items in accordance with this policy
- monitor policy and recommend changes to the policy as necessary
- maintain detailed information on all deferred foreign exchange gains/losses
- record amortization of foreign exchange gains/losses
- report foreign currency denominated monetary items and transactions appropriately on the financial statements of the province

LIABILITY MANAGEMENT AND TREASURY SERVICES (LMTS), DEPARTMENT OF FINANCE

LMTS is responsible to

- monitor policy and recommend changes to the policy as necessary
- recognize the impact of debt-management decisions on the operating budget (i.e., amortization charges)
- determine the most appropriate sources and terms of financing
- ensure that proper control of foreign currency monetary items is maintained

GOVERNMENT ACCOUNTING, DEPARTMENT OF FINANCE

Government Accounting is responsible to

- coordinate the annual audit with Capital Markets Administration , LMTS and the auditors
- update this policy in consultation with Capital Markets Administration and LMTS

Monitoring

LMTS, Capital Markets Administration and Government Accounting of the Department of Finance are responsible for monitoring the application and audit of this policy.

References

Public Sector Accounting Board (PSAB) Handbook

Appendices

Appendix 19-A	Definitions
Appendix 19-B	Public Sector Accounting Board Handbook References

Note: These appendices are an integral part of this policy.

Enquiries

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Appendix 19-A

Definitions for Province of Nova Scotia

AMORTIZATION
The process of allocating costs over the estimated or known life of the monetary item to match costs with the revenues or public services that they help generate. The method of amortization used should best match the costs of the associated revenues or expenses.

CURRENCY RISK
Currency risk is the risk of changes in the value of an asset or liability due to changes in exchange rates.

FAIR VALUE
Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

FOREIGN CURRENCY TRANSACTIONS
Transactions denominated in a currency other than Canadian dollars.

FOREIGN EXCHANGE GAINS AND LOSSES
Result when a foreign currency denominated monetary item is settled or translated at an exchange rate different from that at which it was previously recorded or carried. The exchange gain or loss would be included in net income except when the monetary item has a fixed or ascertainable life extending beyond the end of the following fiscal year, in which case the exchange gain or loss would be deferred and amortized over the remaining life of the related monetary item.

HEDGE ACCOUNTING
Hedge accounting is a method for recognizing the gains, losses, revenues and expenses associated with the items in a hedging relationship, such that those gains, losses, revenues and expenses are recognized in operations in the same period when they would otherwise be recognized in different periods.

HEDGE EFFECTIVENESS

Hedge effectiveness is the extent to which changes in fair value or cash flows of a hedged item relating to the foreign exchange risk being hedged and arising during the term of a hedging relationship are offset by changes in fair value or cash flows of the corresponding hedging item related to the foreign exchange rate and arising during the same period.

HEDGED ITEM

Hedged item is all or a specified portion of an asset, a liability, or a group of similar assets or liabilities having an identified foreign exchange risk exposure that a government has taken steps to modify.

HEDGING ITEM

Hedging item is all or a specified portion of an asset, a liability or group of similar assets or liabilities modifying the foreign exchange risk exposure identified in the hedged item.

HEDGING RELATIONSHIP

Hedging relationship is a relationship established by government between a hedged item and a hedging item, including a synthetic instrument relationship.

HISTORICAL RATE

The foreign currency exchange rate in effect at the date of issue of the debt. It becomes the basis for any future gains and losses as the exchange rates fluctuate.

MONETARY ITEMS

Cash and claims to cash, the value of which, in terms of the monetary unit, whether foreign or domestic, is fixed by contract or otherwise.

REPLACEMENT DEBT

Issued to replace original debt that has been paid out. The terms are essentially the same, such that it is really a continuation of the original debt. The currency denomination and creditors are the same. The present value of future cash flows is substantially the same, not more than 10 per cent difference from the original expected cash flows.

SYNTHETIC INSTRUMENTS

Synthetic instruments are monetary items that are artificially created through the use of other monetary or derivative items in combination to emulate the characteristics and behaviour of a specific monetary item.

SYNTHETIC INSTRUMENT ACCOUNTING

Synthetic instrument accounting is a method of accounting for the assets and liabilities in a synthetic instrument relationship as though they were the item being emulated.

Appendix 19-B

Public Sector Accounting Board Handbook References

Accounting

INITIAL RECOGNITION

PS2600.10

At the transaction date, each asset, liability, revenue or expense arising from a foreign currency transaction of the government should be translated into Canadian dollars by apploying the exchange rate in effect at that date, except as noted in paragraph PS 2600.40.

SUBSEQUENT REPORTING DATES

PS2600.13

At each reporting date, monetary assets and liabilities denominated in a foreign currency should be adjusted to reflect the exchange rate in effect at the reporting date and be recognized in the statement of the financial position.

EXCHANGE GAINS OR LOSSES

PS2600.16

The foreign exchange gain or loss relating to a long-term foreign currency denominated monetary item should be recognized in the financial statements and deferred and amortized to income/expense over the remaining life of the monetary item.

SETTLEMENT

PS2600.19

An exchange gain or loss of the government that arises on settlement of a foreign currency denominated monetary item should be recognized in the statement of operations for the current period.

Presentation

PS2600.24

The unamotized foreign exchange gain or loss should be separately reported on the statement of financial position as an offset or addition to the related monetary item.

Hedging of Foreign Currency Items

PS2600.29

When hedge accounting is used, counterbalancing gains and losses that result from the translation of the components of a foreign currency hedging relationship should be recognized in the statement of operations in the same period(s).

PS2600.32

A foreign currency hedging relationship qualifies for hedge accounting only when all of the following conditions are satisfied:

a) At the inception of the hedging relationship, the government:
   - i) identifies the nature of the specific risk exposure(s) being hedged in accordance with its risk managment objective and strategy; and
   - ii) designates that hedge accounting will be applied to the hedging relationship.

b) At the inception of the hedging relationship, the government has formal documentation of:
   - i) its risk management objective and strategy for establishing the relationship;
   - ii) the hedging relationships, identifying the hedged items, the related hedging items and the intended term of the hedging relationships;
   - iii) the method for assessing the effectiveness of the hedging relationship; and
   - iv) the method for recognizing in operations the gains, losses, revenues and expenses associated with the items in the hedging relationship.

c) Both at inception of the hedging relationship and throughout its term, the government expects it to be effective and consistent with the originally documented risk management objective and strategy. Accordingly,
   - i) the effectiveness of the hedging relationship should be reliably measureable, which requires that the effects of the risk exposure being modified be reliably measurable for each hedged item and each hedging item; and
   - ii) the hedging relationship should be assessed on a regular periodic basis over its term to determine that it has remained, and is expected to continue to be, effective. [JAN. 2003]

PS2600.40

When synthetic instrument accounting is used for foreign currency denominated items, the Canadian dollar equivalent of the synthetic instrument at initial recognition and at subsequent reporting dates is established by the rate implied by the terms of the hedge(s).

Disclosure

PS2600.48

The government should disclose the following:

a) the government's policy for managing foreign currency risk, including a general description of the nature of the hedges undertaken to mitigate the government's currency exposure, the government's method for assessing hedge effectiveness, and information about the magnitude of hedging activities;
b) the Canadian dollar equivalent of the unhedged foreign denominated monetary items at the reporting date by major currency;
c) the Canadian dollar equivalent of the aggregate amount, by major currency, estimated to be required in each of the next five years and thereafter to meet sinking fund or retirement provisions for the foreign denominated debt;
d) the exchange gains or losses that have been recognized in the statement of operations; and
e) a sensitivity analysis illustrating the impact on the unhedged foreign currency denominated monetary item of foreign exchange rate changes.