



**Statement of reasons for the
update of CEMLA's Statites on
October 12, 2022**

Introduction

Recent events have evidenced the need to amend the Statutes of the Center for Latin American Monetary Studies (CEMLA), to allow, on the one hand, to manage its membership, attending to the needs and convenience of its Members; and, on the other hand, to ensure that the institution's accounting information reflects its economic and financial reality, with truthfulness, clarity and transparency.

With respect to membership management, it should be clarified that the current Statutes establish the possibility for central banks and related institutions to join CEMLA as Associate Members; however, the conditions for the cancellation of their membership are not provided for, an aspect that must necessarily be considered.

With respect to accounting information, there are no clear rules regarding the validity of debts due to non-payment of CEMLA's membership dues and, consequently, accounts receivable may accumulate indefinitely. Both the Audit Committee and CEMLA's external auditors have issued recommendations to address this problem, since it not only has an impact on the accounting information, with "inflated" and growing accounts receivable that distort the Center's financial reality, but also on the determination of the amount payable (deferred) of Income Tax (ISR) and Employee Profit Sharing (PTU). It is therefore essential to address this issue, which is intended to be resolved by amending the Statutes.

Recommendation of the Audit Committee of CEMLA

For the past four years, from 2018 to 2021, CEMLA has not received the payment of the membership fee from the *Banco Central de Venezuela* (BCV), given the restrictions that such central bank currently faces¹. This has led CEMLA's management, as well as the Audit Committee,

¹ On May 21, 2018, the Lima Group, formed by the governments of Argentina, Brazil, Canada, Chile, Colombia, Costa Rica, Guatemala, Guyana, Honduras, Mexico, Panama, Paraguay, Peru and Saint Lucia, reiterated the pronouncement contained in the Lima Declaration and agreed that the competent authorities of each country, issue and update circulars or bulletins at the national level to inform the financial and banking sector of the risk they could incur if they carry out operations with the Venezuelan government that do not have the approval of the Venezuelan National Assembly, including payment agreements and reciprocal credits for foreign trade operations -including military and security goods. In such virtue, on May 23, 2018, a joint communiqué was issued by the Ministry of Finance and Public Credit, the National Banking and Securities Commission, the National Insurance and Bonding Commission and the National Commission of the Retirement Savings System in which:

"warn entities operating under Mexican financial legislation, about the risks of entering into transactions with persons or subjects, created or originated by the Constituent Assembly of Venezuela that are considered invalid by international organizations and consistent with the Lima Declaration, taking into account that this could violate the regulations applicable to such entities and jeopardize the achievement of the operations entered into in contravention of the above determinations, to the detriment of the general public."

Thus, the *Banco Central de Venezuela*, despite the fact that in 2019 it tried to make the payment of its quota in favor of CEMLA, was rejected by BBVA Bancomer in Mexico.

to analyze the implications of the prevalence of this situation for an indefinite period and/or the possibility of similar cases arising in the future.

Article 8 of CEMLA's Statutes establishes the rights and obligations of the Associate Members. On the other hand, Article 11 grants each Associate a voice and vote in the deliberations of the Assembly. In the latter case, it is also established that "Associate Members who have paid their dues for the previous and preceding fiscal year may vote in the Assembly", being this statement the only one that refers to the loss of a right.

Based on the foregoing, the BCV retained its voting rights until 2019, when it participated in the appointment of the Board of Governors. As of that date, after two years of not receiving its quota, the vote of the BCV has not been requested for any of the subsequent decisions of the Assembly.

Likewise, taking as a reference the period of non-payment for two years for the loss of voting rights established in the Statutes, it is considered that, upon non-compliance with the payment obligation, the rights conferred by Article 8 are cancelled, which are understood to be subject to the fulfillment of its obligations, a situation that prevails to date.

Being an Associate Member of CEMLA, BCV continues to accumulate debt with the Center for its membership fee, in an amount equivalent to 421,587 US dollars (USD) each passing year, which, according to the Audit Committee, could have accounting and tax implications for CEMLA.

In view of this, the Audit Committee instructed CEMLA's General Management to study in depth the situation of the membership of BCV given the non-payment of its quota for the last four years and the accumulation of the corresponding accounts receivable. It also requested the General Management to examine the effect of the possible exit of BCV as a member of CEMLA; the treatment of the accounts receivable in tax terms, specifically, their impact on the determination of deferred income tax and employee profit sharing; and to approach the authorities of BCV to know their position and explore possible solutions, whether definitive or transitory.

Recommendation of the external auditors

On June 18, 2021, as a result of the audit performed by Castillo, Miranda y Compañía, S. C. to CEMLA's financial statements for fiscal years 2019 and 2020, a recommendation was issued in relation to the current policy of allowance for doubtful accounts.

The auditor found a significant balance of accounts receivable and its corresponding allowance for doubtful recovery, due to non-payment of dues from the Banco Central de Venezuela. Although CEMLA has a written policy that establishes when the allowance for doubtful accounts

arising from extraordinary events should be estimated, it does not specify the period in which they will remain in effect, which results in the accumulation of balances that cannot be removed from the financial information.

Thus, it is suggested that the policy for estimating doubtful accounts be supplemented to establish in detail the times or conditions in which these accounts receivable should be applied or written off, analyzing each of the assumptions under which the fee was estimated, in order to avoid having a portfolio of accounts receivable that is very old and indefinite and with significant balances.

Accounting and tax repercussions on CEMLA's financial statements due to the debt of the *Banco Central de Venezuela*

As of December 31, 2021, CEMLA has recognized in its financial statements deferred income tax of 215,757 USD and deferred PTU (participation of workers in utilities) of 85,094 USD, derived, among other items, from temporary differences between the book values and the tax values of the balance of fees receivable from the Banco Central de Venezuela.

For tax purposes, CEMLA is taxed on a cash flow basis, which means that it accrues its income until it is effectively collected; whereas, for accounting purposes, such fees are considered income in the year in which they should have been received, regardless of whether they have been collected or not.

This situation generates temporary differences in accordance with NIF D-4 "Income taxes", since although the book value of accounts receivable is zero (under Mexican financial reporting standards, an allowance for doubtful accounts is recognized equal to 100% of the uncollected installments), the value for tax purposes is the amount of the fees receivable from the Banco Central de Venezuela (1,686,348 USD at December 31, 2021), which should be accrued to income tax for income tax purposes at the time they are collected, which will generate a payment of such tax to be paid to the tax authorities.

Under these considerations, for accounting purposes, with the eventual elimination of the balance of the fees receivable from the Banco Central de Venezuela, given the impossibility of receiving payment thereof due to the restrictions that such central bank currently faces, the deferred tax previously determined would decrease as the temporary difference that originated it would disappear, and this effect would be reflected in CEMLA's financial statements.

With respect to the tax aspect, the derecognition of the balance of the fees receivable from the Venezuelan central bank would not generate any tax payment, since, as mentioned above, CEMLA accrues its income for tax purposes until the collection of such income. As long as CEMLA

does not receive the payment of the corresponding overdue installments, no income tax payment will be generated.

Finally, with respect to deferred PTU, the accounting and tax effect is the same as for deferred tax; i.e., the amount previously determined would be reduced in the financial statements and, for tax purposes, there would be no obligation to pay the employees as long as the corresponding installments are not collected, since PTU is determined on the taxable income for the year.

The objective of accounting is to reasonably show the financial situation of the entity, and therefore it is not advisable to keep accounts in CEMLA's financial statements that visibly show a practical impossibility of collection. A good practice is to derecognize from the accounts receivable balances that cannot be recovered and prevent them from continuing to accumulate indefinitely, generating uncertainty in the information presented.

To this end, a proposal to amend Article 8 of CEMLA's Statutes was presented to the Center Assembly, as described below, and was approved at its October 12, 2022 session in Washington, D.C., USA.

Proposed amendment to the New Statutes (last amendment in 2021)

Article 8 of CEMLA's Statutes describes the rights and obligations of Associate Members. Evidently, the fulfillment of the obligations, which include "contributing to the support of the Center with the contributions agreed by the Assembly", gives rise to the possibility of enjoying the rights, such as having access to activities and services organized by the Center, among others.

The wording of Article 8 suggests that failure to comply with the obligations entails the impossibility of enjoying the services offered by CEMLA, among other rights. However, in the case that gives rise to propose an amendment to this article, this has not been the case. In practice, the Banco Central de Venezuela exercised its rights for up to two years without the corresponding payment of its quotas; subsequently, the following two years in which CEMLA did not receive its quota, it did not have access to services either.

The unprecedented nature of this situation makes it necessary to establish a procedure to address this and any other similar contingency that may arise. That is why the proposed amendment to Article 8 of CEMLA's Bylaws establishes the maximum term in which an Associate Member may continue to access the benefits of its membership even without paying its dues, accumulating a debt for an amount equivalent to up to two years of dues, after which the membership will be

cancelled and may only be recovered through the payment of a reinstatement fee, equivalent to the total amount of the outstanding debt.

In this way, it is intended to avoid the indefinite accumulation of accounts receivable balances in CEMLA's financial statements, which, as already mentioned, prevents showing the real financial situation of the institution when it is evident that it is impossible to collect in the short or medium term, and benefits the Member by preventing the accumulation of debts for services not received.

Thus, Article 8 would read as follows:

Article 8. The Associates of the Center have the following rights and obligations:

- a) Be represented in the Assembly and propose any amendment to these Statutes through the Governing Board;
- b) Participate in the election of the Governing Board as well as be part of it.
- c) Have access to the activities and services organized by the Center in accordance with the programs approved by the Governing Board.
- d) Contribute to the maintenance of the Center with the contributions agreed by the Assembly.
- e) Provide the Center with effective and permanent assistance in obtaining reports for conducting its investigations and in general for the achievement of its purposes.
- f) Participate in monitoring the activities of the Center.

When the Associate, for two consecutive years does not comply with the obligation to cover the payment of its fee, the rights established in this Article will be suspended and its membership will be canceled; which may be recovered by paying a reinstatement fee to CEMLA equivalent to two years of his/her last dues as an Associate Member.