

# Accounting Aspects of International Reserves and Gold

## *Banco de la República de Colombia*



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# Agenda

1. Introduction
2. Accounting Framework of Central Bank.
3. Accounting policies of the Central Bank applicable to financial instruments, particularly to:
  - The Investment Portfolio of the International Reserves.
  - Gold



# 1. Introduction

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# Introduction

The purpose of this presentation is to describe the accounting practices applied by the Central Bank to financial instruments that are part of the international reserves and the treatment of gold.



# Accounting Framework applied by the Central Bank

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# Accounting framework of *Banco de la República*

Until 2014

## Sources of Accounting Regulation based on the following Standards:

- Issued by the National Government
- Provided by the Office of the Financial Superintendent for entities in the financial sector and the Central Bank.
- As per the Law and the Bylaws of the Central Bank.

Since 2015

Framework based on IFRS

## Modernization of the Accounting Framework of the Central Bank

- Act 1314 of 2009

Starts the process of convergence to IFRS in Colombia.

Accounting model for *Banco de la República*

IFRS with exceptions:

- Joint study between the National Accountant General for the public sector and the Office of the Financial Superintendent of Colombia (FSC).

Norms that are contrary to its special regime (as per the Law and the Bylaws of the Central Bank).

Treatment of credit portfolio and its deterioration. (Special rules issued by the FSC are applied).

**The Central Bank does not produce any explicit statement of compliance with IFRS.**



# **Accounting Policies of the Central Bank applicable to Financial Instruments**



# Treatment of Financial Instruments

Financial instruments are classified depending on their intent and capability of management, addressing the following premises:

1. The characteristics of the contractual cash flows of a financial asset (its existence).
2. How the entity manages its financial assets (Business Model).

## Classification and Recognition

### Management Model and Characteristics of the Instrument

### Classification

### Recognition of Gains and Losses

Assets held for contractual cash flows in future dates, throughout the life of the instrument more than to sell the instrument before the due date.

Amortized Cost  
(Effective Interest Rate Method)

Result of the period

Assets for short term sale and benefits of change in fair value (fair value gains).

Fair value with changes in results

Period Results

Assets held for obtaining (i) contractual cash flows and (ii) to be sold prior to maturity, but not in the short term.

Fair value with changes in OCI / Equity

Results of the period

- TIR yields
  - Realized Results
  - Deterioration
- Equity (OCI)
- Market Variations





# International Reserves

## Concept

## Characteristics

### International Reserves (IR)

#### Definition and Characteristics

The IR are assets abroad controlled by the monetary authority, which:

- (i) Are under the direct and effective control of the monetary authority and,
- (ii) Are available for immediate use.

#### Objective

To maintain an adequate level of assets in foreign currencies, available to intervene in the foreign exchange market and facilitate access of the public and private sector to international capital markets.

#### Composition

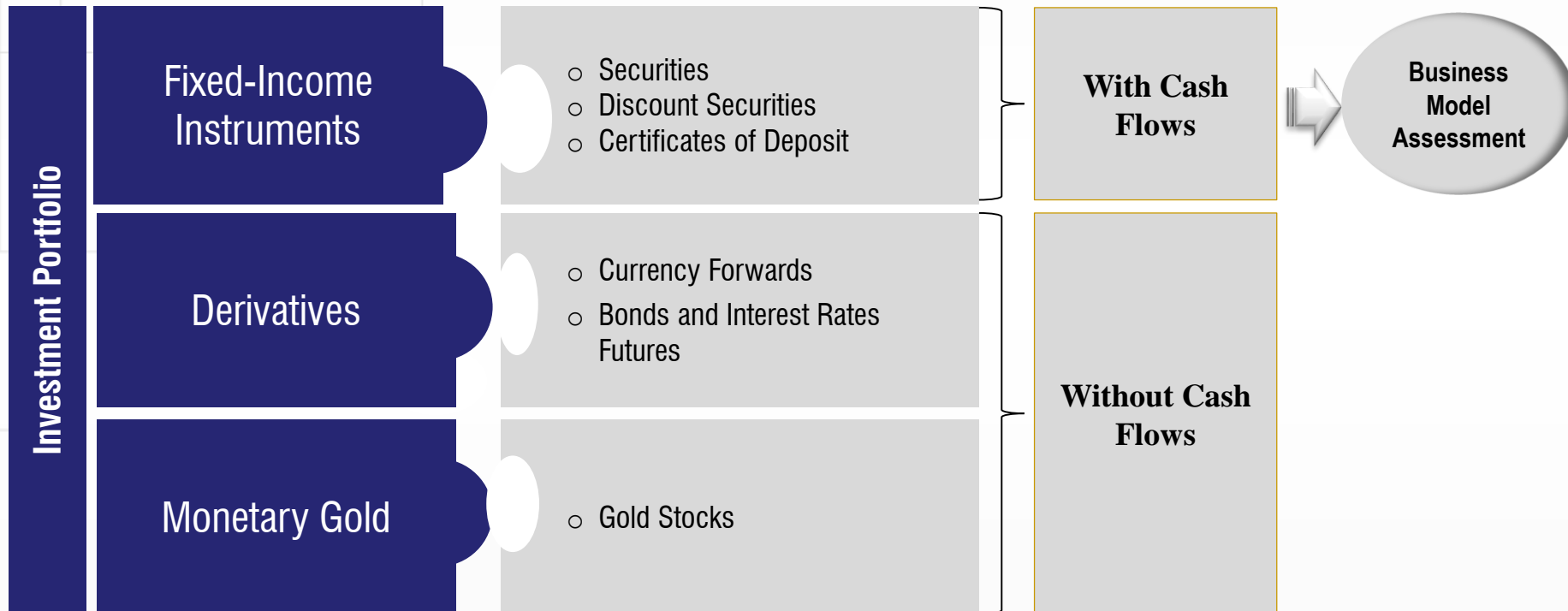
- 1) Investment Portfolio excluding Monetary Gold (94.7%)
- 2) Gold (1.5%)
- 3) Contributions to supranational entities (IMF, FLAR) and contribution to international conventions (ALADI). (3.5%)
- 4) Cash (0.4%)



# International Reserves

## Determination of Accounting Policy - Classification and Measurement

### 1. Cash-Flow Assessment



# International Reserves

## 2. Business Model Assessment

Assessment Criteria	Observations	
<b>1. Objectives and Composition</b>	<b>1.Objective</b> Maintain an adequate equity level to meet the objectives of the IR efficiently	<b>2. Composition</b> <ul style="list-style-type: none"> <li>○ Investment Portfolio and Gold.</li> <li>○ Contributions to entities and international organizations (IMF, FLAR, ALADI).</li> </ul>
<b>2. Purpose of the Tranches</b>	<b>Short-Term Tranche</b> Cover potential liquidity needs of the reserves up to 12 months	<b>Medium-Term Tranche</b> Maximize profitability. Runs with a time limit and a profile of expected profitability of over 12 months
<b>3. Sales Volumes</b>	Significant sales volume	Implementation of different strategies: <ul style="list-style-type: none"> <li>○ Review of benchmarks.</li> <li>○ Rebalancing</li> </ul>
<b>4. Risk Parameter</b>	Management parameters of portfolios to meet the objectives	Policies addressed to the preservation of capital, showing the intent to obtain higher yields through sales as well as of through contractual cash flows.



# International Reserves

## Assessment Criteria

## Observations

### 5. Basis for Management Decision Making

**The administration of the Central Bank focuses mainly on information of reasonable value for decision-making.**

Documents constructed through this information

- ❑ Absolute and relative returns and their attribution based on market factors of the portfolios that make up the international reserves.
- ❑ Market risk indicators of the aggregate portfolio of the international reserves
- ❑ Annual assessment of the active administrators of the reserves including excess returns on the portfolios compared with their corresponding indexes.
- ❑ Documents with proposals on strategic asset composition for trenches of the international reserves, using return and risk estimates and restrictions established related to the valuation at market prices.

### 6. Performance Evaluation

**How is the performance of the administrators of the Central Bank's portfolio assessed and how is it related to remuneration (including compensation)?**

Regarding the portion of the reserves that is delegated to external managers, both the assessment and the compensation depend on the valuation of the portfolio at market prices and their relative profitability compared to the reference index.

### Business Model

The activities carried out for the administration of the IR establish that the aim of the management model is to collect cash flows through the sale of assets, and to take decisions based on the fair values and their management to obtain profit from the fair values.

**Fair Value with  
Changes to Results**



# Treatment of International Reserves

## Legal Restrictions

The Bylaws of the Central Bank establish the following in paragraph 4 of Article 62:

"4. The international reserves should be accounted for at market rate. The exchange adjustment of the international reserves caused by fluctuations in the exchange rate of the peso *vis-à-vis* the currencies in which they are represented shall be recorded as a surplus (equity). The unfavorable adjustment of the exchange rate will apply to said surplus (equity). The variations in international reserves generated by changes in the prices of investments will constitute revenues and expenditures of the Bank."

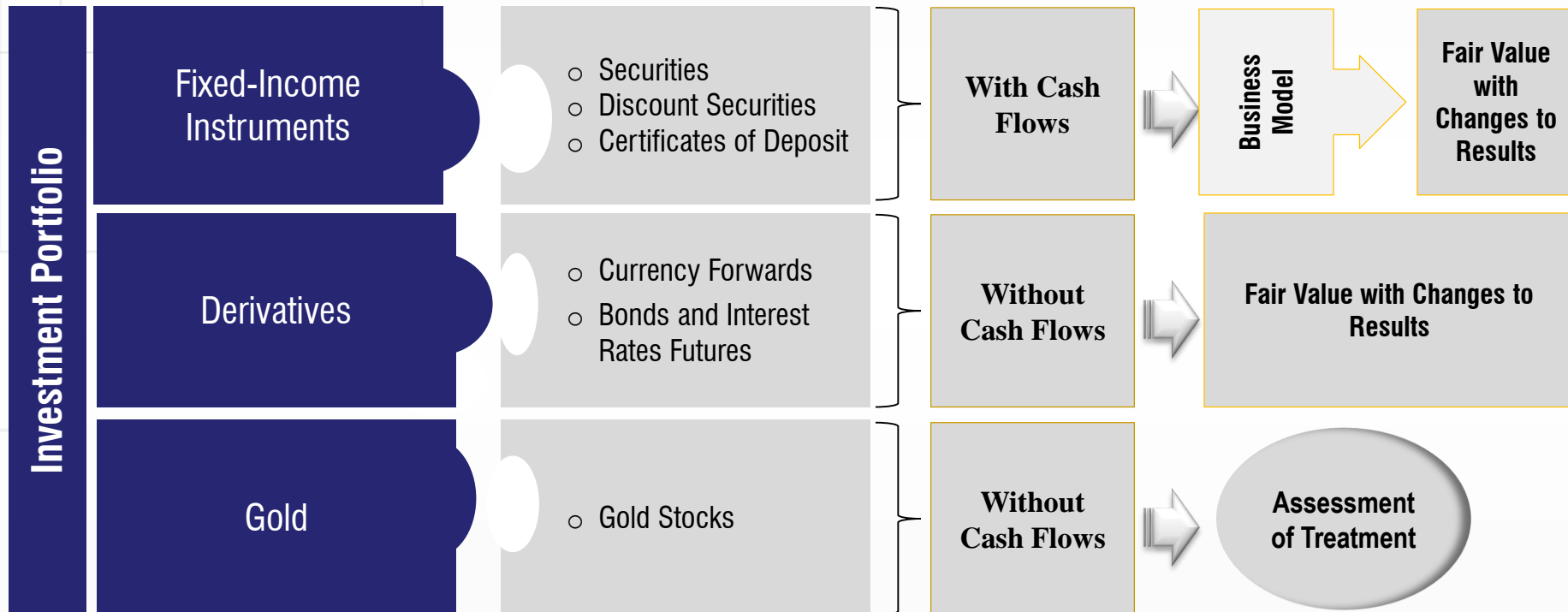
As a result, should the business model applicable to the IR be otherwise, then the Bylaws of the Central Bank would need to be modified.



# International Reserves

## Determination of Accounting Policy - Classification and Measurement

### 1. Assessment of Cash Flows

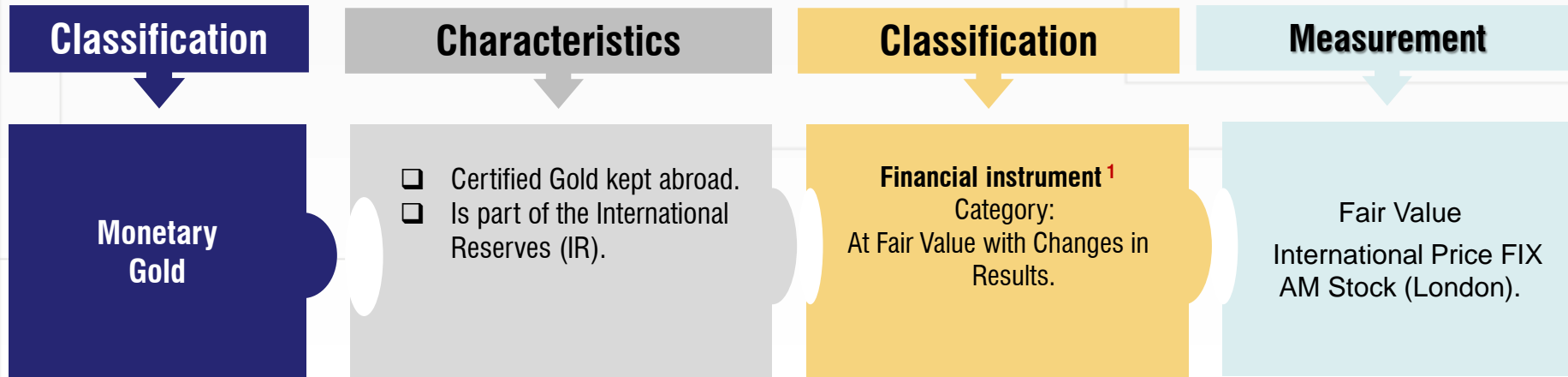


# Treatment of Gold

Classification	Characteristics	Classification	Measurement
Monetary Gold	<ul style="list-style-type: none"><li>❑ Certified Gold kept abroad.</li><li>❑ Is part of the International Reserves (IR).</li></ul>	Financial instruments	Fair Value
Non-Monetary Gold	<ul style="list-style-type: none"><li>❑ Is not part of the IR.</li><li>❑ Is used in internal purchase and sale operations or for export.</li></ul>	Other assets	Fair Value
Gold Cultural Asset (Historical)	<ul style="list-style-type: none"><li>❑ Is not part of the IR.</li><li>❑ Is used to comply with the missionary function related to cultural activity.</li></ul>	Historical, artistic and cultural heritage assets	Historical cost



# Treatment of Gold



According to IFRS 9 Application Guide, Section B.1, inasmuch as monetary gold does not represent a right and does not have a liability as a counterpart, as required by the definition of a financial asset, suggests the classification as INVENTORY; being considered as a commodity.

## **<sup>1</sup> Justification for the Treatment of Gold as a Financial Instrument:**

- ✓ Being part of the assets of the international reserves (Statutory Act of the Central Bank).
- ✓ Gold was incorporated as an eligible asset within the estimate of the reference index of the two reserve tranches, in order to take into account the market risk incurred with the holdings of gold. I.e., it was incorporated to take in to account its volatility and correlation compared to other reserve assets.





# Treatment of Gold



## Justification of the Classification and Measurement

- ✓ Does not comply with the specifications required to be monetary gold.
- ✓ By recognizing gold at its historical cost (or net realizable value, if less), would not be a fair presentation in the FS. (NIC 1, p. 19, and conceptual framework).



# Treatment of Gold

Classification	Characteristics	Classification	Measurement
<p><b>Monetary Gold</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> Certified Gold kept Abroad.</li> <li><input type="checkbox"/> Is part of the International Reserves (IR).</li> </ul>	<p>Financial instruments In the category: At Fair Value with Changes in Results.</p>	<p>Fair Value International Price FIX AM Stock (London).</p>
<p><b>Non-Monetary Gold</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> Is not part of the IR.</li> <li><input type="checkbox"/> Is used in internal purchase and sale operations or for export.</li> </ul>	<p>Other assets</p>	<p>Fair Value International Price FIX AM Stock (London).</p>
<p><b>Gold Cultural Asset (historical)</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> Is not part of the IR.</li> <li><input type="checkbox"/> Is used to comply with the missionary function related to cultural activity.</li> </ul>	<p>Historical, artistic and cultural heritage assets</p>	<p>Historical Cost. International Public Sector Accounting Standards IPSAS 17</p>



# Recognition of Results

## Financial Instruments and Non-Monetary Gold Revenue

Changes in Market Prices.  
(IR portfolio including  
Monetary Gold)

Total Comprehensive Financial  
Statement

In line with IFRS 9 Financial  
Instruments.  
Bylaws of the Central Bank.

Exchange-Rate Fluctuations  
IR portfolios, including  
Monetary Gold

Equity  
(Surplus)

Exception from the Law and Bylaws of  
the Central Bank.

Non-Monetary Gold  
Subsequent Measurement

Total Comprehensive Financial  
Statement



# Treatment of Distribution of Results

## International Reserves Portfolio (including Monetary Gold)

Concept	Distributes	Retains
Market Price Variations	X	
Exchange-Rate Fluctuations <sup>1</sup>		X

<sup>1</sup> Variations due to exchange-rate fluctuations are retained in equity (surplus), not transferred to results when realized.



# Position and Study for the Application of New Policies

- The Central Bank is currently assessing the following mechanisms to retain non-realized profit:
  - Creation of an equity reserve equivalent to non-realized results.
  - Adoption<sup>1</sup> of the Guide issued by the World Gold Council regarding:
    - Recognition: Financial Instrument.
    - Measurement: treating the difference in change and the market price variations as one valuation input.
    - Recognize unrealized earnings and losses in equity.

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<sup>1</sup> As allowed by IAS 8 “Accounting Policies, Changes in Accounting Estimates and Errors.”



**Thank you for your attention.**

