Chapter 1

INTEGRATIVE REPORT
FUNDAMENTAL PRINCIPLES OF CENTRAL BANK FINANCIAL REPORTING: A PRELIMINARY STUDY IN SEACEN ECONOMIES

By
M. Agung Hastowo[1]
Tonny Indarto[2]

1. Introduction

The submission of a central bank's financial statements to its stakeholders is one way to discharge accountability and transparency. At a glance, the financial statements of central banks are almost similar to those of commercial entities. They usually provide information regarding the central bank's assets, liabilities, capital and also results of operations. But if readers take a closer look at them, they will find certain information which is not available in the financial statements of commercial entities. Obviously, this information comprises policy instruments the central bank implements and results of its policy implementations. Hence, the financial statements play an important role in revealing information on the discharge of the responsibilities of the central bank.

To conduct its monetary policy operations, the central bank may hold a large number of financial instruments, both in domestic currency and foreign currencies. The financial instruments possessed by the central bank may have similar features as those owned by commercial entities. However, the central banks' financial instruments are intended for policy implementation instead of means of profit creation. When necessary, a central bank might continue to undertake financial instrument transactions even though they can create an unfavorable impact on its financial position or profit and loss.

While each central bank has its own preference, central banks generally have similar objectives which results in the similarity of their transactions. The absence of global standards for central bank financial reporting has caused a wide variation in financial reporting frameworks implemented among central banks. Some central banks have been empowered to develop their accounting framework[3] which diverges from local accounting standards while the others have adopted the International Financial Reporting Standards (IFRS) with some minor or major modifications. It is noted that the aforementioned differences of accounting standards used by the central bank, lead to (1) the differences in presenting monetary policy implementations in the central bank's financial statements and (2)

---

[1] Deputy Director, Department of Internal Financial Management, Bank Indonesia.
[2] Senior Financial Analyst, Department of Internal Financial Management, Bank Indonesia
[3] The report uses accounting framework and accounting standards interchangeably. Accounting standards refer to accounting principle that governs the current accounting practice issued by a standards setting body. The accounting framework refers to a system of ideas and objectives that lead to the selection of a consistent set of accounting rules and standards, which is established by the central bank.

may affect the comparability of the financial statements of the central bank for cross-sectional analysis.[4]

In the past decade, it has been apparent that accounting practices and standards among central banks have converged to internationally recognized accounting standards. A large number of central banks have adopted international accounting standards (which now are recognized as the IFRS) or standards of the European System of Central Bank (ESCB).[5] Particularly, the impetus towards adopting the IFRS is because of the encouragement of the International Monetary Fund's (IMF) safeguard assessment policy. While those closer to the European Union, have been influenced by standards of the ESCB, central banks elsewhere have moved towards the IFRS.

One other push factor expediting the convergence to international accounting standards is the implementation of the International Public Sector Accounting Standards (IPSAS), recognized international accounting standards for the public sector. The IPSAS has obviously converged to the IFRS. However, in several aspects, the IPSAS explicitly excludes central banks from the scope of several standards. The IPSAS state that certain aspects of IPSAS' rules on financial instruments need to be adjusted for certain transactions undertaken by the central bank (IPSAS 28 and 29: Financial instruments, 2014). This, indeed, indicates the recognition of the uniqueness of the central bank compared to other public sector entities, which have an impact on its accounting and financial reporting.

Another important issue of central banking accounting practice is the governance of the accounting standards setting process which has become an important mechanism to ensure that the financial reporting framework of the central bank meets the objective of the financial statements. The credibility of the financial reporting framework applied by the central bank depends on the mechanism of governance in the standards setting process. Generally, there are several methods used by central banks in deciding the appropriate accounting standards: first, the accounting standards that are internally set by the central bank; second, the adoption of the IFRS or adoption of its national accounting standards; third, the development of accounting framework by independent bodies (Bank Indonesia, 2011; Sullivan, 2014). However, the discussion papers on the governance of the accounting standards setting for central banks are still limited.

---

[4] For example, government treasury bonds may be presented at amortized cost or at fair value. If bonds are presented under fair value; the change of fair value could be recognized as gains/losses in the bank's statement of income; or as unrealized gains/losses in the bank's balance sheet.

[5] The ECB has developed its own accounting framework: The Guideline on Legal Framework for Accounting and Financial Reporting, which applies to all central banks in the European System. This framework is tailored to the needs of the European System central banks and differs from the IFRS with respect to the treatment of the core central bank operations. It was established on the foundations of basic accounting assumptions, including economic reality and transparency, prudence, post balance sheet events, materiality, going concern basis, the accrual principle, and the consistency and comparability (Decision ECB/2010/20, 2010). These principles are consistent with accounting framework in commercial entities. The ECB framework focuses on the accounting policies that correspond to the main pillars of any central bank accounting framework including: (i) composition and valuation rules for the balance sheet; (ii) income recognition; (iii) accounting rules for off balance sheet instruments; and, (iv) reporting obligation, format, and rules (Decision ECB/2010/20, 2010).

2. Central Bank Financial Statements

Sullivan (2005) has pointed out that, similar to other entities, the objective of the central bank's financial statements is to provide information that is relevant and reliable to the decision making needs of users. According to Sullivan (2005), the information required by the users of central bank's financial statements is information on the economic resources under control of the central bank, legal and economic obligations of the central bank, inflows and increases in economic resources and consumption or declines in economic resources of the central bank, cost information on central bank operations, future risks to the maintenance of the resources of the central bank, potential obligations and resources not yet measured by the central bank and why, level of transactions with parties related to the central bank including unconsolidated subsidiaries, and methods used to portray and measure the actual economic resources. In line with Sullivan (2005), studies of Filardo and Yetman (2012) and Caruana (2012) also argue that the objective of central bank's financial statements is to describe the resources and obligations of the central banks in implementing the monetary policy.

For commercial entities, the financial statements should meet the qualitative characteristics (as the ideal characteristics) and present specific components in their financial statements in order to meet the objective of financial statements. The international accounting standards, such as the IFRS or United States Generally Accepted Accounting Principles (US GAAP), in principle, concur in declaring that the accounting information of commercial entities must meet the qualitative characteristics of "relevance" and "reliability". However, for the central bank, it is uncertain if the similar qualitative characteristics could be applied in the same way.

Although there are no internationally accepted accounting standards for the central banks, they have, generally, arrived at several consensus about the characteristics of accounting information for financial statements. For central banks which have fully or partially adopted the IFRS and central banks which have developed their own accounting standards, the qualitative characteristics of relevance and reliability should remain as the ideal criterias that should be met by central banks' accounting information (Djakman and Rahadian, 2011). In order to be relevant, the accounting information of the central bank should be material, contain feedback value, predictive value, and timeliness. The information presented in the central bank's financial statements should help users to learn about the financial impact of central bank policies. The central bank's financial statements must also contain information that can be used by users to gain an insight of the direction of central bank's policies and the impact of those policies in the future. The financial statements of the central bank should also be presented periodically in a timely manner, as stated in the practice of good transparency developed by the IMF (1999).

In order to be reliable, Djakman and Rahadian (2011) stated that the financial information of the central bank should emphasize the substance rather than legal form. The accounting treatment should be based on the economic substance of a transaction.

Furthermore, in determining the accounting estimates, it should stress the principle of prudence. Reliable financial information also includes that which is verifiable, free from bias and free from material misstatement. Djakman and Rahadian (2011) stated that the central bank's financial information must be verifiable by an independent party, so it must be able to be audited by an independent party, i.e. a public accountant. Furthermore, the central bank's financial statements must be prepared in accordance with accounting policies that are consistent over time. Changes in accounting policies are permissible if only to present more relevant and reliable information.

The information needed by users will generally be provided through various components of the central bank financial statements. In order to present high quality information, there are minimum requirements that should be presented in the financial statements of the central bank, i.e. statement of financial position (balance sheet), statement of income, statement of changes in equity, and notes to the financial statements. The study of Firdhaus (2010) shows that the financial statements presented by most central banks comprise of: (i) balance sheet; (ii) statement of income; and, (iii) notes to the financial statements. Some central banks also present statement of changes in equity. However, the presentation of the statement of cash flows is not common among central banks. The Reserve Bank of New Zealand (RBNZ) is one of the few central banks which prepares the statement of cash flows (Firdhaus, 2010). Also, the central bank which has decided to adopt commercial accounting standards such as the IFRS, is required to present the complete components of financial statements, including statement of cash flows, perhaps with some modifications. [6]

Since its assets are dominated by financial assets, the central bank. in presenting the financial statements, can classify assets based on the nature and liquidity of the financial assets. For example, financial assets are classified into securities and bills. Assets presentation based on liquidity is considered to be more relevant for central banks rather than to classify the assets based on the current and non-current classification as the central bank does not have a clear operational cycle as entities that manufacture products do. In addition, the central bank can also classify assets based on their functions, for example, the separation of financial assets for monetary operations and other financial assets (Firdhaus, 2010). According to Djakman and Rahadian (2011), the presentation of the statement of the financial position should be guided by its relevance to monetary policy and liquidity. The arrangement based on liquidity order could sensibly accommodate the nature of the central bank's assets which are dominated by financial assets. Moreover, the presentation based on its relevance to monetary policy would improve the relevance of the information, since the users of central bank financial statements would be able to evaluate easily, the relationship of monetary policy with assets/liabilities owned by the central bank.

[6]The balance sheet is useful for determining the strength and ability of central banks to implement monetary policy while the statement of income (or statement of surplus deficit) is useful for determining the results of the use of public funds. Meanwhile, the statement of changes in equity is necessary to determine the level of the central bank dependence from the government while notes to the financial statements are required to understand the accounting policies and other information related to the company's financial information. However, unlike the commercial entities, the statement of cash flows is not particularly relevant to the central bank, because the central bank has the authority to create money (Firdhaus, 2010).

In presenting the statement of comprehensive income, the term profit and loss can be converted into surplus-deficit, according to the characteristics of the central bank as a non-profit entity. The central bank can choose to present the expenses by their nature (as widely used by commercial non-bank entities) or by their function (as used by commercial banks). Both approaches are permissible under the IFRS (Firdhaus, 2010). Djakman and Rahadian (2011) find that the central bank's statement of income, in principle, does not have many differences with the commercial bank's statement of comprehensive income, which presents the entity's revenues and expenses, since the central bank essentially engages in a similar industry as the commercial bank. Detailed revenues and expenses items of the central bank represent the central bank's activities, i.e. the core operations of central bank, monetary policy and foreign reserves management. Similarly, the central bank's statements of changes in equity do not have many differences with those of commercial banks. Under the IFRS, the central bank presents all changes of equity components which are caused by the surplus/deficit or other deposits and/ or distribution to stakeholders, i.e. the government (Firdhaus, 2010).

Central banks should also present notes to the financial statements. Similar with other commercial entities, notes to financial statements provide general information of the entity, measurement bases, estimate and judgment, accounting policies, details of some posts in the face of financial statements, contractual agreements and others. Notes to financial statements are necessary for users to understand the information presented (Djakman and Rahadian, 2011). The notes to financial statements should also be optimized, considering the risks posed by opportunistic market participants who may use the detailed information disclosed by the central bank, to the detriment of the market.

Nevertheless, there are some differences in the presentation of financial statements among central banks. The ECB refers to the decision of the ECB Governing Council while the United States Federal Reserve uses the Financial Accounting Manual (FAM) set by the Federal Reserve Board of Governors. The Bank of England (BoE) adopts the IFRS for banking while the RBNZ uses accounting standards equivalent to the IFRS. According to Blinder et al. (2001), the RBNZ is an example for best practice in financial reporting and transparency, and is often regarded as the central bank that is most compliant with the IFRS.[7]

To present the relevant and reliable accounting information as explained above, there are basic assumptions, accounting principles, and some limitations regarding the financial statement. According to Djakman and Rahadian (2011), the basic assumption of going concern, the presentation of information in a periodic basis (periodicity), the monetary unit, and economic entity could also applied to the central bank's financial reporting. The financial statements of the central bank could only be prepared if it is assumed that the central bank's going concern is not doubted and that is a separate economic entity from other economic

[7] RBNZ is currently using the Public Benefit Entity Standards (PS PBE Standards) which are based mainly on the International Public Sector Accounting Standards. The effective date for the new standards is for reporting periods beginning on or after 1 July 2014.

entities. The central bank's financial statements are presented periodically according to a certain time frame and in the home country's currency.

The accrual basis principle that is applied in commercial entities, is also appropriate to be used as the basis of recognition of income and expenses of a central bank. Arguably, there is no certain characteristic of the central bank for which the accrual basis is more appropriate than the cash basis. The full disclosure principle also applies to the central bank, but with some consideration for the limitations. The full disclosure principle might increase the possibility of such information being misused by opportunistic market participants, leading to the failure of meeting central bank policy objectives (Djakman and Rahadian, 2011). It is found that central banks in developed countries are quite prudent with disclosures in financial statements. Take the case of the BoE which adopts the IFRS as its financial reporting framework. It is stated in its financial statement that:

> *"The Adopted IFRS and the Companies Act have been used as a model for the presentation and disclosure framework to provide additional information and analysis of key items in the financial statements except in so far as the Bank considers disclosures inappropriate to its functions."*

In this case, the BoE acts as a 'lender of last resort' to financial institutions where the Bank may not explicitly identify the existence of such support although the financial effects of such operations will be included in its financial statements in the year in which the support occurs. However, the existence of such support will be reported in the annual report when the need for secrecy or confidentiality has ceased. It can be concluded that in promoting transparency, the central bank should be aware of not publicly disclosing sensitive information which might hamper the policy objective and increase the risk of information void to opportunistic market participants. However, as the level of risk varies between central banks, they are in the best position themselves to analyze the trade-off.

3. The Accounting Framework of the Central Banks and the IFRS

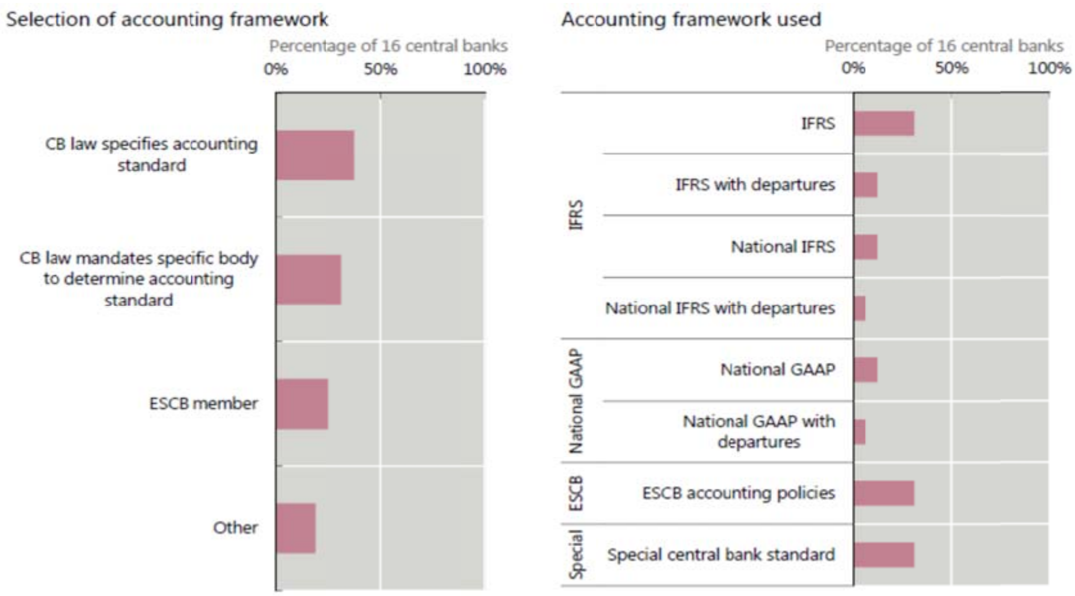
The survey of the Central Banking Publication (2003) shows that accounting practices and standards of more than 160 central banks have converged since the 1990's. Of the 44 central banks that responded to the survey, 39% claimed to have adopted international accounting standards (IAS)[8] to some degree, while only 27% are fully IAS compliant. The other banks surveyed employed either national accounting standards, central bank-specific standards, or some combination thereof. The above survey also suggests that the key driver of the convergence of accounting standards among central banks appears to be the advent of the IMF's safeguards assessment policy. One of the key benchmarks of the IMF's safeguards assessment policy is the adoption of the IAS or its equivalent such as the Eurosystem

[8] IAS are standards issued by the International Accounting Standards Committee (IASC) between 1973 and 2001, whereas the IFRS were published by the International Accounting Standards Board (IASB), starting from 2001. When the IASB was established in 2001, it was agreed to adopt all IAS standards, and name future standards as the IFRS.

Accounting Principles. As a high quality international accounting standard, the IFRS is characterized as a principle-based standard and requires extensive disclosures (Daske et al., 2008). These characteristics are expected to increase the transparency of the central bank. Also, the trend of convergence towards the IFRS is not surprising since its proponents claim that conformity with the IFRS is the measure of accountability and relevance for financial statements.[9]

This is also evidenced by a more recent research conducted by the Bank of International Settlement (BIS) which looks into the accounting standards applied in 16 central banks (Archer and Moser-Boehm, 2013) (see Figure 1). Some central banks have adopted the IFRS. Nevertheless, financial reporting practices still vary among central banks (Sullivan, 2014).

Figure 1
Survey on Accounting Framework Used by Central Banks



Source: Archer and Moser-Boehm, 2013.

One example of central banks that have adopted the IFRS is the South African Reserve Bank (SARB). The SARB adopts the IFRS with the exception for transactions in gold and foreign currencies. The SARB developed specific accounting policies for both transactions. In contrast to the SARB that use international accounting standards, the Federal Reserve Bank chose to develop its own accounting standards named the Financial Accounting Manual for the Reserve Banks (FAM). The FAM sets the accounting principles and practices that are considered appropriate to the nature and function of the central bank.

[9] Under the IFRS, the objective of financial statements is to provide financial information about the reporting entity which would be useful to potential equity investors, lenders, and other creditors in decision-making in their capacity as capital providers

The FAM has some differences with the US GAAP, which are related to the presentation of securities of System Open Market Account (SOMA) (Bank Indonesia, 2011).

Since each central bank has its own objectives, the practice of its financial reporting will vary. The difference in objectives affects the operational activities undertaken by the central bank and, therefore, will impact the presentation of the financial reporting structure. Financial reporting can also be affected by the role of the central bank as the reporting entity. From the perspective of a principal-agency, the central bank may act as a principal or as an agent of the government. The central bank may act as principal, for example, when it has full authority to manage the country's foreign exchange reserves. As a consequence, the central bank will report its assets and liabilities as financial instruments in the financial statements. However, it will be different when the central bank serves as an agent of the government, e.g., BoE and Bank of Canada. The financial impact of central bank operations will be reported by the government and the statement of income provides fewer details about the composition of profit serves. Plausibly, it suggests that the level of income and expenditure are not relevant determinants of central bank performance (Sullivan, 2014).

The IMF suggests that central banks adopt international accounting standards (i.e. IFRS) for several reasons. For commercial entities, the adoption of the IFRS will improve the information quality of financial statements, for attracting and protecting the investors. Arguably, this also applies in the case of the central bank. The adoption of internationally accepted accounting standards will improve the transparency, reliability and comparability of the central bank’s financial statements in order for users to understand the central bank’s achievement of its objectives. Users will also obtain a clearer understanding and more comprehensive information on the operational activities of the central bank (Minzoni, 2014).

However, Minzoni (2014) explains that the adoption of the IFRS has led to problems for the central bank. The IFRS are accounting standards used by commercial entities that have different objectives compared to the central bank. This difference will affect the importance of profit and loss figures presented in the financial statements. For commercial entities, profit and loss figures are very important measures for evaluating their performance. As for the central bank, the income figure may be a mere consequence of the implementation of its duties in achieving its objectives. The central bank is permitted to meet the condition of "good losses", i.e., when the central bank undertakes expansionary policies. Moreover, in other situations, it is permissible for the central bank to obtain “bad profits” i.e., when the country's currency depreciates (Minzoni, 2014). In reading the financial statements of the central bank, users should understand that the profit and loss figures in the financial statements carry different meanings from the profit and loss figures of financial statements of commercial entities. However, there are many users who have a less precise understanding of financial statements in their reading of these statements. BIS states that (Minzoni, 2014):

> *"it may be easy to avoid setting profits as an objective, but it is surely more difficult to educate stakeholders to distinguish between losses that provide a useful signal of performance and losses that provide a neutral or conflicting signal."*.

To overcome the misinterpretations, there should be a statement of income format which can link the central bank's financial statements to the relevant issues in understanding the functions and performance of the central bank (Minzoni, 2014).

The next major issue related to the adoption of the IFRS by the central bank is on the fair value measurement of assets or liabilities.[10] Unrealized gains or losses on assets or liabilities measured at fair value will be presented in the statement of income. This raises problems in calculating the profit to be distributed to the government. The central bank prefers non-inclusion of the unrealized gains in the calculation of the profit that will be distributed to the government (or other shareholders-if any). However, the specification to include unrealized gains or losses on assets or liabilities in the statement of income is inconsistent with the central bank's monetary policy framework since it could affect the amount of liquid assets to execute monetary policy (Paramonova, 2003; Sullivan, 2003; Kurtzig, Hemus and Goodwin, 2003). The existence of fluctuating unrealized gains in the calculation of the profit distributed to the government might also lead the central bank to have insufficient buffers if in the forthcoming financial period, the gains would turn into losses (Sullivan, 2003).

To overcome the problems related to the calculation of distributed profit to the government, the central bank may choose either of two approaches. The first approach is to design accounting guidelines that require the unrealized gain to be excluded from the component of net profit in the statement of income. This approach is effective in assuring that the dividend distributed is free from the component of unrealized gains. However, this strategy has been often criticized as not being in accordance with accounting standards as it allows the dividend policy to direct accounting guidelines (Merriman, 2003; Kurtzig, 2003). This approach is employed by the ECB for which the accounting standards declare that the unrealized gains are not included in the calculation of net profit.

The second approach is to apply the generally accepted accounting standards but for the component of unrealized gains (although listed as net profit) to be not distributed as dividends. With this approach, the central bank may still include components of unrealized gains in net profit (in accordance with general accounting standards). On the other hand, at the same time, the unrealized gains are assured to be not distributed as dividends (Firdhaus, 2010). BoE and Reserve Bank of New Zealand (RBNZ) use the second approach. This

[10] However, when they are applied on central banks, the greater presumption of the IFRS for fair value may cause large swings in unrealized gains and losses due to volatility in asymmetric foreign exchange positions which can significantly impact financial results, affecting reported performance, capital and, as a result, have the potential to compromise policy effectiveness, financial strength and independence.

second approach requires the central bank to have sufficient flexibility in negotiating the distribution of its net profit with the government.

Another issue related to the adoption of the IFRS by the central bank is the issue of impairment of financial assets, i.e. loans to the government. In accordance with the IFRS, the central bank should estimate the probability of impairment on loans to the government and present them in the financial statements. However, in practice, it is difficult to apply such rules, because the government is a major stakeholder of the central bank and the ultimate owner (ultimate underwriter) of the country's currency (Minzoni, 2014).

4. Coverage of this Report

While previous research was mainly conducted by non-central banks, this study is conducted by a group of researchers from central banks to shed light on central bank accounting practices. This study focuses on the followings: (1) Part I covers the roles of the SEACEN central banks in economic development and central banks' independence (2) Part II surveys the current practices in financial reporting among SEACEN member central banks, which includes the framework and governance of the accounting standards setting process (3) Part III looks into the financial reporting from the stakeholders' perspectives (4) Part IV describe the perspectives on variation of financial reporting practices amongst central banks. However, this study will not measure (i) the degree of compliance of each central bank with some notional best practices, and (ii) assert that one financial reporting framework is better than another.

The results of study will be useful for (1) central banks in SEACEN economies to have a reference for the current practices of financial reporting in the region; and, (2) international accounting standards setting bodies to have a reference for developing accounting standards for central banks.

5. Research Methodologies

This paper is a qualitative and preliminary exploratory study. Research issues are divided into several stages of the project and employing several techniques. The use of multiple methods in this study is an effort to triangulate and improve the validity of the study results. As a preliminiary study, this study focuses on 14 samples of the 20 SEACEN member central banks/monetary authorities. The sample selection process assures that the diverse characteristics of SEACEN member central banks/monetary authorities are well represented, e.g. balance sheet size, accounting framework used, and the economy environment in which the central bank operates.

The study was undertaken for period April – December 2015 and designed into 3 stages. Stage 1 of this study was to map the current accounting practices of selected central banks using literature study on central bank objectives, purposes for financial statements, accounting practices and financial reporting, as well as governance of accounting standards setting of these central banks. The source of data was publicly available literature, including the published financial statements and central bank acts. The outputs of the first stage are the map and the analysis of uniformity and uniqueness of the sampled central banks: (i) objectives; (ii) tasks carried out; (iii) accountability of central bank; (iv) financial reporting framework used; and, (v) components of financial statements.

Stage 2 of the study was the distribution of questionnaires to selected samples. The questionnaire was designed not only to validate the results of Stage 1, but also to gather additional information related to the central bank financial reporting framework which cannot be garnered from available sources. The questionnaire covered 7 topics and comprised 40 questions on:

1. Functions of central bank as mandated by laws,
2. Line of authority report for the central bank,
3. Ownership and finance of the central bank,
4. Various aspects of central bank financial statements, including purposes, users, audit and components of financial statements,
5. Accounting framework adopted by central bank and its setting process,
6. Perspectives of users on central bank financial statements, and
7. Opinions of central banks on various accounting practices among central banks.

The questionnaire basically follows a similar survey carried out by the BIS on central bank finances in 2013. The questionnaire (Annex 1) which was distributed to 14 central banks in June 2015 was sent to the decision makers in central banks, i.e. heads of the accounting departments. Responses were received from 12 central banks/monetary authorities, constituting a 86% questionnaire response rate.

In Stage 3, a Focus Group Discussion (FGD) was conducted in October 2015 for the project team members. The FGD led by the Bank Indonesia project leaders was attended by all members of project team (National Bank of Cambodia, Reserve Bank of India, Bangko Sentral ng Pilipinas, Central Bank of Sri Lanka and Bank of Thailand) with observers from Bank Negara Malaysia, Reserve Bank of Fiji, Autoriti Monetari Brunei Darussalam and The Bank of Mongolia. The output of the Stage 3 comprises of (i) views on the variation of SEACEN member central banks' accounting practices; and, (ii) opinion on the recommendations for generally accepted accounting principles and governance of accounting standard setting.

6. Results of the Findings

The findings of the study are presented in the order of research objectives.

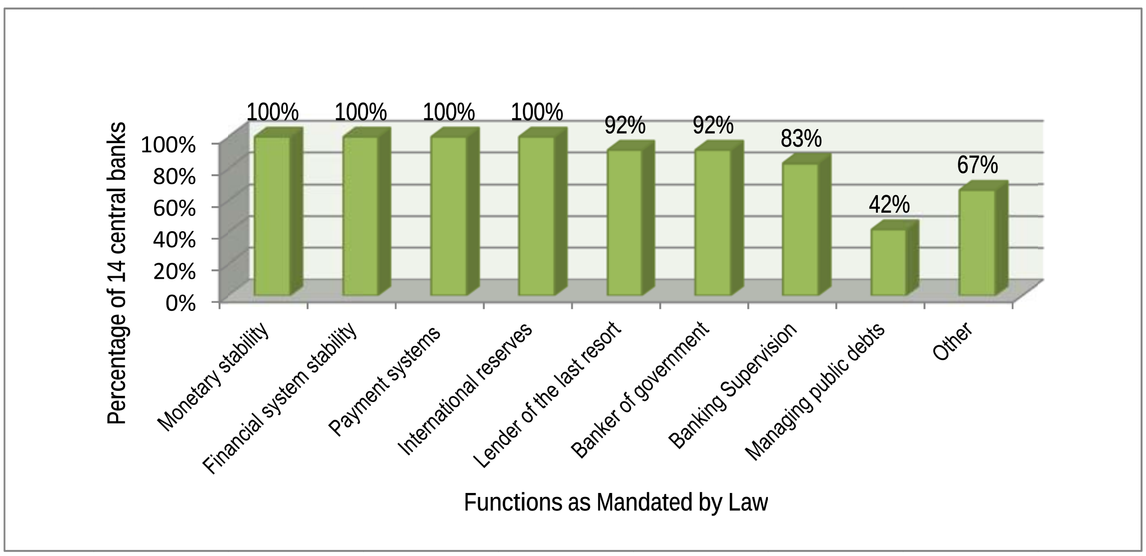
Part I: Roles of the SEACEN Central Banks in Economic Development and Central Banks' Independence

(i) The Roles of the SEACEN Central Banks in Economic Development

One of the institutions that play an important role in the economic development of a country is the central bank whose main objective is to maintain monetary stability. In order to achieve its objective, the central bank is usually entrusted with relevant functions relating to the sound functioning of payment systems, banking supervision, etc. But whatever the set of responsibilities conferred to it, its basic goal is to design and implement monetary policies that could achieve monetary stability as reflected in price and/or currency stability.

Based on the literature study on the objectives of 14 sampled central banks, all central banks operate in order to achieve monetary stability. From the 12 central banks that responded to the survey, 43% of central banks stated that their objective is price stability, whereas 36% have stated currency stability as their target, with the rest 21% aiming for both price and currency stability.

Figure 2
Functions of Central Bank



In order to confirm the relationship of the central bank's objectives with its functions, the survey queried about the main and additional functions carried out by the central bank according to the mandate of the law. The results of the survey confirmed that the central bank's roles have been evolving but are still consistent with its objective, which is monetary stability not profits. As we can see from Figure 2, the survey revealed that the central banks are still assigned the four traditional roles as defined by Blinder (2010): (i) conducting monetary policies, including the possible use of lender of the last resort powers; (ii) preserving financial stability, which in serving this classic role, lender of last resort powers are almost always invoked; (iii) safeguarding payment and settlement systems, in which lender of the last resort powers are likely to be used on occasion; and, (iv) supervising and regulating banks. There are instances where bank supervision is carried out by newly-established financial supervisory institutions. The survey also suggested that all central banks surveyed are responsible for managing the country's international reserves. 92% are mandated by law to act as lender of the last resort as well as banker to the government, but only 42% are in charge of managing public debt.

It was noted that some respondents stated that the central banks are also undertaking other functions including:

1. Fostering small and medium enterprise growth through facilitating access to financial institutions;
2. Regulating financial markets;
3. Providing guidance to anti-money laundering work;
4. Acting as the registrar for the government bonds;
5. Monitoring and regulating the foreign exchange transactions according to the law on foreign exchange;
6. Performing agency functions including managing the nation's Employees' Provident Fund;
7. Acting as Financial Intelligence Unit (FIU);
8. Promoting regional development and growth including in the areas of rural credit and financial inclusion; and,
9. Regulating and supervising of Non–banking Finance Companies (NBFCs).

However, in managing international reserves, some central banks in SEACEN economies are actively involved in the trading of financial instruments with a profit motive while some are not engaged in active trading. One argument that came out of the findings was that despite its profit motive, the ultimate objective of international reserves management is to support the implementation of central bank policies.

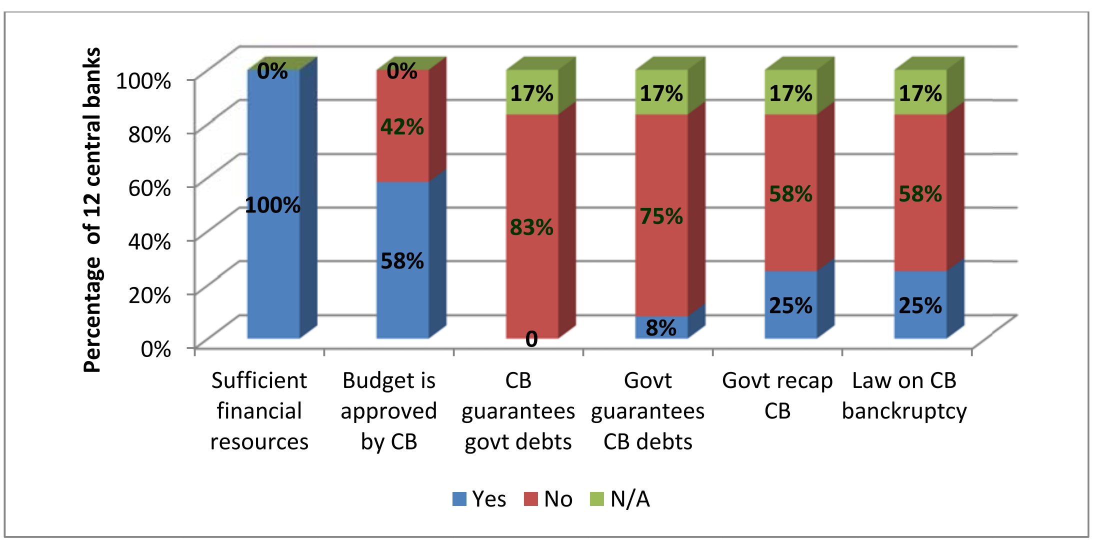
(ii) The Financial Independence of the SEACEN Central Banks

Most central banks around the globe have broad independence in performing their roles to achieve their objectives. However, central bank broad independence should be balanced with a high degree of accountability and transparency. It is normally understood that transparency facilitates accountability, which constitutes central bank independence in a democratic society. In general, transparency of the central bank consists of two parts. First, to what extent the central bank communicates its policy objectives, decisions and outcomes; and second, to what extent the central bank discloses the employment of financial resources for undertaking its policy.

In this Section, the survey attempted to explore the level of financial independence of central banks.[11] There are several indications pointing to the fact that the central bank is financially independent. Figure 3 presents the survey results on the indicators of central bank financial independence. All central banks surveyed were certain that they had sufficient financial resources to perform their functions, implying that the central banks are independent in formulating and implementing monetary policies to achieve their goals.[12] However, in terms of using the resources for non-policy related activities, there are some limitations for some central banks. The survey shows that 5 out of the 12 central banks have their annual operating budget approved by the government or the parliament. In relation with the government, none of central banks were legally obligated to guarantee debts incurred by the government. On the other hand, one central bank had government guarantee for the debts incurred by the central bank.

Theoretically, the central bank will not be faced with a situation where the continuity of existence is threatened. However, in reality, the results of survey show that some central banks are regulated in terms of solvency or capital injection. Three central banks stated that their laws have specific provisions on bankruptcy but there are obligations on the part of the government to inject capital into the central bank. On the other hand, for 10 central banks that are accountable to the government, there are 3 that have provisions in the laws for the government to recapitalize the central bank under certain circumstances.

Figure 3
The Financial Independence of Central Banks based on some Indicators



[11] Two SEACEN central banks have opted not to answer questions related to this part.
[12] Typically, at the time of constituting the central bank, the capital was provided by the government.

Ten (10) central banks (83%) have a clear arrangement on the distribution of central bank profits to the government. However, there is a lack of provisions on the treatment when the central bank suffers excessive losses. Only 3 central banks have laws that clearly state the treatment for central banks' excessive losses or goes into an unfavorable financial condition. Acting as banker to the government, 4 central banks shall pay returns on government deposits.

In the focus group discussions, it is learned that one central bank has full autonomy in its finance. The central bank approves its own budget, determines how much profit to be distributed to the government, and will not be recapitalized by the government in any circumstances.

Part II: Current Practices in Financial Reporting of SEACEN Central Banks

(i) The Qualitative Characteristics of Central Bank Accounting Information

Based on our survey of the financial statements published by central banks, we find that all central banks provide general information related to their unique objectives and functions. There are only 2 central banks (CBSL and Bank Indonesia) which clearly define that the objective of their financial statements as recording the financial impact of policy implementation. For instance, the survey replies of CBSL clearly states that:

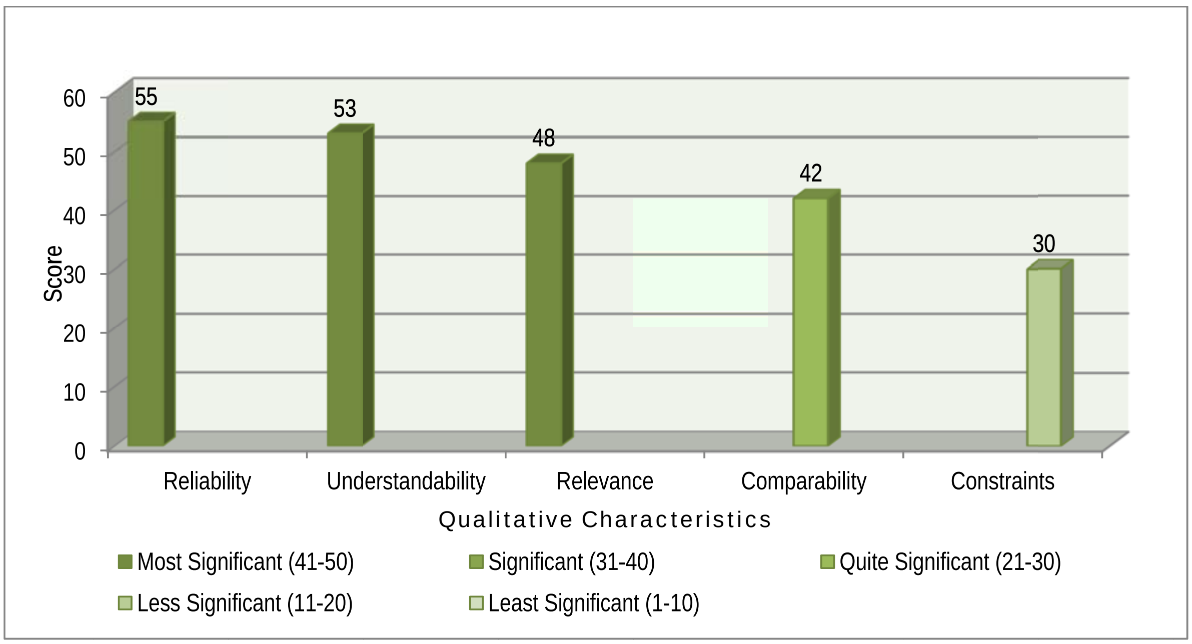
> *"The basis of accountability for the Central Bank and the success of its operations therefore would be the effectiveness of its policies and operations leading towards the achievement of its core objectives and not necessarily its profitability."*

In our survey, it is noted that the questionnaire responses also confirm that all respondents agree that central bank's financial statements have different objectives to those of commercial entities. That is, the objective of central bank financial statements is to demonstrate its accountability in achieving its objectives, which includes information on the impact of central bank policies on the financial position and surplus deficit of central bank.

When the sampled SEACEN central banks were requested to rank 5 qualitative characteristics that must be possessed by their financial statements, only 4 characteristics were considered to be most significant and ranked accordingly. These characteristics are reliability, understandability, relevance, and comparability (Figure 4). As in common practice where accounting concepts consistently consider "relevance" as the most important characteristic in financial statements, the results were surprising. Nevertheless, since central banks should be credible for monetary policy to be effective because they influence longer rates, signaling movements in future policy and anchoring inflation expectations, it may be understandable why reliability is ranked most significant. One respondent pointed out that it is extremely important to ensure that stakeholders place their trust on central bank's financial statements. Therefore, the central bank has to assure that the information it discloses, especially the financial statements, is thoroughly reliable.

With regard to understandability, as a central bank operates differently from commercial entities, it is likely that users may misinterpret central bank's financial statements. For instance, the central bank may fall into "good losses", i.e. when the central bank undertakes expansion policy. Or in another situation, the central bank obtains a "bad profit", i.e. when the country's currency depreciates (Minzoni, 2014). The users should understand that the profit and loss figures in central bank's financial statements have different implications from the profit and loss figures in the financial statements of commercial entities. The business of the central bank is different compared to commercial entities. Unlike commercial entities which operate to maximize shareholders' values, central banks operate in order to achieve their policy objectives.

Figure 4
Qualitative Characteristics of Financial Statements



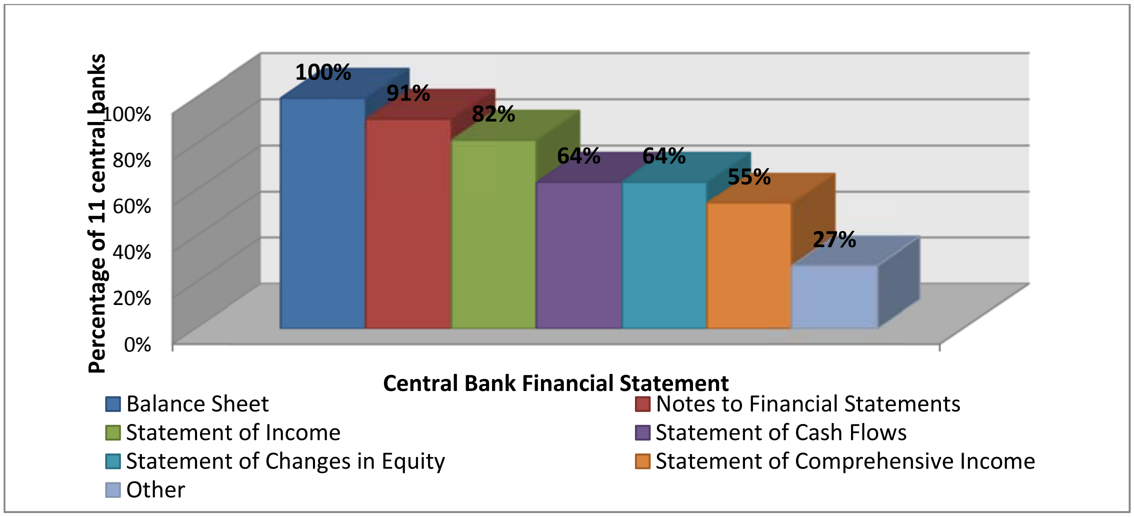
(ii) Components of Central Banks' Financial Statements

In general, the survey suggests that there is a different emphasis on the importance of each component of financial statements. Respondents were asked to rank the component of financial statements, which they see as the most significant component. As can be seen in Figure 5, the components of financial statements in accordance with the level of significance are as follow: (i) balance sheet; (ii) notes to financial statements; (iii) statement of income; (iv) statement of changes in equity; (v) statement of cash flows; and, (vi) statement of comprehensive income. The finding is somewhat consistent with the study by Firdhaus (2010) with the first three components most commonly presented by central banks. Several

SEACEN central banks also present additional reports such as statement of profit distribution and statement of changes in appropriation of retained earnings.

It is noted that several central banks, even one which applies the national IFRS, opt not to present the statement of cash flows. One may argue that given the unique role of a central bank, the statement of cash flows need not be presented because the information contained therein is immaterial. Another argument is that according to legislation, the effectiveness of a central bank in achieving its objective is not measured by its ability to generate future cash flows. In addition, many central banks are empowered by the authorities to print currency and therefore currency liquidity is not a major issue for the Banks.

Figure 5
Components of Financial Statements



Interestingly, respondents which stated their central banks present the statement of cash flows have suggested that it may not be necessary for central banks to present the statement of cash flows. One respondent states that a statement of cash flows may not be meaningful for users especially information on domestic operations, given the unique role of the central bank as the ultimate source of domestic liquidity.[13]

(iii) The SEACEN Central Bank Financial Reporting Framework

As noted earlier, there is general affirmation that profit maximization is not a central bank's objective. The profits or surpluses are not measures of central bank performance and profit and loss figures are the consequence of the execution of central bank duties. Paradoxically, there are many central banks which have adopted the IFRS, which are obviously intended for profit-oriented institutions. For such a contradiction, this survey sets

---

[13] However, CBSL which presents the statement of cash flows since its application of the IFRS in 2002, has indicated that the statement of cash flows is still meaningful, especially for information of sources and uses of resources related to reserves management.

out to discover the reasons of central banks in opting for the IFRS as their accounting framework. The survey also attempts to identify the items which the central banks report in their financial statements. Moreover, the survey also addresses the question of whether the IFRS is sufficient to fulfill the reporting needs of central banking or an alternative accounting framework is needed.

As can be seen in Table 1, the survey shows more than 58% of central banks apply the IFRS or a national version of the IFRS, while the rest of the 42% apply their own financial reporting framework. Moreover, 40% of the central banks which refers to the IFRS have made some modifications to the standards. The Central Bank of Sri Lanka (CBSL)[14] adopted the IFRS as early as 2002 and has been fully compliant since 2004, while the others have adopted IFRS only recently.

The diversity of central banks' accounting framework comes from their different accountability. As shown in Table 1, the five central banks which have their own accounting standard are accountable to different parties.

Table 1
Financial Reporting Framework and Accountability

Financial Reporting Framework	Number of Central Banks	Accountability		
		Parliament	Government	Both
Own Accounting Standards	5	1	2	2
Fully IFRS[15]	4	-	2	2
IFRS/National IFRS with modification	2	1	1	-
Fully National IFRS[16]	1	-	1	-

In the case of a central bank using an accounting framework that significantly departs from the IFRS or National IFRS standards, there are 3 (three) main key departures, summarized in Table 2.

[14] The project team member from CBSL participated in this study and provided valuable inputs on how the IFRS can fit the central bank's financial reporting needs. However, views provided are his own and may not reflect those of CBSL.
[15] Central bank adopts IFRS or a national carbon-copy of IFRS.
[16] National IFRS refers to national accounting standards are similar to but not the same as IFRS.
The survey also asked if central banks which adopt the National Generally Accepted Accounting Principles (GAAP) for national accounting standards are substantially different from the IFRS. None of respondents is applying National GAAP.

Table 2
Key Modification of Accounting Standards in SEACEN Central Banks

Description of Departures	Percentage of Central Banks Surveyed	Argument behind the Departures
1. Effect of changes of foreign exchanges: a. Unrealized gains or losses where changes in exchange rates of financial assets, liabilities and derivative instruments are booked under Reserves in Balance Sheet. b. Gains or losses due to changes in exchange rates are realized only when the foreign currency is repatriated to domestic currency or the foreign currency is used to pay foreign obligations, or upon maturity of an FX forward or option contract involving domestic currency. Therefore, any FX gains or losses arising from the sale of third currencies to USD or vice versa and re-investments shall continue to be treated as unrealized FX gains or losses.	a. 45% b. 27%	• The purpose of central bank acquiring foreign currency assets and liabilities is to attain the central bank's objective, not to make profits. • Translation and transaction of foreign currencies with other foreign currencies is not the ultimate purpose of foreign currencies ownership.
2. Subsequent measurement of financial assets: a. Both domestic and foreign securities are valued at fair market value. Unrealized gains or losses are booked under Reserves in Statement of Financial Position. b. Domestic securities are valued at Lower of Book Value or Market Value. Gold is valued at 90% of the daily average price quoted by London. Unrealized gains or losses are booked under "Revaluation Reserves" in Statement of Financial Position. c. Debt securities are measured at the amortized cost while equity securities are measured at the acquisition cost.	a. 45% b. 9% c. 9%	• The treatment of assets revaluation is specifically provisioned by the law. • The more conservative approach is more suitable for the central bank. • Preventing distribution of unrealized gains. • Securities owned by central bank are to attain the objectives of the central bank, not to make profits.
3. Measurement of FX Swap for monetary operations: It is not treated as derivative instrument, but lending and borrowing. The difference between the spot and forward exchange rates shall be treated as interest income or interest expense on a time proportion basis.	9%	In order to reflect the objective and nature of CB transactions, as FX Swap contract is one of instruments used to influence liquidity conditions in the domestic money market, so the same treatment as a bond repurchase agreement has been used.

In the focus group discussion, it is found that there are two key drivers that trigger central banks in SEACEN economies to adopt the IFRS or national version of the IFRS. Firstly is the pressure from the IMF for the reinforcement of transparency. During the Asian financial crisis of 1997-2002, many SEACEN central banks had received economic support from the IMF. As a high quality international accounting standard, the IFRS is characterized as a principle-based standard and requires extensive disclosures (Daske et al., 2008). These characteristics are expected to increase the transparency of the central bank.

Even though the IMF's Safeguards Assessment Policy was a mandatory requirement for its members that receive loans through any of available credit facilities, there are some variations in adopting the IFRS as dictated by the laws and regulations in each economy. For example, the central bank law may allow the central bank to not comply with generally accepted accounting principles for particular areas that are common practices for the central bank. That is, the central bank may be able to adopt the IFRS with modifications.

Secondly, the IFRS or the national version of the IFRS is a better choice in the absence of a globally accepted central bank specific accounting standard. The respondent from the CBSL suggests that the IFRS is considered beneficial to the country adopting such standards for:

1. Attracting foreign investors for its sovereign bond issues, government securities;
2. Obtaining a better credit rating for the economy;
3. Drawing favorable considerations from international investors, multinational lending/donor agencies because of uniformity and comparability of the financial statements; and,
4. Adding value to the economy, through the "fair value concept" of the IFRS as it gives the real market picture in the financial statements.

Despite the benefits of attracting foreign direct investments, there are inherent limitations when the IFRS is applied for "not-for-profit entities", especially when the law is silent on central banks making modifications on the accounting standards they apply. One central bank raised the issue of the possibility of distributing unrealized profits because of the fair value concept of the IFRS, especially when the law is silent on such an issue. Another example is the application of IAS 37 which might be not suitable for the central bank. IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* outlines the accounting for provisions (liabilities of uncertain timing or amount), together with contingent assets (possible assets) and contingent liabilities (possible obligations and present obligations that are not probable or not reliably measurable). It would not be possible for central banks to make provisions for possible future losses due to exchange and interest rate fluctuations. The recognition of these potential losses is not allowed under IAS 37 which states that a provision in the balance sheet can only be recognized with strict and specific conditions when (i) the entity has a present obligation (legal or derived) as a result of past events; (ii) it is probable that economic outflow of resources will be required to settle the obligation; and, (iii) the amount is reliably estimated.

The respondent from CBSL suggests additional disclosures to overcome such a problematic situation. Any lapses in the IFRS where it is silent due to unique objectives and functions of the central bank compared to commercial entities, could be addressed by providing additional disclosures. The recourse to having additional disclosures would explain the accounting treatment in detail and the relevant central bank functions to the public and other stakeholders in a more lucid manner. Furthermore, additional disclosures would be able to explain recent phenomenon such as the central bank's role in building up reserves (buffers to withstand shocks), and capital erosions, if any, that would result as an outcome of activities that take place in fulfilling the economic stability objectives for the greater welfare of the public.

Since each central bank operates under different laws and circumstances, there is no single solution to fit all. In general, the more autonomy a central bank has in managing its finance, the more space it has in attaining a financial reporting framework which best fits its needs.

(iv) The Accountability and Transparency of Central Bank Financial Statements

The IMF has been an advocate of transparency in central bank financial reporting. According to the IMF (2000), the accountability of central banks can be manifested as follows:

1. Obligation to disclose operating expenses and income of the central bank. This information can improve public confidence regarding the integrity of the central bank and its ability to carry out its public functions effectively;
2. Obligations in setting the guidelines, rules, regulations regarding the principles underlying the behavior and actions of central bank officials and staff;
3. Under certain conditions, the government may have the authority to take over the central bank's monetary policy. The mechanism is a way to improve the accountability of both the central bank as well as the government; and,
4. The selection procedure and the termination of central bank officials. Such procedures should be disclosed to the public so that it will know and be confident about the accountability of central bank officials.

The audited financial statements of the central bank are a means to demonstrate the accountability of central bank activities to the public. It is supported by the IMF transparency code (Sullivan, 2014) which states that:

> *"Regular disclosure of the central bank's audited financial statement of its operations (covering its open market operations, foreign exchange operations, and any other market activities) promotes ex post accountability of the central bank with regards to its operations."*

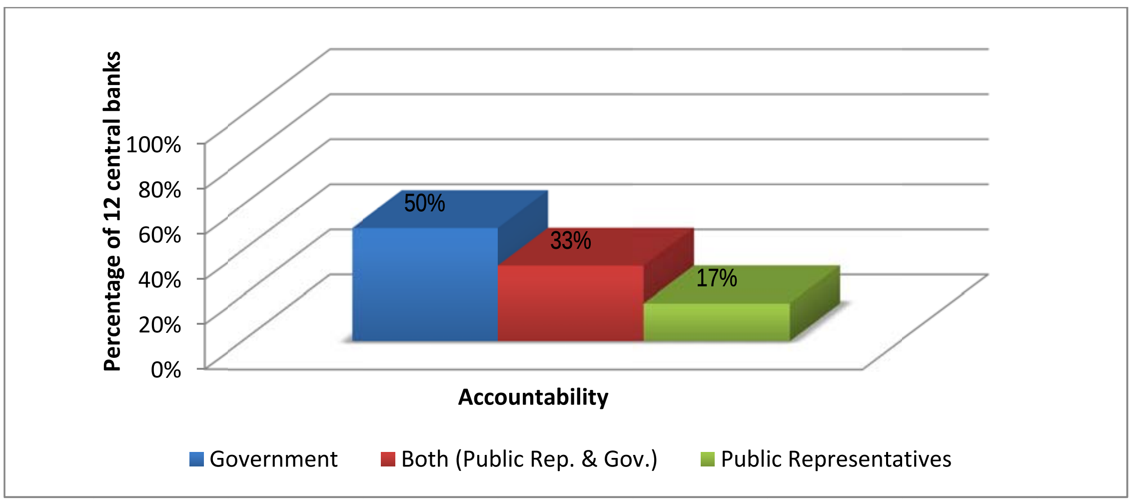
Sullivan (2014) explains that the accountability of the central bank should be viewed from two aspects - first, from the aspect of the efficiency in using its resources, and second, from the aspect of the effectiveness in achieving its objectives. In line with Sullivan (2014), the IMF (2000) states that the financial statements of the central bank should be able to describe the accountability of the central bank, both from the aspect of efficiency in the use of resources and also the effectiveness in achieving the objectives of the central bank.

The survey in this Section focuses on three indicators of accountability suggested by the IMF (2000). First, to whom central banks should report to. Second, whether the central bank is required to submit financial statements which have been audited by an independent auditor to the public. Third, whether the central bank discloses its operating expenses and income to the public in its financial statements.

(a) Obligation to Report to Public Authority

According to the survey, half of the central banks surveyed (50%) have obligations to report to the government, while 33% of them are accountable to both government and public representatives and 13% are accountable to the public representatives. The result is presented in Figure 6.

Figure 6
Ownership and Accountability of Central Banks



(b) Obligation to Submit Audited Financial Statements to the Public

Responses to the survey indicate that all sampled central banks must have their financial statements audited by an independent auditor. Despite the application of the IFRS which is closely related with independent accounting firms, the survey shows that 75% of respondents were audited by the State Auditor General and only 25% were audited by accounting firms (Table 3). One central bank confirms that its auditor is one of the big 4 international accounting firms.

Table 3
Financial Reporting Framework and Auditor

Financial Reporting Framework	Total	Auditor	
		State Auditor – General	Accounting Firm
Own Accounting Standards	5	3	2
Fully IFRS	4	3	1
IFRS/National IFRS with modification	2	2	
Fully National IFRS	1	1	

Based on publicly available information, 11 out 12 of central banks surveyed published their financial statements as described in Table 4. One central bank did not publish its financial statements due to the confidential nature of related information. Two central banks that apply the IFRS opt to publish a partial version.

Table 4
Components of Financial Statements

Financial Reporting Framework	Total	Published Financial Statements (English version)						
		Balance Sheet	Statement of Income	Statement of Comprehensive Income	Statement of Cash Flows	Statement of Changes in Equity	Notes to Financial Statement	Other
Own Accounting Standards	5[17]	4	4	0	1	1	3	1
Fully IFRS	4	4	3	4	3	3	4	0
IFRS/National IFRS with modification	2	2	2	2	2	2	2	0
Fully National IFRS	1	1	1	0	0	0	0	0

(c) Disclosures of Operating Expenses and Income of Central Bank

Based on the published financial statements, we find that all central banks disclose their operating expenses and incomes to the public through the statement of income or statement of comprehensive income. There are variations in the ways central banks present their expenses and income. 82% of them disclose the information based on the nature of

[17] One central bank surveyed does not publish its financial statements due to confidentiality concerns. However, it still reports to the representatives of the public.

expenses and income, while 18% disclose it by combining the function and nature of the accounts. However, the level of disclosure depth varies amongst central banks.

(v) The Governance of Central Banks' Accounting Standard Setting

The independence of the standards setting body is one major aspect of good governance in central bank accounting standards setting (Djakman and Rahadian, 2011). An independent body for setting the accounting standards for the central bank, will promote a higher quality of accounting information and minimize the information asymmetry between the central bank officials and the users of financial statements.

In relation with the choice of accounting standards, according to results of the BIS Survey from Archer and Moser-Boehm (2013) as previously presented in Figure 1, it is a common practice that the Central Bank Law specifies the specific accounting standards to be adopted by the central bank, while others are given authority to set their own accounting standards. According to Djakman and Rahadian (2011), when the Central Bank Law provides the authority or when the law is silent on the selection of accounting standards to be applied, the different practices can be summarized as follows:

1. Set by the Central Bank itself under the decision of the Governor/Board.
   This approach is followed by most of central banks around the world. Since the majority of central banks are independent from the government and unique in the economy, they set their accounting frameworks under the decision of their own Governor/Board.

2. Set by decision-making body whose members consist of central banks in a region/jurisdiction.
   The ECB is one example taking this approach. The accounting framework of the ECB is under decision of the ECB Governing Council. The ECB Governing Council is the main decision-making body of the ECB. It consists of six members of Executive Board, plus the governors of the national central banks of the 19 European System countries. The ECB has developed its own accounting guidelines to be adopted by its members. During the development process, the primary focus was not on the finding of harmonized accounting techniques and reporting guidelines; but rather the importance attached to the idea that the guidelines should serve as fundamental central banking principles. The rules had to be tailor-made to suit the specific nature of the European System central banks. Rules were endorsed after their impact on the equity of the European System central banks had been fully assessed (Merriman et al., 2014).

3. Set by independent standards setting body in one country.
   The independent standard setting body was established with the main tasks of developing the accounting framework for the central bank. The body consists of representatives from the accounting standards setting body for commercial entities, academicians, auditor, government, financial authority services, as well as the experts in central bank accounting framework. Bank Indonesia adopted this approach.

Our survey found that in relation with the setting of the central bank financial reporting framework, several SEACEN central banks are mandated by law to adopt the IFRS or national version of the IFRS, while others are given the authority to develop their own accounting standards. On the other hand, there are two central banks that adopted the IFRS voluntarily (see Table 5).

Table 5
Relations of Legal Provision and Financial Reporting Framework

Legal Provision of Central Bank Financial Reporting Framework	Total	Fully IFRS	Fully National IFRS	IFRS/ National IFRS with Modification	Own Accounting Standards
Law specifies financial reporting framework must be used	3	1	1	-	1
The central bank law specifies the accounting standards that the central must use for financial reporting but allows the Board to specify exceptions.	4	1	-	2	1
The central bank law mandates the Board to determine or develop the accounting standards to be used.	2	-	-	-	2
The central bank law does not specify the accounting standards that the central bank must use nor give mandate to develop its own accounting standards.	3	2	-	-	1

One (1) central bank had its accounting standards developed through a similar setting process as the commercial accounting standards, while the others developed or modified their own accounting standards internally. The commercial accounting standards are commonly set by independent bodies and the standard setting processes follow several steps including public hearings and if necessary, also limited hearings before the standards are approved.

Part III: The Users' Perspective on Central Bank Losses and Negative Capital

In this Section, we attempt to find out how stakeholders perceive the central bank and its financial statements. However, since there was no direct access to central banks' primary stakeholders, i.e. parliament and government, experiences of central bankers in interacting with these concerned stakeholders were taken into consideration for the analysis. In particular, we are concerned about the users' perspective on central bank losses and negative capital. Studies have suggested that the accounting practices for central bank operations could affect the profit or loss (Dziobek and Dalton, 2005). In particular, central bank losses were recorded by countries in Africa, Europe, Latin America and the Asia Pacific region during the 1980's and 1990's that reflected many factors, including operating and valuation losses, and subsidies.[18]

There are two different views on capital losses and negative capital on the central bank, as follows:

1. Central bank losses are a concern as it will cause negative capital. Negative capital will threaten the central bank's credibility and independence in conducting monetary policy (Jeanne and Svensson, 2007). The IMF recommends that the government recapitalize or make capital injections in the form of cash or securities to cover the deficit (Dziobek and Dalton, 2005). In the past, there were several countries that required the injection of government funds to achieve the central bank's minimum capital levels, such as Indonesia and Thailand.
2. Central bank losses and a negative capital will not interfere with the operations of the central bank. The central bank can continue its operation despite losses or negative capital. The Fed Reserve, Bank of Canada, and the Deutsche Bundesbank are examples of central banks that continue to operate with zero capital without any material impact on their policies (Stella, 1997).

In relation to financial stability, 30% of central banks find that the bottom line in central bank financial statements is the central object of stakeholders' criticism. Surprisingly, 90% of central banks suggest that accounting standards applied should be able to support the stability of profit. Some central banks, especially those which have large amounts of international reserves and apply the IFRS or national IFRS, experience volatility in their profits and are of the view that central banks should build provisions to cover losses. This finding is in line with papers written by central bank experts in the past decade on central bank independence and its link with central bank financial strength (Dziobek and Dalton, 2005). Should central bank policy result in losses, this may raise public curiosity on central bank financial management. Central bank policy can be affected and the losses may, in fact, impair the effectiveness of monetary or exchange rate policy.

Regarding the question of whether accounting standards applied should favor the stability of equity, only 40% of the respondents support the idea. Proponents of the idea argue that a central bank should have stable financial strength, which is an important basis for effective implementation of independent monetary policies. On the other hand, some respondents feel that negative capital is not an issue since the laws have taken this into consideration to be accommodated by accounting standards. The latter argument is also in

[18] There are two main causes of central bank losses. First is the high burden of open market operations in the effort of the central bank in controlling inflation through the issuance of debt instruments to attract money supply. This especially apparent when the central bank issues its own debt securities, which implies that the central bank has to bear the burden of large interest. Second is the foreign exchange loss or decline in the value of investments in foreign currency due to the appreciation of the domestic currency, which are risks mainly faced by central banks with high foreign currency assets. These losses will reduce the capital that could lead to negative capital.

line with previous research (Stella, 1997) which shows that even though financial weakness could impair the central bank's objective of maintaining price stability, it is evident that central bank can still successfully operate with negative equity.

Part IV: Perspectives on Variation of Financial Reporting Practices amongst Central Banks

All central banks surveyed confirm that their primary stakeholders have overall knowledge regarding the central banks' objectives, primary activities and how the central banks differ from commercial banks. The stakeholders are also perceived to understand the objectives of central bank financial statements with only 9% doubting stakeholders' understanding. However, the findings of the focus group discussions suggest differently. The results suggest that each stakeholder group seems to have different level of knowledge of central banks and their financial statements. Some groups might consider that central bank operations are similar to commercial entities, especially in the case of central bank losses and negative capital. It is a major challenge for the central bank, through its financial statements, to convince the public and stakeholders that profit is not a measure of the central bank's performance, but indicates the impact of the central bank policy and functions to achieve its objectives.

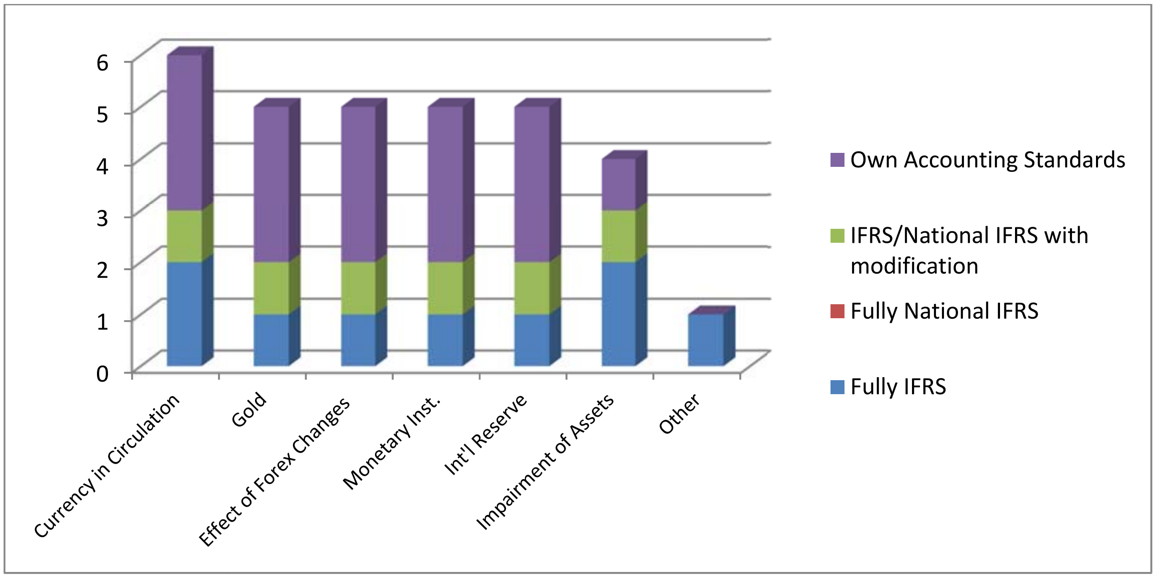
The survey also attempts to uncover how central banks view existing variations of central bank financial reporting practices. 75% of the respondents states that there should be central bank-specialized accounting standards. One respondent of a central bank which applies a national IFRS with modifications states that some transactions of the central bank may be performed with different purposes from commercial entities, e.g., gold, foreign exchange revaluation and derivative instruments. There are also unique central bank transactions such as liquidity injections or absorption activity for the financial system. Therefore, central bank-specialized accounting standards would be useful to improve the comparability aspects of central bank financial statements. One respondent of a central bank that developed its own accounting standards suggests that central banks should develop more prudent and specialized accounting standards in order to ensure sound financial capacity for fulfilling their duties. Two other respondents add that it would be easier for the preparers of central bank financial statements to refer to those accounting standards. Specialized accounting standards could also help the public in understanding a central bank's role more clearly.

However, developing central bank-specialized accounting standards is a challenging task. First, the standards should be developed by a global accounting standards setting body. Research or discussion on the needs of such specialized standards have been going on for more than a decade, but up to now, the IASB, as the global accounting standards setting body, has yet to have a plan to include central banks in its purview. However, the International Public Sector Accounting Standards Board (IPSASB) has started working on public sector financial instruments. In its meeting in June 2015, the IPSASB agreed to develop a consultation paper (CP) covering monetary gold, currency in circulation and IMF-related transactions. The IPSASB perceives these issues primarily related to monetary authorities and, therefore, are relevant to a different constituency (Ernst and Young, 2015). While central banks cannot expect the IPSASB to release those standards any time soon, it is quite a significant progress because central banks rarely use the IPSAS, except RBNZ.[19] Once the standards are launched, there might be a significant global shift in central bank financial reporting frameworks.

Second, the specialized accounting standards should be applicable and consistent with local central bank laws. Although located in the same region, the survey shows that Central Bank Acts vary among the economies. As the Acts affect the central banking operations and reporting substantially, developing specialized accounting standards which are credible and universal is a difficult task.

It can be gleaned that 25% of surveyed central banks are applying for the full adoption of the IFRS or national equivalent of the IFRS. The respondents noted that the IFRS or national equivalent of the IFRS can accommodate central banking activities and that the IFRS is seen as a support in sourcing foreign assistance. However some central banks that do not apply the IFRS, argue that each central bank has its own policy and is operating under different markets and circumstances.

Figure 7
Recommendation of Accounting Treatment Conventions



Despite the uniqueness of each central bank, there is, nonetheless, some uniformity in activities. As seen in Figure 7, six (6) out of the 12 respondents suggest that these central bank transactions require conventions of accounting treatment.

[19] Please see footnote 7.

The discussion on the need for accounting treatment conventions for some common activities of the central bank are as follows:

1. Accounting for Currency in Circulation

One transaction that is conducted by a central bank and which is not found in other entities, whether commercial or government, is related to currency in circulation. Currency in circulation represents a liability of the central bank, but it does not indicate a claim against specific assets of the central bank and has no maturity date.

The IFRS' definition on asset and liability does not apply to currency in circulation. This shows up the IFRS' lack of reference points for traditional central bank transactions. However, there is an informal convention among central banks on how to book currency in circulation.

2. Accounting for Gold

Many central banks still hold significant quantities of gold bullion. The IFRS, which is written primarily for commercial entities, does not provide a straightforward guidance for this issue. The study by Sermon (2011) suggests that gold is in a class of its own. The IFRS' closest approach to be used is deciding on whether gold bullion is a financial instrument or commodity. But none of the approach is deemed appropriate. Gold bullion cannot be classified as financial instrument and although it is highly liquid, there is no contractual right to receive cash or another financial asset inherent in bullion.

When approached as a commodity, the IFRS on *Inventories* excludes the application to "*commodity broker-traders who measure their inventories at fair value less costs to sell.*" Central banks are not gold traders and they rarely actively trade gold bullion in a short period of time.

Central banks around the world also seem to have an informal agreement of how they should book and report gold bullion. Gold bullion always takes the highest rank in a central bank's list of assets. Some central banks value the bullion at fair market value, and its cumulative fair value changes stay in the balance sheet until the bullion is sold. Some other central banks, especially ones that apply the IFRS, let the bullion fair value changes go to the statement of income while at the same time adjust the asset value in the balance sheet. These fair value changes can be transferred to a reserve without distribution.

3. Accounting for Monetary Instruments

Reserve requirements and central bank securities are still commonly used monetary instruments in the SEACEN region. However, some central banks have started to employ government securities, reverse repo operations and also derivative instruments as policy tools.

Some central banks find the fair value measurement demanded by the IFRS for government securities and derivatives not appropriate. Although government securities have fair market value, central banks hold government securities for the attainment of central bank objectives and not for profit making

The same problem applies to foreign exchange swaps (*FX Swap*) as one of the instruments used to influence liquidity conditions in the domestic money market. The central bank might sell foreign currency for domestic currency absorption (*spot leg*), and commit to buy the foreign currency at predetermined times and exchange rate (*forward leg*). The cost of monetary operations lies in the forward points, not in the opportunity gained from exchange rate changes. The central bank does not have a problem in providing domestic currency at the forward leg.

The IFRS requires derivatives to be fair valued as there is no initial investment for derivatives. Fair value differences are the only reported items with regard to derivatives. However, some central banks use a different approach and book *FX Swap* as a collateralized lending or borrowing transaction.

4. Accounting for International Reserves Management

All central banks surveyed manage their countries' international reserves, and lately international reserves have been dominating central bank assets. The foreign currency assets held by central banks are intended to primarily serve as policy instruments, unlike assets held by commercial entities, which are employed as productive resources to generate profits, or assets held by government entities, where they are employed as supporting resources for government policies and operations. Fund placements by central banks are mainly employed as a policy instrument to influence the value of the domestic currency. This context has shaped the investment objectives and the approach of international reserves management, with such criteria as security and liquidity ranking higher in priority for most central banks than investment return (Nugee, 2003).

However, some central banks have a more current view on international reserves management. One respondent states that currently, central banks have become more actively involved in financial instruments trading with a profit motive. It is because only a part of the international reserve assets are maintained as a policy instrument to preserve the value of the domestic currency. Idle reserve assets are usually managed for earning a return in some central banks.

5. Accounting for Effect of Changes in Foreign Exchange Rate

The IFRS accounts for both realized and unrealized exchange gains and losses are to be booked into the statement of income in the period in which they occur. The holding of foreign exchange assets has an impact in the form of the conversion of their value into domestic currency or the conversion of value of inter-currency transactions into domestic currency.

Such treatment has been criticized as "not relevant" for central banks, since the central bank does not intend to seek gains in domestic currency from those kinds of conversion.

6. Accounting for Financial Instruments

The IFRS requires that financial instruments to be classified as trading to be marked to market and associated gains/losses are taken into income which will in turn become a part of the distributable profit. However, these gains and losses are unrealized.

Since the IFRS does not specify rules for distribution, it is possible to treat unrealized gains/losses from the fair value adjustment as part of the net profit, but not necessarily part of the distributable profits. But, when the law does not restrict the distribution of these book profits, which are unrealized, such distributions will affect money creation, impacting inappropriate liquidity additions to the market. This point is also relevant for gains/losses from changing in foreign exchange rate which has been described in point (5) above.

7. Impairment of Assets

Most central banks have granted loans to the government. Some central banks might provide the loans at zero or very little interest rate. In the process, the government might put the loan payment on hold and allocate its budget to other projects considered more urgent.

Under the IFRS, loans to government are classified as loans and receivables and therefore, such assets are carried at amortized cost. Similar to other loans, loans to the government are also subject to impairment tests.

In a normal situation, such loans are considered risk-free and having recoverability since they are to the government. Loans to government are impaired in rare situations when the economy of the country deteriorates substantially. Most of the time, when such a situation occurs, international financial agencies will usually intervene to prevent the crisis from worsening and to provide assistance in the recovery process. Because of this, loans to government usually pass the impairment test.

Impairing loans to the government will not only distort the statement of income but may also have other implications such as the downgrade of the country's credit ratings and loss of investor confidence. Therefore, unless there is indisputable doubt about the recoverability, loans to government are not impaired.

5. Conclusion

Central banks have been regarded as institutions of public policy, not commercial entities. They have evolved from policy institutions to the apex financial institutions of the economies, involved in both development and stability of the overall financial system as well as the economy as a whole. The central bank is a unique entity which has unique characteristics that cannot be found in commercial entities or government. In order to achieve the objectives that are defined by the law, central banks perform duties that give rise to different types of transactions, or similar types of transactions with different goals, when compared with other entities. These have an impact on the significance of the financial information related to such transactions. Therefore, financial information on the transactions carried out by central banks must be interpreted holistically in terms of the achievement of central bank objectives. Thus, we argue that the objective of a central bank's financial statements is to demonstrate the central bank's *accountability* in achieving its objectives, which includes information on the impact of central bank policies on its financial position and surplus deficit. Central bank financial statements are not meant for decision-making on investments by stakeholders. The achievement of central bank objectives is not to be assessed in mere monetary terms. Consequently, central bank financial statements and profits *per se* cannot be used to assess the level of achievement of central bank objectives.

In term of financial reporting, consistent with previous research, we find that there are variations in the financial reporting framework used by central banks in the SEACEN economies. We note that some central banks have established their own accounting standards while others have adopted the IFRS fully. In between, we have central banks adopting the IFRS or national IFRS with modifications. The national IFRS are mostly in line with the IFRS, but the enforcement period of some national IFRS is lagging behind due to difficulties in the process preparation or infrastructure. We also note that while the IFRS is considered as the benchmark in terms of accounting standards, it has several limitations when applied on central banks. For instance, the IFRS cannot fully represent costs of central bank policies. It lacks references for central banks' classic transactions such as currency in circulation and gold; and, the fair value concept promoted by the IFRS causes cyclical problems in profits reported by the central bank. While central bank laws do not restrict the distribution of these book profits, which are unrealized, such distributions will, however, trigger money creation and have impacts on inappropriate liquidity additions to the market.

This study finds that there are different views as to whether the bottom line of central bank financial statements is important. There is, nonetheless, agreement that accounting standards applied should be able to support the stability of profit. While the profit or loss of the central bank is only to show the impact of central bank monetary policy, the volatility of the profit or loss or the losses experienced by the central bank may raise public concern on central bank financial management.

In conclusion, it should be noted that there has been no accounting framework that look into the underlying assumptions, principles and limitations of central bank financial statements. This brings us to the question of whether there should be specialized accounting standards for central banks. Proponents of specialized accounting standards recommend the enhancement of conventions of accounting treatments for some specific transactions, namely, (i) currency in circulation; (ii) gold; (iii) effect of changes in foreign exchange rate; (iv) monetary instruments; (v) international reserves management; and, (vi) impairment of assets. However, development of specialized accounting standards for central banks will require extensive time and effort as these need to be accepted internationally, made more complex by the fact that central banks operate in different jurisdictions under their respective domestic laws. While the IPSASB has started the work on developing a consultation paper on central bank-specific transactions such as currency in circulation and monetary gold, these standards are not expected to be completed any time soon.

References

Archer D. and P. Moser-Boehm, (2013), “Central Bank Finances,” Bank for International Settlements.

Bank Indonesia, (2011), “Kerangka Dasar Penyusunan dan Penyajian Laporan Keuangan Bank Indonesia,” Bank Indonesia.

Blinder A.S., (2010), “How Central Should the Central be?” *Journal of Economic Literature.*

Blinder A.; C. Goodhart; P. Hildebrand; D. Lipton and C. Wyplosz, (2001), “How Do Central Banks Talks?” *Geneva: International Center for Monetary and Banking Studies*.

Caruana, J., (2012), “Why Central Bank Balance Sheets Matter,” *Are Central Bank Balance Sheets in Asia Too Large*, Vol. 66, pp. 2-9, Bank for International Settlements.

Daske, H.; L. Hail; C. Leuz and R. Verdi, (2008), :Mandatory IFRS Reporting Around the World: Early Evidence on the Economic Consequences,” *Journal of Accounting Research*, 46(5), pp. 1085-1142.

Decision ECB/2010/20, 2010, Available at: https://www.ecb.europa.eu/ecb/legal/pdf/l_03520110209en00310068.pdf

Djakman C. and Y. Rahadian, (2011), “Pelaporan Keuangan untuk Manajemen dan Para Pemangku Kepentingan Menuju Standar Akuntansi Bank Sentral Indonesia,” Bank Indonesia.

Dziobek M. C. H. and M. J. W Dalton, (2005), “Central Bank Losses and Experiences in Selected Countries,” No. 5-72, International Monetary Fund.

Ernst and Young, (2015), IPSAS Outlook, March.

Filardo, A. J. and J. Yetman, (2012), “The Expansion of Central Bank Balance Sheets in Emerging Asia: What are the Risks?” *BIS Quarterly Review,* June.

Firdhaus F., (2010), “Analisis Kebutuhan Standar atau Pedoman Akuntansi untuk Bank Indonesia: Komparasi dengan Standar Akuntansi Keuangan Indonesia dan Pedoman Akuntansi European Central Bank, Federal Reserve Banks, Bank of England, Reserve Bank of Australia dan Reserve Bank of New Zealand,” Karya Akhir, Magister Akuntansi, Fakultas Ekonomi Universitas Indonesia (MAKSI - FEUI).

International Monetary Fund, (1999), Code of Good Practices on Transparency in Monetary and Financial Policies: Declaration of Principles.

International Monetary Fund, (2000), “Supporting Document to the Code of Good Practices in Monetary and Financial Policies – Glossary of Key Terms,” In D. Lefort, ‘Transparency and Accountability of Central Banks,’ July.

International Public Sector Accounting Standard (IPSAS) Board, (2014), “IPSAS 28 – Financial Instruments: Presentation,” Handbook of International Public Sector Accounting Pronouncements, Volume II, International Federation of Accountants (IFAC).

International Public Sector Accounting Standard (IPSAS) Board, (2014), “IPSAS 29 – Financial Instruments: Recognition and Measurement,” Handbook of International Public Sector Accounting Pronouncements, Volume II, International Federation of Accountants (IFAC).

Jeanne, O. and L.E.O Svensson, (2007), “Credible Commitment to Optimal Escape from a Liquidity Trap: The Role of the Balance Sheet of an Independent Central Bank,” *American Economic Review*, 97, pp. 474-490.

Kurtzig J. and Mander B., (2003), “Survey of Central Bank Accounting Practices,” In ‘Accounting Standards for Central Bank,’ Neil Courtis and Benedict Mander (Eds.), pp. 21-46.

Kurtzig J., (2003), “Coping with Accounting Standards and Central Bank Transparency,” In ‘Accounting Standards for Central Bank,’ Neil Courtis and Benedict Mander (Eds.), pp. 311-317.

Kurtzig J.; C. Hemus and I. Goodwin., (2003), “Accounting for Reserves,” In ‘How Countries Manage Reserve Assets,’ Robert Pringle and Nick Carver (Eds.), pp. 249-269.

Merriman N., (2003), “Financial Reporting in the Eurosystem,” In ‘Accounting Standards for Central Bank,’ in Neil Courtis and Benedict Mander (Eds.), pp. 135-151.

Merriman N.; O. Morelle and K. Apostolou, (2014), “The Eurosystem Accounting Framework: A Central-Bank Specific Accounting Standard,” In ‘Financial Independence and Accountability for Central Banks,’ K. Sullivan and M. Horakova (Eds.), pp.159-179.

Minzoni M., (2014), “The Challenges for IFRS Implementation by Central Banks,” In ‘Financial Independence and Accountability for Central Banks,’ Sullivan K. and M. Horakova (Eds.) pp.143-158.

Nugee J., (2003), “Accounting for Reserves,” In ‘Accounting Standards for Central Bank,’ Neil Courtis and Benedict Mander (Eds.), pp. 193-200.

Paramonova T., (2003), “No Plain Sailing to International Accounting Standards,” In ‘Accounting Standards for Central Bank,’ Neil Courtis and Benedict Mander (Eds.), pp. 223-255.

Sermon C., (2011), “Accountancy Golden Puzzle,” In Central Banking Publication Workshop on Gold as a Reserve Asset.

Stella P., (1997), “Do Central Banks Need Capital?” *IMF Working Paper*, No. 97/83.

Sullivan K., (2005), “Transparency in Central Bank Financial Statement Disclosures,” International Monetary Fund.

Sullivan K., (2003), “Profit, Dividends and Capital – Consideration for Central Bank,” In ‘Accounting Standards for Central Bank,’ Neil Courtis and Benedict Mander (Eds).

Sullivan K., (2014), “Objective of Central Bank Financial Reporting,” In ‘Financial Independence and Accountability for Central Banks,’ K. Sullivan and M. Horakova (Eds.), pp. 123-141.

Annex 1

Questionnaire on Central Bank Financial Reporting: A Preliminary Study in SEACEN Economies

Introduction

This questionnaire seeks to gather information for the purpose of SEACEN customised research project regarding the main principles in the central bank financial reporting setting process amongst SEACEN members' central bank.

The objective of the study is to address and identify conventions and common practices among SEACEN members regarding the main principles in the central bank financial reporting and the governance of accounting standards setting process.

The result of this survey will be distributed to participating SEACEN member of this research. We will add the data to our database of comparable data on central bank finances, for further analytic work. Results may be included in material prepared for central banks or in publications, but only in fully anonymous form. The data of this survey will not be disclosed individually.

<u>Please submit by 25 June 2015</u>

Many thanks for your assistance

We sincerely thank you for taking the time to complete this questionnaire. Please send your response to jamie@seacen.org. If you have any queries regarding this survey, you are very welcome to send us email at a_hastowo@bi.go.id or to call at +62 21 2981 8337

About this research

This research is one SEACEN customised research program in 2015. The research is a collaborative project of SEACEN members. Research team members held the first meeting to discuss the research proposal in Jakarta 29-30 April 2015. This questionnaire is a part of the data collection method in this research. The data colletion is expected to complete by end of June 2015. The final report and findings of the research will be published to SEACEN members by end of 2015.

***Respondent contact details:**

We ask for your contact details in the event that we need clarification in relation to your responses to this questionnaire. The contact details will not be used for any other purpose. We will not disclose contact details on the research report.

Name:	
Position or Title	
Organisation:	
Contact phone number:	
Contact e-mail address:	

Alternate contact detail

Name:	
Position or Title	
Organisation:	
Contact phone number:	
Contact e-mail address:	

1. The roles of the central bank in the country's economy development and institutional framework for central bank

In accordance with the mandate provided by law:

1.1. The central bank shall perform the following functions (could be multiple answers):

- ☐ Promotes monetary stability, formulate and implements monetary policies.
- ☐ Promotes sound and efficient national payment systems.
- ☐ Manages the country's international reserves.
- ☐ Promotes financial system stability.
- ☐ Acts as lender of the last resort for banking institutions.
- ☐ Acts as a banker of the government.
- ☐ Manages the public debts.
- ☐ Other, please describe:

1.2. In terms of accountability, the central bank is held responsible to:

- ☐ Public representatives, i.e. House of Representatives, Parliament.
- ☐ State i.e. Ministry of Finance or Treasury.
- ☐ Other, please describe:

1.3. Which statement below best describes the ownership of the central bank?
Please select one answer.

- ☐ Fully owned by state (public), *please proceed to question 1.4.*
- ☐ Majority (more than half) owned by state (public), *please proceed to question 1.4*
- ☐ Majority (more than half) owned by private sector), *please skip question 1.4*
- ☐ Half owned by the state (public) and half owned by private sector), *please skip question 1.4*
- ☐ Fully owned by private sector, *please skip question 1.4*
- ☐ Other, please explain:

1.4. In relation to question 1.3., if the central bank is fully owned or majority owned by state (public), to what extent is your central bank financially independent from the state or parliament. *Please tick below the coloumn **Yes** or **No***

	Yes	**No**
The central bank has enough resources appropriate to perform its functions.		
The central bank shall have its annual budget approved by the state (e.g. Treasury or Ministry of Finance, or parliament).		
The central bank has a clear arrangement on how much central bank shall distribute its profit/surplus to the state.		
The central bank has a clear arrangement that central bank shall receive transfer/funds or indemnities from the state if in the period its finance considered vulnerable or had significant losses in its financial statement.		
The central bank considers the provisions of transfers/funds from the state in managing its financial condition.		
The central bank has a special arrangement of return (interest rate) on government deposits in central bank		
Other, please describe: ______________________ ______________________		

1.5. Are there any legal provisions obliging the central bank to guarantee debts incurred by the state?

☐ No
☐ Yes, please describe nature and legal sources:

____
____
____

1.6. Are there any legal provisions obliging the state to guarantee debts incurred by the central bank?

☐ No
☐ Yes, please describe nature and legal sources:

____
____
____

1.7. Are there specific legal provisions obliging the government to recapitalise the central bank (in part or full) under certain circumstances?

☐ No
☐ Yes – partial, please describe nature and legal sources:

____

☐ Yes – full, please describe nature and legal sources:

____
____
____

1.8. Are there specific legal provisions concerning bankruptcy or winding-up the central bank?
- ☐ No
- ☐ Yes, please describe nature and legal sources:

____

____

____

2. The objective of central bank financial statements

2.1. Presentation and audit of financial statements in accordance with the central bank law

2.1.1. Is the central bank required to present financial statements?
- ☐ Yes
- ☐ No

2.1.2. Is it required that the central bank financial statements to be audited by external auditor?
- ☐ Yes, please go to question 2.1.3.
- ☐ No, please proceed to question 2.1.5.

2.1.3. Who does perform the audit of financial statements?
- ☐ Auditor General (State Auditor)
- ☐ Accounting firm
- ☐ Accounting firm appointed by State Auditor

Please proceed to question 2.2.

2.1.4. Do you have auditor engaged to perform a review on the central bank financial statements and no published report was issued?
- ☐ Yes
- ☐ No

Please provide details and an explanation below:

____

____

____

2.2. The objective of central bank financial statements

2.2.1. In your opinion, which statement best describe the main purpose/objective of central bank financial statements:
- ☐ Similar to commercial entities, the objective of financial statements is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions
- ☐ The objective of central bank financial statements is to demonstrate the central bank's accountability in achieving its objectives, which includes information on the impact of central bank's policies on the financial position and surplus deficit of central bank.

☐ Other, please describe:

____
____
____

2.2.2. In relation to question 2.2.1 in your opinion, the presentation of central bank financial statement is intended to :
(from the most significant (5) to the least significant (1)).

	5	**4**	**3**	**2**	**1**
Meet the legal requirements					
Reflect the operations of central bank					
Reflect the attainment of the objective of central bank					
Present financial viability and profitability of central bank					
Present the financial accountability to stakeholder					
Other, please describe: ______________________________ ______________________________					

2.2.3. Do you think the current objective of central bank financial statements relate to the existing objectives of central bank?

☐ Yes, because the purpose financial statements is to demonstrate the accountability of the central bank in achieving its objectives.

☐ Yes-other reasons, please describe:

____
____
____

☐ No, please explain why:

____
____
____

2.3. Users of central bank financial statements

In your opinion, please rank the stakeholders of central bank financial statements below:

(from the most significant (5) to the least significant (1)).

	5	**4**	**3**	**2**	**1**
Public representatives, i.e. house of representatives, parliament					
State, i.e. Ministry of Finance					
Audit institution, i.e. State Auditor					
Economic actors, i,e. domestic and international financial institutions					
International financial organisation, i.e. International Monetary Fund					
Other central banks					

	5	4	3	2	1
Others, please describe: ______________________________ ______________________________ ______________________________					

3. Central bank financial reporting framework

3.1. Which statement does best describe the central bank's financial reporting framework?

- ☐ The central bank law specifies the accounting standards that the central bank must use for financial reporting.
- ☐ The central bank law specifies the accounting standards that the central must use for financial reporting but allows the following body: ___________________________ (e.g. the Board; please specify) to specify exceptions.
- ☐ The central bank law mandates the following body: ___________-______________ (e.g. the Board; please specify) to determine or develop the accounting standards to be used.
- ☐ The central bank law does not specify the accounting standards that the central bank must use nor give mandate to develop its own accounting standards.
- ☐ Other, please describe:

  ____

  ____

  ____

3.2. In line with question 3.1., the central bank uses the following accounting standards or framework[20]:

- ☐ Central bank adopts International Financial Reporting Standards (IFRS) or a national carbon-copy of IFRS.
- ☐ Central bank adopts "National IFRS" (if National IFRS is similar to but not the same as IFRS).
- ☐ Central bank adopts National Generally Accepted Accounting Principles (if National GAAP is substantially different from IFRS).
- ☐ The central bank law does not specify the accounting standards that the central bank must use nor give mandate to develop its own accounting standards.
- ☐ Central bank establishes its own central bank accounting standards, as …
  (Please proceed to question 3.4. in case you select this answer).
  - ☐ set out in law
  - ☐ adopted by central bank board;
  - ☐ other source, as follows:

    ____

    ____

    ____

[20] The question is inspired by 2013 BIS questionnaire.

3.3. In line to your response to question 3.2, how do you describe the level of compliance to accounting standards or framework chosen?

- ☐ Full adoption (slight modification is considered "Full adoption"). *Please proceed to question 3.7.*
- ☐ With any departures.

3.4. If you are using accounting framework that significantly departs from the reference standards (IFRS/National IFRS/ National GAAP), do you explained the departures in the financial statements?

- ☐ Yes
- ☐ No

3.5. In line to your response to question 3.2., if you are not using IFRS (or a national carbon copy version of it) or if you are using accounting framework that significantly departs from the reference standards (IFRS/National IFRS/ National GAAP), please :

a. Summarise the key differences or departures.

____

____

____

____

____

b. Explain briefly the motivation or arguments behind the departure.

____

____

____

3.6. This question is only for the central bank which applies its own accounting standards or applies IFRS / national IFRS / national GAAP with any departures /modification.

The setting process of accounting standards/modification includes the following steps:

Accounting Standards Setting Process	**Yes**	**No**
The accounting standards used are established by Board of Governor	☐	☐
Development of accounting standards is carried out by an independent body outside the central bank.	☐	☐
Prior establishment of the accounting standards, a hearing is conducted to obtain inputs from stakeholders.	☐	☐
The central bank publishes its accounting standards/accounting manuals in the public domain.	☐	☐
The central bank has the modification clearly disclosed in its notes to financial statements.	☐	☐

3.7. In line to your response to question 3.2., do you consider that the current accounting framework has satisfactorily fulfilled the objective of central bank financial reporting?

☐ Yes

☐ No, please describe:

☐ Yes in overall but not in several areas – please describe:

4. Components and elements of central bank financial statements

4.1. Your central bank financial statements consist of (could be multiple answers):

☐ Statement of financial position **or** balance sheet

☐ Statement of surplus deficit **or** Statement of income **or** Statement of profit and loss

☐ Statement of comprehensive income

☐ Statement of cash flows

☐ Statement of changes in equity

☐ Notes to financial statement

☐ Other, please describe:

In your opinion, should central bank not present any of these reports? Please explain why.

4.2. In your opinion, please rank the components of your central bank financial statements, that the main stakeholders (refer to question 2.3.) consider the most (5) to the least significant (1).

Components of financial statements	**5**	**4**	**3**	**2**	**1**
Statement of financial position **or** balance sheet					
Statement of surplus deficit **or** Statement of income **or** Statement of profit and loss					
Statement of comprehensive income					
Statement of cash flows					
Statement of changes in equity					
Notes to financial statements					
Others, please describe :					

4.3. In the history of your central bank, have there been episodes when one or several of the following (or closely related) events or issues made them into headlines, or were the subject of intense discussion between the central bank and government?[21]

No.	Description	Never	Year or period	Summary of event
1.	Public or political demands for access to/appropriations of central bank assets or equity (net worth), or to special dividends.	☐		
2.	Major losses/deficit from exchange rate (incl. sterilisation, interventions)	☐		
3.	Major losses/deficit from other reasons or actions (e.g. lender of the last resort)	☐		
4.	Central bank capital approaching zero or failing below zero	☐		
5.	Persistent negative capital (and possibly, recapitalisation plans or actions)	☐		
6.	Auditor's concerns regarding central bank losses and/or low/negative capital	☐		
7.	A special increase in central bank capital (in addition to or different from established mechanisms to rebuild or maintain capital, in absolute or relative terms)	☐		
8.	Other major events concerning the central bank's financial position, strength or autonomy. Please describe:	☐		

[21] The question is inspired by 2013 BIS questionnaire

4.4. In line with question 4.3., do you think that the central bank should apply accounting standards which support the **stability of equity/net worth**, e.g. deferring losses when the amount is so huge that will cause negative equity/net worth?

☐ No, please explain why:

☐ Yes, please explain why:

4.5. In line with question 4.3., do you think that the central bank should apply accounting standards which support the **stability of profit**, e.g. central bank is allowed to build provision to cover losses?

☐ No, please explain why:

☐ Yes, please explain why:

5. How stakeholders' perspectives on the central bank and its financial statements

Based your experiences interacting with the central bank stakeholders, please provide the following information:

5.1. Do you think the central bank's main stakeholders (consistent with response to question 2.3) have knowledge regarding the central bank objectives, primary activities and how the central bank differs from commercial banks?

☐ Yes, please describe:

☐ No, please describe:

☐ Yes in overall but not in several area (s), please describe:

5.2. Do you think the stakeholders understand the objectives of central bank financial statements?

☐ Yes, please describe:

☐ No, please describe:

☐ Not sure, please describe:

5.3. Do you think the stakeholders consider central bank's profit/surplus as a reflection of its performance?

☐ Yes, please describe:

☐ No, please describe:

☐ Not sure, please describe:

5.4. Do you think that the stakeholders central bank's profit affects (has positive correlation with) development of the country's economy (e.g. the stability of domestic currency value)?

☐ Yes, please describe:

☐ No, please describe:

☐ Not sure, please describe:

5.5. In connection with central bank auditor's opinion regarding the accounting standards used by central banks in the preparation of financial statements:

a. How is the auditor's opinion regarding the accounting standards used by the central bank:
   - ☐ Is appropriate, and do not need to be changed
   - ☐ Is appropriate, but could be refined
   - ☐ Need to be improved
   - ☐ Other, please explain:

b. Has the auditor ever suggested the central bank accounting standard should be in line with the accounting standards used by other central banks?
   - ☐ Yes
   - ☐ No
   - ☐ Other, please describe

c. Any concerns from the auditor regarding the accounting standards used by the central bank, please describe:

6. Variation of practices and financial reporting amongst SEACEN member central banks

6.1. Have you ever read other central banks' financial statements?
   - ☐ No, please proceed to question 6.3.
   - ☐ Yes, please specify the country (s):

6.2. In line with your response to question 6.1. have you ever found difficulties in understanding their financial statements
   - ☐ No
   - ☐ Yes, please specify the area (s):

6.3. Do you think that variation of practices and financial reporting amongst central banks has created incomparability problem?

☐ No, please explain:

☐ Yes, please explain:

6.4. In your opinion, please rank the following qualitative characteristics of financial statements that should be possessed by central bank financial statement?
The most significant (5) to the least significant (1).

Qualitative characteristics of financial statements	**5**	**4**	**3**	**2**	**1**
Understandability *Please explain why :*					
Relevance *Please explain why :*					
Reliability *Please explain why :*					
Comparability *Please explain why :*					
Constraints on Relevance and Reliability *Please explain why :*					
Other *Please describe and explain why :*					

6.5. In your opinion, should there be specialised accounting standards intended for central banks?

☐ No, please explain:

Please proceed to question 6.6.

☐ Yes, please explain:

Please proceed to question 7.

6.6. In your opinion, should there be a convention of accounting treatment for particular central bank's transactions?

☐ No, please explain:

Please proceed to question 7.

☐ Yes, please explain:

Please proceed to question 6.7.

6.7. Which central bank's activities do you think should have a convention of accounting treatment among central bank, particularly in SEACEN economies? (could be multiple answers)

☐ Gold transactions, please explain why:

- ☐ Gold transactions are unique transactions of central bank and have same function amongst central banks.
- ☐ Other reason (s):

☐ Currency in circulation, please explain why:

- ☐ Currency in circulation transactions are unique transactions of central bank and have the same function amongst central banks
- ☐ Other reason (s):

☐ Monetary instruments, including derivative instruments, please explain why:
- ☐ Monetary instruments transactions are unique transactions of central bank and have the same function amongst central banks
- ☐ Other reason (s):

☐ International reserve management, including derivative instruments, please explain why:
- ☐ International reserve management transactions are unique transactions of central bank and have the similar function amongst central banks
- ☐ Other reason (s):

☐ Effect of changes in foreign exchange rate, please explain why:
- ☐ Effect of changes in foreign exchange rate is unique transaction of central bank and has the same function amongst central banks
- ☐ Other reason (s):

☐ Impairment of assets, please explain why:
- ☐ Impairment of assets is unique transaction of central bank and has the similar function amongst central banks
- ☐ Other reason (s):

☐ Other, please describe and explain why:

7. Please write below if you have issues to add:

THANK YOU

This completes your involvement in the questionnaire. Thank you for your participation.

Annex 2

PROJECT LEADERS

Mr. M. Agung Hastowo
Deputy Director
Department of Internal Financial Management
Bank Indonesia

Mr. Tonny Indarto
Senior Financial Analyst
Department of Internal Financial Management
Bank Indonesia

PROJECT TEAM MEMBERS

National Bank of Cambodia

Mr. Ponlork Koy
Deputy of Division
Accounting Department

Mr. Sivalen Roth
Head of Section
Accounting Department

Mr. Chandararith Top
Officer
Governor's Office

Reserve Bank of India

Dr. Jai Chander
Assistant Adviser
Department of Economic and Policy Research

Bank Indonesia

Ms. Linda Kurniawati
Senior Financial Analyst
Department of Internal Financial Management

Bangko Sentral ng Pilipinas

Mr. Romeo S. Diaz
Acting Bank Officer IV
Financial Accounting Department

Central Bank of Sri Lanka

Mr. Ayesh I Ariyasinghe
Senior Economist
Economic Research Department

Ms. Lasanthi Sirimanne
Deputy Chief Accountant
Finance Department

Bank of Thailand

Mrs. Palida Amornsawadwatana
Team Executive
Finance and Accounting Department

Ms. Waewwalai Maneepairoj
Senior Accountant
Finance and Accounting Department