

Meeting: International Public Sector Accounting
Standards Board
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Agenda Item 12

For:
 Approval
 Discussion
 Information

Public Sector Specific Financial Instruments

Objective(s) of Agenda Item

1. The objective of this session is to **consider** key issues in this Issues Paper and **review the draft** Consultation Paper (CP) on Public Sector Specific Financial Instruments; and to **provide directions** for further developing the CP.

Material(s) Presented

Agenda Item 12.1	Draft Issues Paper, Public Sector Specific Financial Instruments
Agenda Item 12.2	Draft Monetary Gold Chapter of the CP, Public Sector Specific Financial Instruments (mark up version available upon request)
Agenda Item 12.3	Draft Currency in Circulation Chapter of the CP, Public Sector Specific Financial Instruments

Issues Paper, Public Sector Specific Financial Instruments

Objective of the Issues Paper

1. The objective of this session is to **consider** key issues in this Issues Paper and **review the** draft Consultation Paper (CP) on Public Sector Specific Financial Instruments; and to **provide directions** for further development of the CP.

Background

2. At its March 2015 meeting, the IPSASB discussed a revised draft of the introduction and objective and monetary gold chapters. The IPSASB provided directions to staff regarding the further development of the CP.
3. A revised draft of the introduction and monetary gold chapters has been included as Agenda Item 12.2. A marked-up version of the draft is available upon request.
4. A new draft chapter on currency and coin in circulation has been included as Agenda Item 12.3.
5. This Issues Paper seeks the IPSASB's views on the key issues identified in revising the draft chapters.

Key Issues

Chapter 3 – Monetary Gold

6. Update of the definition “physical” gold to “tangible” gold based on IPSASB feedback in March, see paragraph 3.18.
7. Several revisions were made, based on IPSASB feedback in March, to revise the discussion for the reason monetary authorities hold gold assets. The previous version, linked the objectives monetary authorities have in holding gold assets, to the measurement options which satisfy those objectives. The IPSASB determined that a compelling argument had not been made for linking historical cost to operational capacity. It was decided that it is better relate the intentions monetary authorities have in holding gold assets to the measurement options, similar to how the IPSAS financial instruments standards have been developed.
8. Changes have been included to reflect the change from an “objectives” to an “intentions” approach. Additional material has been included which links the historical cost option to exiting IPSAS literature (where the historical cost model) is used. The substantive changes are included in the following paragraphs; 3.6, 3.41–3.49, 3.55–3.64, 3.65–3.74 and 3.75–3.76.

Matter(s) for Consideration

1. The IPSASB is asked to:
 - (a) **Confirm** that the amended definition of tangible gold included in 3.18 is appropriate; and

- (b) **Confirm** if the amendments included for the revisions to introduce an intentions approach (substantively included in paragraphs; 3.6, 3.41–3.49, 3.55–3.64, 3.65–3.74 and 3.75–3.76) adequately capture the requested changes, or alternatively suggest amendments.

Chapter 3 – Monetary Gold – Option vs. Alternative

9. In considering the revisions to the monetary gold chapter, TBG members questioned whether the IPSASB had a view as to if the CP was advocating for a business model approach to developing guidance. Would such an approach allow preparers an option, based on their intentions (similar to the IPSAS 28–30 where financial instruments are designated at inception into a particular class which impacts accounting requirements). Alternatively, is the IPSASB asking for views on the approaches from constituents, to use in developing one specified option in a future ED. The TBG considered this to be an important issue for the IPSASB to consider at this time, given the potential implications which may arise later in the project.

Matter(s) for Consideration

2. The IPSASB is asked to **Confirm** if the use of an the intentions based approach, is meant to develop guidance, which would provide options for accounting for monetary gold, based on intentions, or, alternatively, ask constituents to provide a preferred option, to narrow and develop future guidance.

Chapter 2 – Currency Issued by the Entity: Chapter Objective

10. The first draft of the currency issued by the entity chapter has been developed, using a similar approach to the development of the monetary gold chapter.
11. The chapter objective has been developed as follows:

An entity shall account for currency in circulation in a manner that helps users of its financial statements assess:

- The impact of currency in circulation on the entity's financial performance and financial position;
- The nature and extent of risks arising from distributing currency in circulation, and how the entity manages those risks; and
- The types (different categories and series) of currency in circulation issued by the entity.

Matter(s) for Consideration

3. The IPSASB is asked to **Indicate** whether the chapter objective for currency in circulation is appropriate.

Chapter 2 – Currency Issued by the Entity: Definitions and Scope

12. The proposed definition considers the definitions and descriptions in the Balance of Payments International Investment Position Manual–Sixth Edition (BPM6). The following definition is proposed for currency in circulation:

- (a) “Physical notes and coins with fixed and determinable values that are legal tender issued by the monetary authority that is, either that of an individual economy or, in a currency union that the economy belongs.”

13. Paragraphs 1.13–1.15 include further descriptions related the components of the definition.

Matter(s) for Consideration

4. The IPSASB is asked to **confirm** the definition of currency in circulation or provide amendments.

Chapter 2 – Currency Issued by the Entity: Purchase and Production

14. Monetary authorities are required because of legislation to maintain currency in circulation in most jurisdictions. To do this, an inventory of new notes and coins is required. The costs incurred at each step in the inventory cycle meet the definitions of inventory in IPSAS 12.9. Further, IPSAS 12.11 states that: *inventories encompass goods purchased and held for resale... Inventories also encompass finished goods produced, or work-in-progress being produced, by the entity. Inventories also include (a) material and supplies waiting use in the production process, and (b) good purchased or produced by an entity.* Therefore, the chapter notes that costs related to the purchase of materials, and production of currency, are appropriate costs for recognition as inventory (raw materials, work in process and finished goods) in accordance with IPSAS 12, *Inventories*. Full discussion is included in paragraphs 1.18–1.22.

Matter(s) for Consideration

5. The IPSASB is asked to **confirm** the view in the chapter that IPSAS 12, *Inventories* is appropriate to account for the costs of producing currency.

Chapter 2 – Currency Issued by the Entity: Notes – Recognition

15. Current practice for accounting for notes in circulation by all monetary authorities considered is to recognize a liability. Further, the GFS requirements are consistent with recognition of a liability for notes in circulation.
16. The obligation to recognize a liability for notes issued, arises because of the legal requirements monetary authorities have to maintain the notes supply.
17. The distribution of new notes, can result from the following two different types of transactions:
- (a) Transactions to increase the money supply, by increasing the number of notes in circulation; and
 - (b) Transactions which result in no change in the money supply, by exchanging old notes for new notes.
18. Appendix A, included in the Agenda item 2.3, includes example transactions showing the different steps in the process as well as the journal entries related to each step.
19. An explanation of the two types of transactions is included in paragraphs 1.32 and 1.33.

Matter(s) for Consideration

6. The IPSASB is asked to:
- (a) **Confirm** if it agrees with the staff view that notes in circulation result in the recognition of a liability;
 - (b) **Indicate** if the discussion of the types of transactions related to distribution of notes is helpful;
 - (c) **Indicate** if additional transactions have not identified by staff; and
 - (d) **Indicate** if Appendix A is helpful for understanding and if so, if any changes or further examples might be helpful.

Chapter 2 – Currency Issued by the Entity: Notes – Measurement

20. Current practice for measuring the liability recognized by monetary authorities is consistent; all measure the liability at the face value of the notes issued. This treatment is consistent with the requirements of GFS.
21. An analysis of the measurement bases available in the Conceptual Framework is included in paragraph 1.37.
22. Based on the analysis performed, staff is of the view that:
- (a) Historical cost would likely result in measurement at the face value of notes issued. Because distribution of notes, to either increase the money supply or exchange old notes (maintain money supply), results in consideration received equal to the face value of the notes issued.
 - (b) Market value may also result in measurement of the liability at the face value of the notes issued, as the face value of currency issued is equal to the amount of currency, or a financial asset—other than currency, received.
 - (c) Cost of fulfillment may result in measurement at the face value of the notes issued or an estimated cost of producing new notes. If it is assumed that the least costly manner to fulfill the obligation is the cost of producing new notes and not related to the face value of the notes. This may indicate that the value using cost of fulfillment is limited to the cost of producing replacement notes. However, if the view is taken that the cost of fulfilling the obligations is based on the value of the notes or financial assets—other than currency exchanged, the cost of fulfillment also may lead to measurement at face value of the notes issued.

Matter(s) for Consideration

7. The IPSASB is asked to:
- (a) **Confirm** if it supports the analysis related the various measurement bases;
 - (b) **Indicate** if it has a view as to which measurement basis is most appropriate; and
 - (c) **Confirm** if it agrees with the approach to discussion of measurement of the liability for notes in circulation, or alternatively suggest amendments.

Chapter 2 – Currency Issued by the Entity: Notes – Derecognition

23. As discussed in the chapter, staff is of the view, that there are two types of transactions related to derecognition:

- (a) Transactions which lead to the decrease in the supply of money, where notes are taken out of circulation by exchanging a financial asset—other than notes; and
 - (b) Notes which have been issued for which an obligation no longer exists, because they are no longer legal tender or lost/damaged and unlikely to be exchanged.
24. Transactions to reduce the money supply, result in derecognition, because the currency is removed from circulation.
25. Notes which have been issued for which an obligation may no longer exists, are more complicated. Because it may be difficult to identify when the obligation no longer exists. For example, it is likely to be impractical for a monetary authority to monitor how many notes exist in circulation. If it is deemed that an obligation no longer exists because an old series of currency is no longer legal tender, it may be easier to identify notes to be replaced. Staff is of the view that when an obligation no longer exists for a series of notes, it should be derecognized.
26. Derecognition in these circumstances raises the issue of the appropriate place to recognize the gain (derecognition of an old series of notes, results in a gain, as the liability is reversed). This gives rise to the issue of the appropriate place in the financial statements to recognize the gain. The options presented in the CP are as follows (paragraphs 1.39–1.43):
- (a) Recognition directly in net financial position, as the transaction to reverse a liability which relates to prior periods, may impair the current cost of services in the statement of financial performance; and
 - (b) Recognition in the statement of financial performance, to communicate the impact on current period performance, because it is a realized gain.

Matter(s) for Consideration

8. The IPSASB is asked to **Indicate** if it agrees with the discussion of derecognition and the options presented.

Chapter 2 – Currency Issued by the Entity: Coins – Recognition

27. Unlike notes, there is variation in accounting for coins in circulation, with some monetary authorities recognizing a liability for coins in circulation, while others do not.
28. Similar to the discussion of notes, a transactional approach is used to help understand the different potential accounting considerations at each step in the process. Due to the variability in the recognition of a liability for coins in circulation. The key issue for coins is whether a liability should be recognized.
29. There may be various reasons why a liability is not recognized for coins in circulation, such as:
- (a) The overall value of the coins in circulation which may not be material for a particular monetary authority;
 - (b) The monetary authority may not view the possibility of an outflow of resources to be probable and therefore does not recognize a liability; or

- (c) The monetary authority may estimate that because coins are made of metal, they are harder to damage and will require replacement less often, and even when exchanged can be recycled and reused to produce new coins, which may reduce the outflow of resources.
30. The TBG raised a question for the IPSASB, to consider if the discussion for potential reasons why a liability may not be recognized for coins is appropriate to include in the chapter, see paragraphs 1.46–1.50.

Matter(s) for Consideration

9. The IPSASB is asked to:
- (a) **Indicate** If it agrees with the possible reasons why monetary authorities might not recognize a liability for coins in circulation; and
 - (b) **Indicate** if the discussion on reasons why monetary authorities may not recognize a liability for coins in circulation is appropriate (paragraphs 1.46–1.50).

Chapter 2 – Currency Issued by the Entity: Coins – Measurement and Derecognition

31. Staff is of the view that when a liability is recognized for coins in circulation, the treatment for measurement and derecognition should be consistent with notes in circulation.

Matter(s) for Consideration

10. The IPSASB is asked to **Indicate** if it agrees with the view that when a liability is recognized for coins in circulation, the treatment should be consistent with notes in circulation.

Chapter 2 – Currency Issued by the Entity: Consistency with Current IPSAS

32. The draft chapter considers current IPSAS requirements for recognition and measurement which may apply to currency liabilities to contrast against the Conceptual Framework accounting analysis of the transactions in paragraphs 1.56–1.61.

Matter(s) for Consideration

11. The IPSASB is asked is asked to **Indicate** if it agrees with the analysis in paragraphs 1.56–1.61.

1 Introduction and Objective

- 1.1 IPSASs do not provide requirements or guidance on how to account for a number of monetary items that have been termed “public sector specific financial instruments”. The lack of guidance for these transactions leads to reporting that is inconsistent between entities and may be inappropriate. As a result, users may not have the information they need for accountability and decision-making purposes. This lack of guidance is a significant gap in the IPSASB’s literature.
- 1.2 This Consultation Paper (CP) is an important step in determining the appropriate reporting for public sector specific financial instruments. The CP considers the issues related to these instruments and possible approaches to accounting for them. The objective of the CP is to initiate a debate about matters such as:
- The types of instruments considered to be public sector specific financial instruments;
 - Approaches to recognition, measurement and derecognition; and
 - Presentation and disclosure of information.

History of the Project

- 1.3 The project to develop IPSAS 28, *Financial Instruments: Presentation*, IPSAS 29, *Financial Instruments: Recognition and Measurement*, and IPSAS 30, *Financial Instruments: Disclosures*, identified several items, some of which may meet the definition of a financial instrument but have certain public sector specific characteristics. Others do not strictly meet the financial instrument definition, but are similar to financial instruments. Items identified during the initial financial instruments project as “public sector specific financial instruments” were:
- Monetary gold;
 - Special Drawing Rights;
 - Reserve position in the IMF;
 - Currency issued by the entity;
 - Financial guarantee contracts; and
 - Concessionary loans.
- 1.4 Two public sector specific issues—concessionary loans and large-scale financial guarantee contracts—were addressed in application guidance in IPSAS 29. Both these instruments clearly meet the definitions of a financial instrument. The guidance has been applicable since January 1, 2013.
- 1.5 The IPSASB agreed to address the remaining issues through a further public sector specific financial instruments project.
- 1.6 In December 2013, the IPSASB identified additional issues to those noted in paragraph 1.3—statutory receivables, statutory payables and certain types of securitization transactions unique to the public sector. The IPSASB considers that it is in the public interest to consider these additional topics.
- 1.7 All of the topics have public interest implications given their significance to the public sector and their service delivery objectives. Considering these issues from a public sector perspective is important in

meeting the information needs of users; specifically related to assessing the ability of public sector entities to deliver services effectively, to manage the resources used and available to provide services, and to assess the liquidity and solvency of key institutions in the public sector.

- 1.8 Some topics in scope apply mainly to specific entities, such as central banks, which may apply national standards or international standards for the private sector. Because of the importance of central banks to the public sector, developing guidance for these entities is important for the IPSASB. Further, the IPSASB notes that because central banks form a part of the public sector in many jurisdictions they are likely to be controlled and consolidated into the financial accounts of the central government, even if they do apply national standards or international standards for the private sector.

Approach taken in this CP

- 1.9 The CP is organized into separate chapters by topic. The output of this project has not been determined by the IPSASB at this time. The project may lead to the development of a single standard or several standards and/or additional application guidance. However, the IPSASB feels it is important to deal with all the issues in a single CP, to allow consideration of all topics by constituents. Not all topics will be relevant for all constituents.

- 1.10 The CP has the following structure:

- Chapter 1: Introduction and Objective;
- Chapter 2: Currency and Coin Issued by the Entity;
- Chapter 3: Monetary Gold;
- Chapter 4: IMF Special Drawing Rights and Other IMF Transactions;
- Chapter 5: Statutory Receivables;
- Chapter 6: Statutory Payables; and
- Chapter 7: Securitizations.

Conceptual Framework

- 1.11 The complete Conceptual Framework was published in October 2014. This development influences the CP in the following ways:

- The objectives of financial reporting, the qualitative characteristics and the constraints on information included in general purpose financial reports (GPFRs), provide a framework against which the information needs of users can be weighed against accounting considerations for each chapter;
- The definitions of elements and the recognition criteria provide guidance for evaluating transactions and recognition in financial statements.
- The measurement objective provides a framework for assessing the information needs of users and which measurement basis appropriately meet such needs; and
- The concepts for presentation and disclosure provide guidance on information selection, location and organization.

Objectives of financial reporting and qualitative characteristics

1.12 The objectives of financial reporting are set out in paragraph 2.1 of the Conceptual Framework.

“The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of GPFs for accountability purposes and for decision-making purposes (hereafter referred to as “useful for accountability and decision-making purposes”).”

1.13 The CP considers how well the options for accounting put forward in each chapter satisfy the objectives of financial reporting and meet users’ information needs.

Objective of measurement

1.14 The CP identifies viable measurement bases and assesses how well they meet the information needs of users.

Concepts of presentation

1.15 The CP considers how the information needs of users can be enhanced through presentation and disclosure.

Consideration of Government Finance Statistics (GFS)

1.16 The IPSASB considers it important to reduce differences with the statistical basis of reporting where appropriate. The Preface to the Conceptual Framework states that the removal of differences between GFS reports and IPSAS financial statements can provide benefits to users in terms of report quality, timeliness and understandability. Further, the IPSASB has published a policy paper, *Process for Considering GFS Reporting Guidelines during Development of IPSASs* in February 2014¹ (GFS Policy Paper), which has been considered in developing this chapter.

1.17 Informed by the Conceptual Framework and the GFS Policy Paper, the IPSASB reviewed the definitions and descriptions related to each topic in scope of the project. The IPSASB considered the *System of National Accounts 2008 (SNA)*, *Government Finance Statistics Manual 2014 (GFSM)* and *Balance of Payments and International Investment Position Manual—Sixth Edition (BPM6)*. The guidance from the applicable manuals related to each topic will be considered by the IPSASB in developing accounting guidance to minimize unnecessary differences.

2 Chapter 2: Currency and Coin Issued by the Entity

To be developed

3 Chapter 3: Monetary Gold

Introduction

3.1 Physical gold has a long history as a reserve asset. Historically, currency was produced from precious metals (gold, silver). As economies advanced, paper money became more prevalent; however, it would typically be exchangeable for a precious metal. Gold played a more direct role in the monetary system until the early 1970’s, when the US dollar², was allowed to float freely. Although currencies

¹ <http://www.ifac.org/sites/default/files/publications/files/IPSASB-GFS-Policy-Paper.pdf>

² The US dollar was the last currency which was exchangeable for a fixed amount of gold.

are no longer linked to gold, central banks and governments continue to hold physical gold, because it has intrinsic value and there is a global liquid market for it.

3.2 Public sector entities, such as central government departments and/or central banks hold gold as a reserve asset. The unique characteristics of gold make it an important reserve asset for such entities, for the following reasons:

- Economic security—Gold does not deteriorate or decay. It has a high density, so small amounts have high value. It is physical and therefore is not a liability of another party (no counterparty risk);
- Risk diversification—It has a large global market to transact it, but a unique market to those of other reserve assets (gold markets often move inverse to key global currency markets, such as the US dollar);
- Confidence—Currency is no longer backed or exchangeable for gold. However, confidence in currency and central banks often can be linked to gold holdings; and
- Asset available for unexpected liquidity needs—In periods of uncertainty, high inflation or large negative economic events, gold becomes a critical asset as it can be sold for foreign currency reserves, used directly for international payments or as collateral for borrowings.

3.3 Accounting for monetary gold is inconsistent in the public sector, with a range of measurement bases used.

3.4 This chapter of the CP considers the approaches to, and issues arising in, accounting for monetary gold. The objective is to initiate a debate about matters such as:

- (a) The nature of different types of gold assets and how they are used by monetary authorities; and
- (b) The appropriate way to measure monetary gold assets in order to provide the best information to users.

Chapter Objective

3.5 The IPSASB proposes the following objective for future guidance on accounting for monetary gold:

An entity shall account for monetary gold in a manner that helps users of its financial statements assess:

- The impact of monetary gold on the entity's financial performance and financial position;
- The nature and extent of risks arising from holding monetary gold, and how the entity manages those risks; and
- The types (different categories and characteristics) of monetary gold held by the entity.

3.6 In developing options for accounting for monetary gold, it is important to identify the intentions for which monetary authorities hold monetary gold as reserve assets. The two main intentions identified, for which monetary authorities hold gold assets, are as follows:

- Intention 1: Monetary gold intended to be held for its financial capacity because of its ability to be sold, in the global liquid gold trading markets. Therefore, information on the current market value of gold is important; and

- Intention 2: Monetary gold intended to be held for an indeterminate period of time, because it provides confidence in the monetary authority's financial strength and ability to carry out its activities. Further, there may be prohibitions or restrictions placed on these monetary authorities which limit the ability to sell monetary gold assets. Therefore, when monetary gold is held with this intention, the quantity and the price paid to acquire it is important, with less concern as to the current market value.
- 3.7 The CP identifies two options to account for monetary gold, both options are linked to the intentions monetary authorities have in holding it, as described in paragraph 3.6. In assessing these options, the IPSASB will consider how well they satisfy the objectives of financial reporting and meet users' information needs.
- 3.8 The CP also considers how well each option satisfies the qualitative characteristics (QCs) set out in the Conceptual Framework.

Scope and Definitions

- 3.9 This section of the CP addresses the scope and definitions for any future guidance on monetary gold.

Consideration of GFS

- 3.10 As noted in the introduction, the IPSASB considers it important to reduce differences with the statistical basis or reporting where appropriate. The most comprehensive guidance on statistical accounting for monetary gold, can be found in the Balance of Payments International Investment Position Manual—Sixth Edition (BPM6).
- 3.11 BPM6 notes in paragraph 6.78: *Monetary gold is gold to which the monetary authorities (or others who are subject to the effective control of the monetary authorities) have title and is held as reserve assets. It consists of gold bullion (including gold coins, ingots, bars with a purity of at least 995/1000, and gold bullion held in allocated gold accounts, regardless of the location of the account) and unallocated gold accounts with nonresidents that give title to claim the delivery of gold. Gold bullion is usually traded on organized markets or through bilateral arrangements between central banks. To qualify as reserve assets, gold accounts must be readily available upon demand to the monetary authorities.*
- 3.12 BPM6 explains the relationship of monetary gold to non-monetary gold in paragraph 5.78: *In contrast to monetary gold, which is a financial asset, nonmonetary physical gold is a good. (Paragraphs 10.50–10.54 deal with nonmonetary gold in the goods and services account.) Similarly, other precious metals are goods and not financial assets. Monetary gold is treated differently because of its role as a means of international payments and store of value for use in reserve assets.*
- 3.13 BPM6 notes in paragraph 6.64: *Reserve assets are those external assets that are readily available to and controlled by monetary authorities for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing).*
- 3.14 BPM6 notes in paragraph 6.66: *The functional concept of monetary authorities is essential for defining reserve assets. Monetary authorities encompass the central bank (which subsumes other institutional units included in the central bank subsector, such as the currency board) and certain operations usually attributed to the central bank but sometimes carried out by other government*

institutions or commercial banks, such as government-owned commercial banks. Such operations include the issuance of currency; maintenance and management of reserve assets, including those resulting from transactions with the IMF; and operation of exchange stabilization funds. In economies with extensive reserve assets that are held outside of the central bank, supplementary information should be provided on the institutional sector of holdings of those reserve assets.

Definitions and Descriptions

3.15 Considering the above definitions and descriptions from BPM6, the IPSASB proposes the definitions and supporting guidance, discussed below.

3.16 **Monetary gold** is defined as follows:

“Tangible gold assets held by monetary authorities as reserve assets.”

3.17 The definition is restricted to those gold assets held by monetary authorities as reserve assets, as these are the assets available for use to monetary authorities in carrying out their mandates. Gold assets not held by monetary authorities or those held by monetary authorities but not as reserve assets, would not be considered to be held to assist in achieving the core mandate of monetary authorities and therefore have been excluded.

3.18 **Tangible gold** is defined as follows:

“Physical gold that has a minimum purity of 995 parts per 1000.”

3.19 Tangible gold which does not meet the minimum purity requirements of 995 parts per 1000, is not considered to be in saleable form, according to the internationally accepted rules³ for trading on markets and exchanges.

3.20 The main requirement to be in saleable form is to meet the minimum purity requirement of 995/1000. However, assets should also be in a form which facilitates a timely transaction, meaning a form⁴ of tangible gold which is quantifiable⁵, in a standard size and form. This allows for gold to be easily identified and measured, as required to facilitate market transactions.

3.21 **Monetary authority** is defined as follows:

“The monetary authority is the entity or entities which include the central bank or a department(s) of the central (national) government, which carry out operations usually attributed to the central bank.”

3.22 In limited circumstances a monetary authority may be (or include) an international or regional entity⁶.

³ The international standard for transacting in physical gold, are the rules of the London Bullion Exchange.

⁴ A specific standardized shape and size of gold asset is not proposed, as there are many different standards for shapes and sizes used in various gold markets globally.

⁵ Physical gold sold by central banks and refineries, are normally in bar form and stamped with identifiable markings noting weight, purity and where gold was produced or refined.

⁶ An example of an international entity which holds reserve assets to provide stability to the global monetary system is the IMF, which has significant monetary gold assets. An example of a regional entity which holds reserve assets to provide stability to the European monetary system is the European Central Bank. Both of these entities work in a capacity similar to national governments and central banks in terms of their use of reserve assets, such as monetary gold.

- 3.23 Monetary authorities have a broad mandate to oversee various aspects of the economy, such as the issuance and maintenance of currency, management of reserve assets and operation and administration of exchange rate stabilization funds.
- 3.24 **Reserve assets** are defined as follows:
“Assets held by monetary authorities, which are readily available for international payment needs, intervention in the currency markets to affect exchange rates and maintaining confidence in the currency and the economy.”
- 3.25 Reserve assets comprise monetary gold, foreign currency, highly liquid investments, and Special Drawing Rights (SDRs).
- 3.26 To be effective, reserve assets must be readily available for trading.
- 3.27 Monetary gold is one particular type of reserve asset. It is held by monetary authorities for its intrinsic value as a precious metal and because a global liquid trading market exists. Monetary gold is similar to foreign exchange holdings, another key type of reserve asset. The characteristics of monetary gold help monetary authorities to achieve their objectives as well as their intentions in holding them. Therefore, monetary gold has an economic substance that differs from tangible gold holdings held for other purposes such as use in operations, manufacturing and/or because such holdings have historical or cultural significance.⁷
- 3.28 The definition excludes other precious metals (silver or platinum). Unlike gold, non-gold precious metals are not considered a store of value, or as a medium for international payments, in the manner that gold is. Because of this central banks do not hold non-gold precious metals as reserve assets. The IPSASB noted that none of the central bank financial statements examined accounted for or disclosed any holdings of precious metals, other than gold.

Scope

- 3.29 Monetary gold must meet the definition set out in paragraph 3.16 and must be held to achieve the intentions of a monetary authority.
- 3.30 Tangible gold, can have a range of purities, from low to high gold content⁸ and can take many forms⁹. However, only tangible gold which satisfies the definition of monetary gold, as defined in paragraph 3.16, should be in scope of guidance. Monetary authorities have a number of options for holding tangible gold as discussed in the following paragraphs.
- 3.31 Tangible gold can be held directly by monetary authorities or stored with a third party in an allocated or unallocated gold account; as explained below:
- (a) Tangible gold held directly by monetary authorities with a purity greater than or equal to 995/1000 which is held for use as reserve assets, satisfies the definition of monetary gold and should be in the scope of guidance;

⁷ Some monetary authorities may hold physical gold for the purpose of facilitating trading with banks or commodity brokers (to facilitate trading in the markets). Monetary authorities may also hold physical gold for use in manufacturing for items such as gold coins.

⁸ Tradable physical gold requires a purity of 995 parts per 1000 or greater gold content.

⁹ Physical form of gold can be in the form of bars of various shapes and sizes. Sometimes physical gold exists in the form of nuggets. Also, gold bars are sometimes referred to as ingots.

- (b) Tangible gold held in an allocated account, is gold which is stored with a third party for safekeeping. Gold assets are specifically identified and segregated in the third party's storage facilities. Monetary authorities can demand delivery of the specific gold, or instruct the third party to undertake transactions on their behalf. The rights and obligations of owning the gold assets have not been transferred as the third party is an agent providing safekeeping services. Therefore tangible gold held in an allocated account, which satisfies the monetary gold definition, should be included in the scope of guidance; and
- (c) Tangible gold held as a deposit in an unallocated account, is gold deposited by the monetary authority with a third party (in a manner similar to how cash is deposited at a bank). Deposits of gold assets are not segregated or identified. Monetary authorities have the right to request on call delivery¹⁰ of the deposited gold. Gold assets held in unallocated accounts have different risks than those held directly by monetary authorities or in allocated accounts. However, such deposits are still denominated in tangible gold and allow for the delivery of a specific quantity of gold. Therefore, gold assets held in unallocated accounts, which meet the definition of monetary gold, should be included in the scope of guidance.

3.32 Gold coins which are minted from gold, either as commemorative gold coins or as legal tender gold coins, as described below:

- (a) Commemorative gold coins derive their value based on the gold content or the numismatic¹¹ value. Commemorative gold coins are not legal tender and are not considered cash. The value of such coins may be greater than the intrinsic value of the gold. Because of this, monetary authorities may be less likely to use these as reserve assets, as it would be unlikely such coins would be sold through the gold commodity markets, given higher values could be achieved through other non-commodity markets. However, if the monetary gold definition is satisfied and monetary authorities do hold commemorative gold coins for use as reserve assets, then they should be included in the scope of guidance. Alternatively, if they are held because of their numismatic value or used for purposes other than as reserve assets, they should not be in the scope of guidance; and
- (b) Legal tender gold coins are legal tender in a particular jurisdiction, such as the Canadian Maple Leaf, and China Panda gold coins. The legal tender face value is less than the value of the gold content in the coins. Such coins are legal tender and therefore cash. Some legal tender gold coins, do not contain a high enough gold content to satisfy the requirements of the definition¹². However, those legal tender gold coins which meet the monetary gold definition and which are held for use as reserve assets should be included in the scope of guidance.

3.33 The banking and gold industries have developed a range of securities linked to gold. The main categories of gold-related instruments are discussed below:

¹⁰ Similar to cash held by banks as deposits, banks holding monetary gold in unallocated gold accounts, would not in the normal course of operations hold enough gold to deliver to all depositors on demand. This is one of the risks and key differences between gold held in allocated gold accounts versus unallocated gold accounts.

¹¹ Numismatic value is the value of money or coins, based on collector value, as opposed to the face value or underlying value of precious metals they are comprised of.

¹² The South African Kruggerand, American Gold Eagle and British Britannia are all legal tender gold coins. However, their gold content is lower than the definition requirements of 995/1000.

- (a) Gold loans are debt agreements for borrowings where gold is posted as collateral to secure the loan. These types of debt agreements are not monetary gold, as they do not meet the definition of monetary gold, as they are a contractual instrument and not tangible gold in saleable form. The fact that a loan is secured by gold, does not mean that such gold is available to monetary authorities for use as reserve assets and therefore should not be in scope of guidance;
 - (b) Gold exchange traded funds (ETFs) are securities (investment instruments and funds) traded on public markets which are linked to an underlying amount of gold, to the market price of gold, or which hold underlying securities of entities which produce gold. Gold ETFs are financial instruments as they result from a contract, which gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. The majority of these types of instruments should be accounted for as financial instruments using IPSAS 28–30, and would not be considered in scope of monetary gold guidance. However if these gold instruments allow for settlement in tangible gold on demand, the gold assets satisfy the monetary gold definition and the monetary authority has the intention of taking physical delivery of such gold, such instruments may be considered monetary gold¹³;
 - (c) Gold forward/futures are derivative contracts for the exchange of a quantity of gold at a future date at a specified price. Gold derivatives are financial instruments as they result from a contract, which gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. However, in some instances monetary authorities may hold such instruments with the intention of taking physical delivery of gold. When these instruments allow for settlement in tangible gold on demand, and the gold assets satisfy the monetary gold definition, such instruments may be considered monetary and should be in scope of monetary gold guidance; and
 - (d) Gold equities are common and preferred shares of companies which explore, develop and mine gold. These are companies which generate revenue through the exploration, development and mining of gold. Gold equities are financial instruments as they result from a contract, which gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Gold equities are not tangible in nature and the value of such gold equities is related to the combined operations of the entity, and not an underlying amount of tangible gold. Therefore, gold equities are financial instruments. IPSAS 28–30 should be applied and they should not be in scope of monetary gold guidance.
- 3.34 Gold antiques are cultural and historical items which contain gold. These items have value arising from their gold content, as well as their historical and/or cultural value. Gold antiques are likely to be held by government entities because of their cultural and/or historical significance and are unlikely to be held as reserve assets. Even if such items are held by monetary authorities and the gold items meet the purity requirements, it is unlikely they would be in saleable form and therefore would not satisfy the definition requirements. Gold antiques are not considered to be in scope of monetary gold guidance.

¹³ Staff view is that any instrument that allows for delivery of a fixed quantity of physical gold, which are held by monetary authorities as reserve assets, could meet the scope exclusion of IPSAS 29.4: which states: *...contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments, with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale, or usage requirements.*

- 3.35 Gold assets in scope of monetary gold guidance, should be only those items which satisfy the definition and those which are intended to be held by monetary authorities as reserve assets. The following types of gold assets should be included:
- Tangible gold (including gold held directly, in allocated and unallocated gold accounts);
 - Commemorative and legal tender gold coins; and
 - Some financial instruments which allow for physical settlement in gold on demand and for which monetary authorities have the intention of taking physical delivery.

Recognition and Measurement

Recognition

- 3.36 Monetary gold should be recognized in the statement of financial position when it meets the definition in paragraph 3.16 and the definition of an asset in the Conceptual Framework which is “an asset is a resource presently controlled by the entity as a result of a past event.”
- 3.37 The Conceptual Framework provides recognition guidance in paragraph 6.7, which requires consideration of measurement uncertainty. When applying this guidance to monetary gold, because the asset is tangible and the existence of the global market for trading it, the risk of measurement uncertainty is minimal.
- 3.38 Control over monetary gold arises through acquisition which normally results from a purchase. Control can be exercised even if the gold is not directly held by the entity, as it is common for entities to store gold with another monetary authority or international banking institution for safe keeping, as discussed in paragraph 3.31.

Measurement

- 3.39 Monetary authorities are inconsistent in how they measure monetary gold with some using historical cost, others using fair value/market value and a further group using a statutory rate¹⁴.
- 3.40 Chapter 7 on measurement in the Conceptual Framework, paragraph 7.2, states the *objective of measurement is to select those measurement bases that most fairly reflect the cost of services, operational capacity and financial capacity of the entity in a manner that is useful in holding the entity to account and for decision-making purposes*. Paragraph 7.3 further elaborates *that selection of a measurement basis contributes to meeting the objectives of financial reporting in the public sector by providing information that enables users to assess:*
- (a) *The cost of services provided in the period in historical or current terms.*
 - (b) *Operational capacity—the capacity of the entity to support the provision of services in future periods through physical and other resources; and*
 - (c) *Financial capacity—the capacity of the entity to continue to fund its activities.*
- 3.41 The nature of monetary gold and its use by monetary authorities for reserve purposes, means that information on the contribution to financial capacity is relevant. Monetary gold is not used directly in

¹⁴ Two examples of monetary authorities using statutory rates to measure monetary gold are the US Federal Reserve Bank and the South African Reserve bank. The US Federal Reserve measures monetary gold at the statutory rate set by law at \$42.22 per fine troy ounce. The South African Reserve Bank measures monetary gold at the market price take at 14:30 on the reporting date.

operations or to directly provide services, like other tangible assets. However, the acquisition cost and information on cost of services, provides relevant information for users, when monetary gold assets are intended to be held for an indeterminate period of time.

- 3.42 Measurement bases that provide information on financial capacity are relevant, because they enable users to assess the ability of monetary authorities to provide stability and liquidity into the monetary system or to support the provision of services in future periods through physical and other resources. Monetary authorities may have different intentions for holding monetary gold, which impacts whether information on financial capacity is useful to users.
- 3.43 Measurement bases that provide information on cost of service may also be relevant, when monetary authorities have the intention of holding gold assets for an indeterminate period of time. Because they enable users to assess the cost of acquiring monetary gold assets and holding them. Only when monetary gold assets are sold or impaired will their impact on costs of services will be recognized in the statement of financial performance which may provide users with useful information.
- 3.44 Monetary authorities have a variety of different reserve assets available for use to achieve their objectives. Depending on management of such reserves by monetary authorities, monetary gold may be held for a specific intention, as discussed in paragraph 3.6. If the intention of holding monetary gold is trading purposes, such as use for international payments, to influence the money supply and/or to provide liquidity and stability to the economy, then a measurement basis which provides information on financial capacity may be relevant.
- 3.45 Alternatively, if the intention in holding monetary gold is to hold it for an indeterminate period, because it provides confidence in the in ability of monetary authorities to carry out their activities, then a measurement basis which provides information on cost of services may be relevant.
- 3.46 Monetary authorities currently measure monetary gold either on a historical cost basis, or fair value/market value basis¹⁵. A smaller group of monetary authorities also use a statutory rate. While statutory rates and their application vary between jurisdictions, monetary authorities using this method have a common aim of reducing the volatility caused by changes in gold prices. Use of a statutory rate is not a basis discussed in the Conceptual Framework.
- 3.47 The IPSASB considered the Conceptual Framework and noted that of the six potential bases available, only historical cost and market value in open, active and orderly market, were practical to consider:
- (a) Historical cost, as it is an entry value which provides information on the resources exchanged to acquire monetary gold assets, which are available to provide services in future periods. Such information allows users to assess the minimum service potential monetary gold assets can provide to monetary authorities.
 - (b) Market value in open, active and orderly market, as it is a current value measurement basis which provides users with the information required to assess the ability of monetary gold to contribute to the financial capacity of monetary authorities.

¹⁵ Only measurement bases consistent with the conceptual frameworks guidelines are discussed, which is why a statutory rate, is not referred to here.

3.48 Other measurement bases were not considered appropriate by the IPSASB for the following reasons:

- Market value in inactive market is not appropriate as a global liquid, active market exists for gold;
- Replacement cost is not appropriate, as monetary gold held for reserve purposes is not consumed in operations. Further, replacement cost would be equal to the amount to purchase gold in the market, which would be market value in open, active and orderly market;
- Net selling price is generally more useful when an open, active and orderly market does not exist and needs to reflect constraints on a sale and is therefore not appropriate; and
- Value in use is most useful for entity-specific asset valuations, such as, assets of a specialized nature used for a specific purpose, where the service potential or ability to generate economic benefits creates more value to the entity than, the value using replacement cost. Gold is a commodity and is held for its intrinsic value and global liquid trading market and therefore is not used in a specialized way. Value in use therefore does not appear to be an appropriate basis.

3.49 The Conceptual Framework paragraph 7.4 states, *that selection of a measurement basis also includes an evaluation of the extent to which the information provided achieves the Qualitative Characteristics (QCs)*. The IPSASB determined that historical cost and market value in open, active and orderly market, are the appropriate measurement bases available for consideration, and has analyzed these against the QCs in paragraphs 3.50 and 3.51.

Historical Cost

3.50 An assessment of the information provided by measuring monetary gold using historical cost for each of the QCs is summarized as follows:

- **Relevance**—Historical cost information provides information on the minimum resources available to provide future services, based on their acquisition cost, which is useful in assessing cost of services;
- **Faithful Representation**—Historical cost provides a faithfully representative view of the transaction price to acquire monetary gold, providing information on the minimum service potential but not information on the financial capacity it provides;
- **Understandability**—Historical cost information is not complex. It provides information on the cost to acquire (entry value of) monetary gold;
- **Timeliness**—Historical cost information is timely, because transaction prices are easily obtainable and the carrying amount is stable between accounting periods unless monetary gold is acquired, sold or impaired;
- **Comparability**—Historical cost does not provide comparable information from one entity to another, as the value is based on the timing of the purchase of the gold by each entity and not the current economic value. However, it does provide comparable information from period to period for an individual entity, as changes in carrying amounts are stable, unless gold is acquired, sold or impaired; and
- **Verifiability**—Historical cost information for monetary gold is transaction based and easily verifiable.

Market Value

- 3.51 An assessment of the information provided by measuring monetary gold at market value for each of the QCs is summarized as follows:
- **Relevance**—Market value is a relevant measure that provides information on the contribution of monetary gold to financial;
 - **Faithful Representation**—Market value provides a faithfully representative view of the financial capacity monetary gold provides as it represents the exit value and is an objective price, available in a transparent, liquid market. Market value is also an entry value, because of the open, active and orderly market for gold, and therefore provides a faithfully representative view of operational capacity as well;
 - **Understandability**—Market value information is understandable; the valuation of monetary gold using a spot rate is not complex;
 - **Timeliness**—Market value provides measurement information in a timely manner. The gold markets are transparent and prices are available in real time. Information required for financial statements can be prepared quickly using simple calculations;
 - **Comparability**—Market value provides measurement information which allows direct comparability of monetary gold assets with other assets, and between different monetary authorities; and
 - **Verifiability**—Market value provides information which is verifiable, because there is an open, active and orderly market.
- 3.52 Both historical cost and market value measurement provide information which is useful to users when considered against the QCs. Monetary authorities may hold monetary gold assets to aid in achieving different intentions as discussed in paragraph 3.6. Depending on the primary intention a monetary authority has in holding monetary gold, there may be benefits for using historical cost over market value as a measurement basis, or vice versa.
- 3.53 Monetary authorities with the main intention of holding monetary gold for use in a manner similar to foreign currency, may prefer an exit value measurement basis. In this case, market value may be more useful for measuring monetary gold, because it provides relevant information to assess the financial capacity of the entity. The best exit value measure is market value because there is an open, active and orderly market for gold, which is non-entity specific. By using market value to measure the value of monetary gold, it allows for the faithful representation of the contribution of monetary gold to an entity's financial capacity.
- 3.54 Monetary authorities with the main intention in holding monetary gold for an indeterminate period of time, may prefer an entry value measurement basis. Some monetary authorities hold large quantities of monetary gold and do not have a history of sales. Also some monetary authorities may have restrictions on selling monetary gold assets. Therefore, a historical value measurement basis may be more appropriate, as it reflects the value to acquire monetary gold assets. It also allows users to assess the cost of acquiring/holding monetary gold and the service potential provided, by reference to an actual transaction. Using historical cost to measure monetary gold also avoids introducing volatility into the statement of financial position, which is consistent with some monetary authorities' intentions of holding gold assets. Gold prices change significantly over time and the impact of using

a market value measurement basis, can impair users' ability to assess the real cost of providing services.

- 3.55 Considering the different intentions for which monetary authorities hold gold, the CP proposes two measurement options:
- Option 1: Measurement at market value in an open, active and orderly market; and
 - Option 2: Measurement at historical cost.

Measurement

Option 1: Market Value in Open, Active and Orderly Market

- 3.56 Measurement of monetary gold at market value gives rise to two sub issues—accounting for changes in value and transaction costs. The Conceptual Framework is considered in developing the accounting alternatives for each issue. Additionally, relevant IPSAS standards are also considered.
- 3.57 Market value measurement requires monetary gold assets recognized in the statement of financial position to be revalued based on the spot rate. This provides users information to assess the financial capacity of monetary authorities. However, it does give rise to the issue of the appropriate place to recognize unrealized (temporary) gains and losses, due to revaluations.
- 3.58 There are different approaches for dealing with the recognition of unrealized losses. One approach is to recognize all gains and losses in the statement of financial performance. Another approach is to recognize unrealized gains or losses directly in net financial position (net assets/equity), until realized.
- 3.59 Some may view recognition of all gains and losses due to changes in value in the statement of financial performance to be appropriate because IPSAS 1, requires this, unless an IPSAS specifies otherwise. Further, Chapter 7¹⁶ of The Conceptual Framework notes that *revenue from providing services reported in the financial statements is measured on the basis of prices current in the reporting period. Thus the surplus or deficit for the period includes prices movements that take place over the period during which assets and liabilities are held, and no profit or loss is reported on the sale of an asset. Where the asset is traded on an open, active and orderly market, the existence of the market provides assurance that the entity would be able to realize the market value (and no more) at the reporting date: it is therefore unnecessary to postpone recognition of changes in value until a surplus is realized on a sale.* This guidance in the Conceptual Framework may support recognition of changes in value in the statement of financial performance. However, the Conceptual Framework does not link revenues and expenses to specific financial statements and also does permit recognition of other resources and other obligations for other economic phenomena.
- 3.60 However, some may view the approach to recognize unrealized gains or losses directly in net financial position (net assets/equity), as appropriate because it is consistent with IPSAS 29, which

¹⁶ The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities states in paragraph 7.32 “...revenue from providing services reported in financial statements is measured on the basis of prices current in the reporting period. Thus the surplus or deficit for a period includes price movements that take place over the period during which assets and liabilities are held, and no profit or loss is reported on the sale of an asset. Where the asset is traded on an open, active and orderly market, the existence of the market provides assurance that the entity would be able to realize the market value (and no more) at the reporting date: it is therefore unnecessary to postpone recognition of changes in value until a surplus is realized on sale. However, where assets used to provide services are not traded on open, active and orderly markets, or a close approximation to markets, the relevance of revenue and expense related to changes in market value is more questionable.”

requires unrealized gains and losses for financial assets designated as available-for-sale (AFS) to be recognized directly in net financial position, until realized.

- 3.61 Further, Chapter 5 of the Conceptual Framework notes that *revenue and (expenses), are increases (decreases) in the net financial position of the entity other than increases (decreases) arising from ownership contributions (distributions)*. Changes in fair value of monetary gold assets, both unrealized (temporary) and realized will give rise to revenue or expense as they result in changes in the net financial position (net assets) of the entity which are not ownership contributions or distributions. Therefore, recognition of unrealized losses directly in net financial position (net assets) or in the statement of financial performance may be appropriate when considering the guidance on recognition of elements in the Conceptual Framework.
- 3.62 The global markets for trading gold can be very volatile. The volatility can cause significant changes in the value of monetary gold assets. Some may argue that recognizing unrealized gains or losses in the statement of financial performance, may prevent a faithfully representative view of the cost of service for the period presented. Further, some view that this impairs the objectives of financial reporting by presenting information to users which does not reflect the true cost of service for the period, or the change in financial capacity provided by holding monetary gold assets. Because of this it may be more appropriate to recognize unrealized gains or losses directly in net financial position (net assets/equity) until they are realized.
- 3.63 Another consideration in determining the appropriate approach to recognition of unrealized gains or losses relates to monetary authorities relationship with the central government. Many monetary authorities are required to pay dividends to the central (national) governments based on accounting profits. Dividends paid based on unrealized gains or losses may lead to insufficient capital levels. As monetary authorities have an important role in the economy, it is important that they have adequate capital available. When monetary authorities are not properly capitalized, they may not be able to perform their role effectively.
- 3.64 The approach to recognize unrealized gains and losses directly in net financial position (net assets/equity) and only realized gains and losses in surplus or deficit for the period addresses the issue of dividend distributions. It also ensures that surplus and deficit for each period reflects actual realized changes in capital (financial capacity) of monetary authorities. This allows users to evaluate the impact on surplus or deficit related to the sale and derecognition of monetary gold assets, and is consistent with the purpose monetary authorities hold gold assets for trading purposes. This approach is also consistent with how available-for-sale (AFS) financial assets are accounted for in IPSAS 29, *Financial Instruments: Recognition and Measurement*.

Consistency with Current IPSAS

- 3.65 Accounting requirements for financial assets are included in IPSAS 29, *Financial Instruments: Recognition and Measurement*. IPSAS 29 requirements are based on the classification of the financial instrument, with differences related to fair value, transaction costs and subsequent changes in value.
- 3.66 Monetary gold held with the intention of trading is similar to the IPSAS 29 requirements for financial assets classified at fair value through surplus or deficit (FV) or available-for-sale (AFS).
- 3.67 Fair value in current IPSAS, is the amount for which assets could be exchanged between knowledgeable, willing parties in an arm's length transaction. In the case of monetary gold this would

be the spot rate of gold. Fair value for monetary gold assets is the same regardless of whether it is classified as FV or AFS.

- 3.68 IPSAS 29 requires initial transaction costs to be expensed as incurred in the statement of financial performance when classified as FV. Transaction costs directly attributable to the acquisition of AFS assets are included as part of the initial cost of the assets (fair value plus directly attributable transaction costs).
- 3.69 The classification of FV and AFS for financial assets also impacts how subsequent changes in value are accounted for. For those assets classified as FV, all changes in value, both realized and unrealized, are recognized in the statement of financial performance. For those assets classified as AFS, unrealized changes in value are recognized directly in net financial position. Changes in value which are realized (due to derecognition of the assets), or when the financial assets are impaired, the cumulative gain or loss is recognized in the statement of financial performance.
- 3.70 Market value—in open, active and orderly market provides information on the contribution that monetary gold makes to financial capacity.

Option 2: Historical Cost

- 3.71 Monetary authorities may hold monetary gold for different intentions, as noted in paragraphs 3.53–3.55. Under such circumstances, use of an entry value measurement basis such as historical cost is appropriate, when the main objective in holding gold is for its service potential.
- 3.72 From an accounting perspective accounting for monetary gold at historical cost is simple and straight forward compared to market value.
- 3.73 Historical cost is normally recognized at the fair value at the time of acquisition plus transaction costs as these are part of the cost of acquiring the asset. Changes to historical cost of monetary gold assets only result from an impairment, when the price of gold decreases below the acquisition price. Losses due to impairment are recognized in the statement of financial performance, with a corresponding decrease in the carrying amount.
- 3.74 Historical cost reflects the cost to acquire the gold assets and the minimum service potential provided by holding it. Monetary authorities with the intention of holding monetary gold, are often more concerned with the quantity of gold held. Therefore, changes in the historical cost values on the statement of financial position would directly relate to either increases or decreases in the quantity of monetary gold assets, or impairments of monetary gold assets; all changes which relate to the service potential of the assets. The historical cost approach also addresses the issue of ensuring the unrealized gains and losses are not distributed as dividends by monetary authorities.

Consistency with Current IPSAS

- 3.75 There are many current IPSASs which use a historical cost measurement model. The appropriate measurement model to consider, depends on if monetary gold is viewed as a tangible asset or as a financial asset. The most appropriate applications of the historical cost measurement model in IPSAS are as follows:
- IPSAS 12, *Inventories* requires measurement at the lower of cost and net realizable value, except where inventories are acquired in a non-exchange transaction or where inventories are likely to be distributed at no or nominal charge (not likely in the monetary gold case). The cost of inventories includes all costs of purchase, plus costs of conversion and other costs incurred

in bringing inventories to their present location and condition. For monetary gold, this would be fair value plus initial transaction costs. However since the inventory standard is intended for goods purchased and held for resale, it may not be appropriate for monetary gold assets held for an indeterminate period of time.

- IPSAS 17, *Property, Plant and Equipment* requires an item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its cost. Cost includes purchase price, plus non-refundable duties and taxes, net of rebates, plus any costs attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management, plus any estimate of the costs of dismantling and removing the item and restoring the site is located, for which the obligation related to such costs has been recognized. For monetary gold, this would be fair value plus initial transaction costs. Using IPSAS 17 by analogy to measure monetary gold assets, is similar to how the standard treats land. Land is measured at its initial fair value plus transaction costs and is not amortized.
- IPSAS 29, *Financial Instruments: Recognition and Measurement* requires that financial assets classified as AFS for which there is not a quoted market price in an active market and which cannot be reliably measured are required to be measured at cost¹⁷. Although, an active market for gold does exist, this does demonstrate the use of the historical cost model in the IPSAS financial instrument standards. Monetary authorities which hold monetary gold assets for an indeterminate period of time, without a history of selling such assets, may be considered similar transactions to those in thinly traded or illiquid equity securities which lack a market price.

3.76 Monetary authorities with the intention of holding monetary gold for an indeterminate period of time, historical cost measurement provides information on the cost to acquire and hold the assets and their minimum service potential.

Derecognition

3.77 The Conceptual Framework in chapter 6.10 notes that *derecognition is the process of evaluating whether changes have occurred since the previous reporting date that warrant removing an element that has been previously recognized from the financial statements, and removing the item if such changes have occurred.*

3.78 In accordance with this guidance, derecognition would occur when monetary gold assets are sold or transferred to another entity. Given the tangible nature of monetary gold, other than an outright transfer or sale, any sale of an interest or percentage of gold, or use as gold for collateral would be contractual and give rise to a financial asset of one entity and a financial liability or equity instrument of another entity, and therefore be assessed under IPSAS 28–30.

Presentation and Disclosure

3.79 This section of the CP discusses at a high level the information to be presented in respect of monetary gold. It does not propose specific requirements. These requirements are linked to decisions regarding the approach to recognition and measurement, and therefore will be determined once the IPSASB has considered the responses to this chapter of the CP.

¹⁷ IPSAS 29.48(c) notes that *Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to an must be settled by delivery of such unquoted equity instruments, shall be measured as cost.*

- 3.80 The information to be presented will need to be useful for accountability and decision-making purposes to ensure it meets the objectives of financial reporting. Information will need to be consistent with the QCs set out in the Conceptual Framework. Decisions about the information to include will also need to take into account the constraints on information included in general purpose financial reporting.

Chapter 2: Currency Issued by the Entity

Introduction

- 1.1 Although laws vary by jurisdiction, monetary authorities generally are responsible for maintaining currency in circulation. All of the financial statements of monetary authorities examined recognized a liability at the face value of the notes in circulation. However, for coins, some monetary authorities recognize a liability while others do not. For those which recognize a liability it is measured at the face value of the coins issued.
- 1.2 This CP chapter considers the approaches to, and issues arising in, accounting for currency in circulation. The objective is to initiate a debate about matters such as:
- (a) The different types of currency in circulation;
 - (b) The recognition of revenue for currency issued into circulation; and
 - (c) The accounting options for recognition, measurement and derecognition of currency in circulation liabilities in order to provide the best information to users.

Chapter Objective

- 1.3 The IPSASB proposes the following objective for future guidance on accounting for currency in circulation:

An entity shall account for currency in circulation in a manner that helps users of its financial statements assess:

- The impact of currency in circulation on the entity's financial performance and financial position;
- The nature and extent of risks arising from distributing currency in circulation, and how the entity manages those risks; and
- The types (different categories and series) of currency in circulation issued by the entity.

- 1.4 The CP identifies options for accounting for currency in circulation (both notes and coins).
- 1.5 The options identified, relate to the type of currency, the stage in the development and distribution process, as well as the obligations monetary authorities incur in distributing and maintaining currency. The IPSASB will assess each option to consider how well each satisfies the objectives of financial reporting and meet users' information needs.

Scope and Definitions

- 1.6 This section of the CP addresses the scope and definitions for any future guidance on currency in circulation.

Consideration of GFS

- 1.7 The IPSASB considers it important to reduce differences with the statistical basis of reporting where appropriate. The most comprehensive guidance on statistical accounting for transactions of monetary authorities, is found in the Balance of Payments International Investment Position Manual—Sixth Edition (BPM6).

- 1.8 BPM6 notes in paragraph 3.95: *For an economy, a domestic currency is distinguished from foreign currency. Domestic currency is that which is legal tender in the economy and issued by the monetary authority for that economy; that is, either that of an individual economy or, in a currency union, that of the common currency area to which the economy belongs. All other currencies are foreign currencies.*
- 1.9 BPM6 notes in paragraph 5.36: *Currency consists of notes and coins that are of fixed nominal values and are issued or authorized by central banks or governments.*
- 1.10 BPM6 notes in paragraph 11.53: *Notes and coins are treated as liabilities at full face value. The cost of producing the physical notes and coins is recorded as government expenditure and not netted against the receipts from issuing the currency.*

Scope, Definitions and Descriptions

- 1.11 Having considered the above definitions and descriptions from BPM6, the IPSASB proposes the following definitions and supporting guidance.
- 1.12 **Currency in Circulation** is defined as:
“Physical notes and coins with fixed and determinable values that are legal tender issued by the monetary authority that is, either that of an individual economy or, in a currency union that the economy belongs.”
- 1.13 Legal tender is a medium of payment, recognized by a legal system as a valid form of payment. In the context of currency in circulation, this is physical notes and coins issued as legal tender.
- 1.14 Currency in circulation is domestic currency only. A domestic currency is distinguished from foreign currency. Domestic currency is that which is legal tender in the economy and issued by the monetary authority for that economy; that is, either that of an individual economy or, in a currency union, that of the common currency area to which the economy belongs. All other currencies are foreign currencies.
- 1.15 Adoption of a foreign currency as legal tender by a monetary authority, does not give rise to currency in circulation liabilities. For example, some monetary authorities, for countries other than the United States of America (US) use the US dollar as legal tender. Adoption of a foreign currency in this manner does not meet the definition of currency in circulation, as these are notes and coins issued by a foreign monetary authority for another economy. Therefore, accounting for such currency is not in the scope of guidance¹.

Accounting for Currency in Circulation – Notes – Conceptual Framework Approach

- 1.16 Issues related to currency in circulation will be examined through the cycle of transactions broken up into three steps:
- (a) The purchase and production of notes and coins;
 - (b) The distribution of notes and coins into circulation; and
 - (c) The removal of notes and coins from circulation.

¹ IPSAS 4, *The Effects of Changes in Foreign Currency Rates*, is the applicable guidance to account for foreign currency transactions.

- 1.17 A full cycle transactional approach is useful for understanding the potential accounting implications for each step in the process.

Purchase of Materials and Production of Notes

- 1.18 This step entails the purchase of raw materials to produce notes. It also includes labour and overhead costs related to the production of notes². Transactions related to the purchase and production of notes should be accounted for in accordance with IPSAS 12, *Inventories*³, because notes and coins are produced and held by monetary authorities for the issuance and maintenance of the supply of currency.
- 1.19 BPM6 notes in paragraph 11.53: *notes and coins are treated as liabilities at full face value. The cost of producing the physical notes and coins is recorded as government expenditure and not netted against the receipts from issuing the currency.*
- 1.20 According to the guidance existing in BPM6, it is clear that the cost of producing notes and coins should be recognized as an expense from a statistical perspective.
- 1.21 From an IPSAS 12 perspective an issue arises as to the appropriate timing of recognition of the expense. The appropriate recognition point is likely to be when the notes are issued and removed from inventory. See Appendix A, for an example of the transaction and journal entries related to the purchase of materials, production and distribution of notes.
- 1.22 The key issues related to accounting for currency in circulation arise after the purchase and production step, when the notes and coins are ready to be put into circulation.

Recognition of Liability on Distribution of Notes

- 1.23 An important role monetary authorities perform is management of currency in circulation. Monetary authorities, in most cases, are responsible for the production and distribution of notes and coins in circulation. In some jurisdictions production of notes and/or coins, may be contracted out. However, distribution and maintenance of the supply of currency is usually the remit of monetary authorities.
- 1.24 When new notes are put into circulation, the issue arises as to if it the transaction gives rise to the recognition of a liability or revenue.
- 1.25 If monetary authorities do not have an obligation to maintain notes in circulation, then issuance of notes leads to recognition of revenue and a surplus generated equal to the amount of revenue less the cost of the notes. This surplus is referred to as seigniorage⁴.
- 1.26 All of the monetary authorities financial statements examined, recognized a liability for currency in circulation. This is consistent with the treatment under GFS reporting guidelines. No variation was noted for the recognition of a liability for currency in circulation by monetary authorities. Because a

² Some monetary authorities may outsource the production of notes and coins, in such cases purchases of finished notes and coins would be accounted for by applying IPSAS 12, *Inventories*.

³ IPSAS 12.11 notes that inventories encompass goods purchased and held for resale... Inventories also encompass finished goods produced, or work-in-progress being produced, by the entity. Inventories also include (a) material and supplies waiting use in the production process, and (b) good purchased or produced by an entity...

⁴ Seigniorage is the term used to describe earning revenue from the issuance of currency (notes and coins) by an entity with the mandate to do so and is the difference between the cost of producing the currency and the amount received from issuing the currency (notes or coins).

liability is recognized equal to the face value of the notes in circulation, revenue and seigniorage (surplus) is not recognized for notes in circulation.

- 1.27 The Conceptual Framework, notes that a liability is: *A present obligation of the entity for an outflow or resources that results from a past event.*
- 1.28 A liability for notes in circulation arises due to the obligations of monetary authorities related to maintaining legal tender for their respective jurisdiction. The legal wording varies by jurisdiction, however, in most cases legislation requires monetary authorities to produce and maintain notes in circulation.
- 1.29 Because of the requirement to maintain legal tender, a present obligation exists, which is likely to result in an outflow of resources. The obligation arises because monetary authorities are required to exchange new currency for old or damaged notes. Replacement of notes, requires issuance of new notes equal to the face value of those being exchanged, or an equivalent amount of another financial asset.
- 1.30 The issue of whether a liability has been recognized, requires consideration of the different types of transactions which arise through the issuance of new notes.
- 1.31 The distribution of new notes, can result from the following two types of transactions:
 - (a) Transactions to increase the money supply, by increasing the number of notes in circulation; and
 - (b) Transactions with no change in the money supply, by exchanging old notes for new notes.
- 1.32 An increase in the money supply, occurs when notes are issued and consideration in the form of a financial asset—other than notes, is received. For example, issuance of new notes for an equal amount of government securities. Therefore, the liability increases as more notes exist in circulation. See Appendix A, for an example transaction and related journal entries.
- 1.33 A transaction which results in no change in the money supply, occurs when old notes are exchanged for new notes. Because old notes are exchanged for new notes, the total outstanding liability for currency in circulation does not change. See Appendix A, for an example transaction and related journal entries.

Measurement of Liability for Notes in Circulation

- 1.34 GFS requires measurement of the liability for notes in circulation at the cumulative face value of the notes issued.
- 1.35 Monetary authorities' financial statements examined also measure liabilities at the face value of notes in circulation. So current accounting practice, and GFS requirements are consistent with no variation noted.
- 1.36 The Conceptual Framework provides guidance for selecting an appropriate measurement basis by considering the nature of the liability and settlement options available.
- 1.37 An analysis of the different potential measurement bases for the liability for notes in circulation are discussed below:
 - (a) Historical Cost is defined in the Conceptual Framework as: *The consideration received to assume an obligation, which is the cash or cash equivalents or the value of other consideration*

received, at the time the liability is incurred. As noted in the example included in Appendix A, when a liability is incurred, the consideration received equals the face value of the notes issued into circulation. Therefore, it may be appropriate for the liability to be measured at the face value of currency in circulation. Distribution of notes, to either increase the money supply or maintain the current money supply (exchange old notes), results in consideration received, equal to the face value of the notes being issued.

- (b) Cost of Fulfillment is defined in the Conceptual Framework as: *The Costs that the entity will incur in fulfilling the obligations represented by the liability, assuming it does so in the least costly manner.* The Conceptual Framework notes that for this measurement basis, when it is dependent on uncertain future events, all possible outcomes are taken into account. If we assume the least costly manner to fulfill the obligation is the cost of producing new notes and not related to the face value of the notes produced. This may indicate that the value using cost of fulfillment is limited to the cost of producing replacement notes. However, if the view is taken that the cost of fulfilling the obligation is based on the value of the notes or financial assets exchanged, the cost of fulfillment may lead to measurement at face value of the notes issued.
- (c) Market Value is defined in the Conceptual Framework as: *The amount for which a liability could be settled between knowledgeable, willing parties in an arm's length transaction.* This may also be appropriate, as the face value of currency issued would only be exchanged for an equal amount of currency at face value, or a financial asset—other than currency of equal value received. For example, a one hundred dollar note in circulation, would only be exchanged for another 100 dollar note, or alternatively a financial asset—other than cash with a value of 100 dollars.
- (d) Cost of Release is discussed in the Conceptual Framework as follows: *refers to the amount of an immediate exit from the obligation, or the amount a creditor will accept in settlement of the claim.* This measurement basis may not be appropriate as monetary authorities have little to no ability to seek recourse to exit the obligation. However, even if they had the ability to do so, it is unlikely that the settlement would be at an amount less than face value of the notes issued, as holders of notes would not likely agree to an exchange at a discount.
- (e) Assumption Price is discussed in the Conceptual Framework as follows: *The amount that an entity would rationally be willing to accept in exchange for assuming an existing liability.* This measurement basis may not be appropriate, as the obligation to maintain currency is not considered transferrable from the monetary authority.

1.38 Historical cost and market value may both result in measurement of the liability at the face value of the notes issued. Cost of fulfillment may result in measurement at the face value of the notes or the estimated cost of producing new notes.

Derecognition of Liability for Notes in Circulation

1.39 The Conceptual Framework notes that *derecognition is the process of evaluating whether changes have occurred since the previous reporting date that warrant removing an element that has been previously recognized from the financial statements, and removing the item if such changes have occurred.* There are two issues related to derecognition of liabilities for notes in circulation:

- (a) For transactions to decrease the supply of money, notes are removed from circulation, it is appropriate to derecognize the related liability as those notes are no longer outstanding; and

- (b) A further issue relates to notes issued and in circulation for many years (old series of notes). Monetary authorities do not appear to derecognize notes in circulation for very long periods of time. Even those series which have been issued many years in the past and which are unlikely to be exchanged and may even no longer be legal tender.
- 1.40 Transactions to decrease the money supply occur when notes are received as consideration for a financial asset—other than notes. Therefore, the liability for currency in circulation decreases as less notes exist in circulation. See Appendix A, for an example transaction and related journal entries.
 - 1.41 Legal decisions may cancel old series of currency (making it no longer legal tender), and the legal obligation may cease to exist. This raises the issue of how to appropriately derecognize such liabilities, such as the appropriate time period and point of derecognition. As well as assessing if a legal obligation to maintain old series is discharged because notes have been cancelled, or if a constructive obligation may still exist based on past practices of exchanging new notes for old notes. However, in instances where it is deemed that an obligation no longer exists, it is appropriate to derecognize the liability.
 - 1.42 Derecognition of liabilities for currency in circulation, raises an issue of the appropriate place in the financial statements to recognize the resulting gain. Should these gains be recognized in the statement of financial performance, or directly in net financial position?
 - 1.43 Recognition directly in net financial position may be appropriate, as the transaction reverses a liability which relates to prior periods. Recognition of a gain in the statement of financial performance may impair the current cost of services in the statement of financial performance. Alternatively, derecognition of the liability results in a realized gain, and could be argued to be important information to recognize in the statement of financial performance, to communicate the impact on current period performance. The Conceptual Framework is silent on where in the financial statements elements should be recognized.

Accounting for Currency in Circulation – Coins – Conceptual Framework Approach

- 1.44 Unlike notes in circulation, the practice of accounting for coins by monetary authorities is inconsistent. Monetary authority financial statements examined, indicate that some do not recognize a liability for coins in circulation, while others do.
- 1.45 For those monetary authorities which do not recognize a liability for coins in circulation, one reason may be because another government entity recognizes the liability. To confirm if this may be the case, some jurisdictions which do not recognize a liability and which have whole of government accounts, were considered to ascertain whether a liability was recognized. One such jurisdiction which does not recognize a liability for coins is the UK. The UK does produce whole of government accounts, the most recent available are for the year ended 31 March 2014. These financial statements noted that coins in circulation were considered a remote contingent liability. This concept does not exist in IPSAS. A remote contingent liability is a future event that is less likely to occur than a contingent liability.
- 1.46 There may be different reasons for not recognizing a liability for coins, such as:
 - (a) The overall value of the coins in circulation may not be material for the particular monetary authority;

- (b) The monetary authority may not view the possibility of an outflow of resources to be probable and therefore does not recognize a liability; or
 - (c) The monetary authority may estimate that because coins are made of metal, they are harder to damage and will require replacement less often. Even when damaged coins are exchanged they can be recycled and reused to produce new coins, reducing the potential outflow of resources.
- 1.47 Monetary authorities generally have large balance sheets, therefore in some cases recognizing a liability for coins in circulation may not be deemed material by preparers or auditors. If the size of the liability is not material, providing information would not be required as the absence of such information would not impact users' decision making or accountability judgments in regards to the entity.
- 1.48 Monetary authorities in some jurisdictions may not assess that a liability should be recognized because there may not be a legal requirement to do so. If the laws in a particular jurisdiction only require a monetary authority to maintain notes in circulation, a liability may not exist because of the lack of a legal requirement for the monetary authority to maintain the supply of coins (exchange damaged coins or old series for new ones). However, if the monetary authority has a previous pattern of behavior of exchanging damaged coins for new ones, a constructive obligation may exist, even in the absence of a legal obligation.
- 1.49 Another possibility is that there may be a low probability of an outflow of resources related to coins in circulation. The probability of an outflow of resources may be different for coins over notes. Notes, because of the material used to produce them (paper or plastic), have a higher likelihood of being damaged or ruined, compared to coins made from metal. Additionally notes have higher face values and are more valuable, so are more likely to be exchanged when damaged. Under such circumstances the liability may not meet the recognition criteria.
- 1.50 When determining if an outflow of resources is probable, another consideration is the amount which may be recovered because of the residual value of damaged coins. A damaged note has little or no residual value. However, damaged coins have residual value because they are metal and recyclable and in some cases may have a value comparable to the face value of the coins, especially when considering older coins which sometimes contain more valuable metals (such as silver, copper and nickel). Monetary authorities may determine that an outflow of economic of resources may be limited because of the residual value of coins.

Accounting for Coins when a Liability is Recognized

- 1.51 Similar to notes, there are various steps in the process for coins. As for notes, transactions related to the purchase of raw materials and production of coins appear appropriate to be accounted for in accordance with IPSAS 12, *Inventories*⁵. See Appendix B, for a breakdown of the transactions related to this step in the process.
- 1.52 When coins are put into circulation, similar to notes, there are two potential transactions related to the recognition of a liability. The first transaction is to increase the supply of coins. Transactions to put coins into circulation result when another financial asset—other than coins is received as

⁵ IPSAS 12.11 notes that inventories encompass goods purchased and held for resale...Inventories also encompass finished goods produced, or work-in-progress being produced, by the entity. Inventories also include (a) material and supplies waiting use in the production process, and (b) good purchased or produced by an entity.

consideration. For this transaction, the first step in the process is to recognize revenue. If an obligation to maintain coins exists, a liability is also recognized and if so, depending on how the liability is measured, seniorage may occur. See Appendix B, for an example transaction and journal entries.

- 1.53 Seiniorage occurs when currency is issued by the monetary authority and revenue is recognized incremental to the cost of producing it. For notes, as a liability is recognized for the face value of the notes in practice, seiniorage generally does not occur directly⁶. However, for coins, monetary authorities do recognize seiniorage revenue when a liability is not recognized for coins in circulation.
- 1.54 From a measurement perspective, if a liability is recognized, the same basis for measuring it should be used for both coins and notes. The basis used should not differ, even if the probability of the obligation being recognized differs.
- 1.55 Derecognition of liabilities for coins in circulation, should be consistent with derecognition of liabilities for notes in circulation as discussed in paragraphs 1.39–1.43.

Consistency with Current IPSAS

- 1.56 Another approach to consider for currency in circulation liabilities is the accounting requirements under existing IPSAS standards. This provides information to contrast against the Conceptual Framework considerations for currency in circulation liabilities.
- 1.57 IPSAS 19, *Provisions, Contingent Liabilities, and Contingent Assets* requires that *a provision shall be recognized when: (a) An entity has a present obligation (legal or constructive) as a result of a past event; (b) It is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; and (c) A reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognized.* Similar to the discussion based on the Conceptual Framework, the recognition of the liability depends on the existence of a present obligation as a result of a past event, which is probable and expected to result in an outflow of resources. Accounting for currency in circulation under IPSAS 19, would not be inconsistent with the Conceptual Framework discussion presented earlier in this chapter. However, for the case when an obligation is not recognized, IPSAS 19 does provide guidance on contingent liabilities. Noting that contingent liabilities⁷ shall not be recognized and should instead be disclosed unless the possibility of an outflow or resources embodying economic benefits or service potential is remote.
- 1.58 Considering the nature of currency in circulation, the requirements of IPSAS 28–30, *Financial Instruments* are appropriate to consider. Similar to the earlier discussions in this chapter, the key issue is whether or not an obligation exists. When an obligation exists, understanding if financial instruments accounting under IPSAS 28–30 is applicable, is the next consideration.
- 1.59 For financial instruments accounting to be applicable, the liability for currency in circulation needs to satisfy the definitions of a financial instrument and financial liability.

⁶ There is a notion of indirect seiniorage for notes, when interest bearing securities are received as consideration for notes, which do not bear interest. Monetary authorities accrue interest on those interest bearing securities, which is interest revenue to the monetary authority.

⁷ IPSAS 19.18 defines a contingent liability as: *(a) A possible obligation that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or (b) A present obligation that arises from past events, but is not recognized because: (i) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or (ii) The amount of the obligation cannot be measured with sufficient reliability.*

- 1.60 The definition of a financial asset in IPSAS 28, *Financial Instruments: Presentation* states that cash is a financial asset. However, the definition of a financial liability does not indicate that the entity issuing cash has a financial liability. It states that a financial liability is a contractual obligation to deliver cash or another financial asset to another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable. Considering this guidance, it may be appropriate that currency in circulation liabilities are financial liabilities. Because monetary authorities are required to maintain currency in circulation (in most cases) by exchanging old notes and sometimes coins, for new ones. Even though a physical contract may not exist, the substance of the transaction may be contractual because of the currency legislation making it legal tender, gives rise to an obligation. Currency in circulation give rise to similar rights and obligations as a bearer instrument, such as a cheque. When a cheque is written it essentially is a promise pay a fixed amount of money from the cheque writers bank account when the cheque is presented by the holder. When currency is legal tender, monetary authorities have an obligation to deliver cash or another financial asset to holders of currency when presented to the monetary authority. Maintaining currency by monetary authorities has a cost and therefore satisfies the potentially unfavorable element of the definition. The definition of a financial instrument is any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity. As cash is defined as a financial asset, and when currency is legal tender it likely qualifies as a financial liability, it may be appropriate to consider currency liabilities financial instruments.
- 1.61 Accounting for financial liabilities in IPSAS 28–30, requires recognition and subsequent measurement based on the classification of the liability. Those classified as loans and receivables, are initially recognized and measured at fair value plus transactions costs, and subsequently measured at amortized cost. Those classified as fair value through surplus or deficit are initially recognized at fair value with transaction costs expensed as incurred in the statement of financial performance with subsequent measurement at fair value. Accounting for currency in circulation liabilities at amortized cost, may not be appropriate, as they do not have a maturity date or interest payments, because they are cash. Therefore, it may be more appropriate to account for currency liabilities at fair value through surplus or deficit, which would be at the face value of the currency issued and outstanding as discussed in paragraph 1.37.

Presentation and Disclosure

- 1.62 This section of the CP discusses at a high level the information to be presented in respect of currency and coin in circulation. It does not propose specific requirements. These requirements are linked to decisions regarding the approach to recognition and measurement, and therefore will be determined once the IPSASB has considered the responses to this chapter of the CP.
- 1.63 The information to be presented will need to be useful for accountability and decision-making purposes to ensure it meets the objectives of financial reporting. Information will need to be consistent with the QCs set out in the Conceptual Framework. Decisions about the information to include will also need to take into account the constraints on information included in general purpose financial reporting.

Appendix A: Currency in Circulation: Notes

Appendix A, breaks down the different stages in the process to produce, distribute and maintain notes in circulation by monetary authorities. The examples transactions have been developed along with journal entries for each step of the process to demonstrate how transactions are accounted for.

Purchase Materials			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Purchase Materials - Journal Entry	<i>Purchase Material (Ink & Paper) for 100</i>	<i>Purchase Material (Ink & Paper) for 100</i>	<i>No new notes needed for this transaction.</i>
	DR Inventory 100	DR Inventory 100	
	CR Cash 100	CR Cash 100	
Production of Notes			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Production of Notes Journal Entry	<i>Production of 1000, 100 notes. Production costs (Overhead & Labour) - cost 100</i>	<i>Production of 1000, 100 notes. Production costs (Overhead & Labour) cost 100</i>	<i>No new notes needed for this transaction.</i>
	DR Inventory 100	DR Inventory 100	
	CR Cash 100	CR Cash 100	

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Distribution of Notes			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Journal Entry to Recognize Financial Asset Received for Notes Distribution	<i>Distribution of 1000, \$100 notes, total cumulative face value 100,000. Transaction to Increase supply of notes.</i>	<i>Transaction to exchange old notes for new notes. Distribution of 1000, \$100 notes, total cumulative face value 100,000. Net impact of transaction Nil - exchanging old notes for new notes.</i>	<i>No new notes distributed for this transaction.</i>
	DR Financial Asset (Other than cash) 100,000	DR Cash (old notes) - 100,000	
	CR Revenue - Distribution of Notes 100,000	CR Revenue Dist. Of New Notes 100,000	
		DR Revenue Dist of New Notes 100,000	
		CR Cash (new notes) 100,000	
Journal Entry to Recognize Cost of Notes Issued	DR COGS - 200	DR COGS - 200	
	CR Inventory 200	CR Inventory 200	
Journal Entry to Recognize Increase in Liability for Currency Issued.	DR Revenue 100,000	<i>Net impact on liability is nil. As exchanging old notes, for new notes.</i>	
	CR Liability for Currency Issued 100,000		

Removal of Notes From Circulation			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Derecognition of liability due to removal of notes from circulation	<i>No notes being removed from circulation. No transaction to record.</i>	<i>Net change is nil, as old notes exchanged for new notes. Therefore, no impact on liability recognized.</i>	<i>Notes being removed from circulation, must exchange a financial asset other than cash. Assume 1000, \$100 face value notes removed from circulation.</i>
			DR Liability, Currency in Circulation 100,000
			CR Financial Asset (other than cash) 100,000

Appendix B: Currency in Circulation: Coins

Appendix B, breaks down the different stages in the process to produce, distribute and maintain coins in circulation by monetary authorities. The examples transactions have been developed along with journal entries for each step of the process to demonstrate how transactions are accounted for.

Purchase Materials			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Purchase Materials - Journal Entry	<i>Purchase Material (metal) for 100</i>	<i>Purchase Material (Metal) for 100</i>	<i>No new coins needed for this transaction.</i>
	DR Inventory 100	DR Inventory 100	
	CR Cash 100	CR Cash 100	

Production of Coins			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Production of Coins Journal Entry	<i>Production of 1000, .25 coins. Production costs (Overhead & Labour) - cost 100</i>	<i>Production of 1000, .25 coins. Production costs (Overhead & Labour) cost 100</i>	<i>No new coins needed for this transaction.</i>
	DR Inventory 100	DR Inventory 100	
	CR Cash 100	CR Cash 100	

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Distribution of Coins			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Journal Entry to Recognize Financial Asset Received for Coins Distribution	<i>Distribution of 1000, .25 coins, total cumulative face value 250. Transaction to Increase supply of coins.</i>	<i>Transaction to exchange old coins for new coins. Distribution of 1000, .25 coins, total cumulative face value 250. Net impact of transaction Nil - exchanging old coins for new coins.</i>	<i>No new coins distributed for this transaction.</i>
	DR Financial Asset (Other than cash) 250	DR Cash (old Coins) - 250	
	CR Revenue - Distribution of Coins 250	CR Revenue Dist. Of New Coins 250.	
		DR Revenue Dist of New Coins 250	
Journal Entry to Recognize Cost of Coins Issued	DR COGS - 200	DR COGS - 200	
	CR Inventory 200	CR Inventory 200	
Journal Entry to Recognize Increase in Liability for Currency Issued ⁸ .	DR Revenue 100,000	<i>Net impact on liability is nil. As exchanging old coins, for new coins.</i>	
	CR Liability for Currency Issued 250 [assumes liability recognized for coins]		

Removal of Coins From Circulation			
Transaction	Increase Money Supply	No Change Money Supply	Decrease Money Supply
Derecognition of liability due to removal of coins from circulation	<i>No Coins being removed from circulation. No transaction to record.</i>	<i>Net change is nil, as old coins exchanged for new coins. Therefore, no impact on liability recognized⁹.</i>	<i>Coins being removed from circulation, must exchange a financial asset other than cash. Assume 1000, .25 face value coins removed from circulation.</i>
			DR Liability, Currency in Circulation 250
			CR Financial Asset (other than cash) 250

⁸ This journal entry would only be recorded when monetary authorities recognize a liability for coins in circulation. For those which do not recognize the liability, this entry would not be recorded.

⁹ When old coins are received, there may be a journal entry to recognize the residual value of the metal received as inventory which has not been included. However, for coins, monetary authorities would receive old coins which would have residual value due to the scrap metal.

