Chapter 6

PRELIMINARY STUDY ON FUNDAMENTAL PRINCIPLES OF CENTRAL BANK FINANCIAL REPORTING: SRI LANKA[1]

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1. Introduction

A central bank possesses a unique set of objectives aimed at fulfilling its mandate of maintaining economic stability, financial system stability and development of economic resources of a country. The uniqueness of these objectives sets a central bank apart from a commercial entity, which pursues revenue and is commonly attributed as being motivated by profit. Although dissimilar in their objectives, both the central bank and commercial entities require financial reporting as means of identifying transactions, managing historic data, financial data reporting and providing a tool that allows each entity to gauge its performance during the financial calendar. Centering on accountability and good governance, the international accounting standards are wholly suited for the task of financial reporting, which seeks to establish transparency and sound accounting practices among institutions. In this context, central bank accounting practices should remain fully accommodative of the objectives of the central bank. In identifying the present status of financial reporting of the Central Bank of Sri Lanka (CBSL), this report discusses the overview of the establishment and mandate of the Bank, the basic principles and the purpose of a central bank's financial statements, Accounting Framework of the Central Bank of Sri Lanka and some salient accounting treatment provisions and concludes with a brief discussion on the necessity of central banks to have a globally recognized accounting standard.

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[1] This team project paper was prepared for the SEACEN Research Seminar on "Fundamental Principles of Central Bank Financial Reporting: A Preliminary Study on SEACEN Economies," which was attended by project team members from six SEACEN members, namely Cambodia, India, Indonesia, Philippines, Sri Lanka and Thailand. Observers included officials from the member central banks/monetary authorities of Brunei Darussalam, Fiji, Malaysia and Mongolia. Central banks' unique objectives are fully reflected by its financial reporting and the standards followed by the reporting requirements were a key aspect that was explored in detail.

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2. Overview of the Establishment and Mandate of the Central Bank of Sri Lanka

The Central Bank of Sri Lanka was established in August 1950 under the auspices of the Monetary Law Act, No. 58 of 1949 (MLA). Sri Lanka, at the time known as Ceylon, gained independence in February 1948. Ceylon's post-independence Government, recognizing the importance of an effective monetary policy regime and dynamic financial sector for the development of the economy, mooted the establishment of the Central Bank of Ceylon. With the economic policy change prompting an independent monetary system to bolster the newfound political independence, the Government of Ceylon in July 1948, requested technical assistance from the Government of the United States for the setting up of a central bank. As a result of this request, Mr. John Exter, an economist from the United States Federal Reserve Board, was appointed to advise the Government of Ceylon and report on the feasibility of setting up of a central bank. This study yielded the Exter Report (consisting of two parts), which still continue to provide useful insights to the economic principles surrounding the establishment of the central bank and the rationale behind the legal provisions that defines the objectives, powers and functions of the Central Bank of Sri Lanka.

Prior to the setting up of the Central Bank, a currency board system known as the Board of Commissioners of Currency, was in place to administer the issue of currency. In principle, a currency board system required the maintenance of a stock of foreign reserves, as its issue of domestic currency was equivalent to its foreign assets (Balino et al., 1997; Economist, 1997), whereas a central bank system could issue currency against both domestic assets as well as foreign assets (Karunatilake, 1986).The Board of Commissioners of Currency issued Ceylon rupee notes and coins against an equivalent value of the Indian rupee, which in turn, was pegged to the UK sterling pound. The bulk of the foreign reserves of the country were held in sterling as well. With political independence in 1948, there was no longer sound reasoning for linkages to the Indian currency or to the sterling, highlighting the need for a fully-fledged central bank. With the enactment of the Monetary Law Act in 1949, the Central Bank of Ceylon was established and commenced its functions from 28 August 1950. The establishment of the Central Bank in 1950 made history for Ceylon as the first colony after independence to have replaced the currency board currency issuance system with a central bank issuance system. In 1985, the Central Bank of Ceylon was renamed Central Bank of Sri Lanka.

The initial objectives of the Central Bank were - i) stabilization of domestic monetary values; ii) preservation of the par value of the Ceylon rupee; iii) the promotion and maintenance of a high level of production, employment and real income; and, iv) the promotion of the full development of productive resources in Ceylon. These stabilization and developmental objectives guided the functions of the Central Bank over the next four decades. In allowing for the complexities of modern economic development, especially in information technology, the Central Bank embarked on a modernization program in 2000. The modernization program reviewed and reformulated the objectives of the Central Bank to: (i) maintain economic and price stability; and, (ii) maintain financial system stability, …*with a view to encourage and promote the development of the productive resources of the country.*[4] In essence, the initial stabilization and developmental objectives were captured in the current objectives as well.

The statutory powers, duties and functions stemming from the Monetary Law Act are vested with the Monetary Board of the Central Bank. The Monetary Board was also responsible for the management, operations and administration of the Central Bank. The Monetary Board comprised the Governor of the Central Bank in the capacity of the Chairman of the Board, the Secretary to the Ministry in charge of finance and three appointed non-executive members. The latter members are appointed by the President on recommendation by the Minister of Finance with the concurrence of the Constitutional Council. The term of office of the Governor and the non-executive Board members is six (6) years. The quorum for Monetary Board meetings is three (3) members. The concurrence of three (3) members is required for decisions of the Monetary Board to be valid. However, in cases where a unanimous decision is required, the concurrence of all five (5) members is necessary. The Monetary Policy Committee, chaired by the Deputy Governor in charge of price stability, assists the Monetary Board in formulating monetary policy.

Apart from its main objectives, the Central Bank of Sri Lanka performs several agency functions as well. The management and administration of public debt, foreign exchange management, regional development and the management of the largest superannuation fund in the country, the Employee’s Provident Fund are carried out under the auspices of the Central Bank. Further, the Financial Intelligence Unit of the country also functions under the umbrella of the Central Bank.

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[4] Section 5, Monetary Law Act, No. 58 of 1949, as amended.

The Central Bank is technically an autonomous institution, with its governing body, the Monetary Board, consisting of apolitical persons. Monetary policymaking is carried out independently without interference from the Government. However, the MLA provides the Minister of Finance with the power to issue directives especially on economic matters, which states that in matters concerning general economic policy, the views of the Government maybe final (Karunatilake, 1986). The presence of the Secretary to the Ministry of Finance highlights the importance of the close coordination that should be maintained between the Ministry of Finance (which determines fiscal policy) and the Central Bank (which implements finance and the monetary policy). Further, the Central Bank acts as a fiscal agent, banker as well as advisor to the Government. Routine reports are prepared by the Central Bank articulating the economic policies and reviewing the performance of the economy. The Annual Report of the Central Bank is required to be presented to the Minister of Finance every year by 15 September, reporting on the financial and economic conditions, which would serve as pertinent information when preparing the annual budget for the country. These reporting requirements pave the way for close coordination between government policies and monetary policy of the central bank for the betterment of the economy.

Furthermore, capital provisioning provides a glimpse on the level of independence of the Central Bank. The starting capital of the Central Bank of Ceylon was 15 million rupees, being the sum appropriated from the surplus assets of the Board of Commissioners of Currency. Subsequently, for the purpose of operational requirements, unutilized reserves amounting to 25 billion rupees and profit transfers amounting to 10 billion rupees were appropriated as capital. The Monetary Board has the provisions to increase the capital of the Central Bank to a sum not exceeding 50 billion rupees. In doing so, the Central Bank has to give due regard to the viability and stability of the financial system of Sri Lanka and the interests of the national economy. From time to time, the capital of the bank was increased with the concurrence of the Minister of Finance, as per the provisions of the MLA. As of September 2014, with the concurrence of the Minister of Finance, the capital was increased to 50 billion rupees by capitalizing the Central Bank’s reserves.

3. Purpose of the Central Bank’s Financial Statements

The conceptual framework identified by the International Accounting Standard Board (IASB) recognizes the objective of general purpose financial reporting is “...to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.”

The primary users of a central bank's financial reporting often consist of current and potential investors in the economy and its financial instruments. These include investors in International Sovereign Bonds, corporate and government securities, multinational organizations and lenders such as the International Monetary Fund (IMF) and other donor agencies, transaction counterparties and the general public. The financial information is utilized in a myriad of decision making about investments, investment holdings, assessing risks in continuing banking relations and other transactions with the bank and in providing financial assistance or other forms of credit to the country. Therefore, such investors and lenders would review the financial information to verify the financial position and performance of the economy in making their investment decisions.

However, a central bank is different from a commercial entity as its primary objective is not centered on earning profits. The basis of accountability for a central bank and the success of its operations, therefore, would be the effectiveness of its policies and operations leading towards the achievement of its core objectives and not necessarily its profitability. These statutory objectives are the fundamental features that distinguish a central bank from any other commercial entity. Therefore, the main purposes of the financial reporting for a central bank are accountability and good governance.

In the context of the CBSL, the same principles of accountability and good governance apply through the adoption of the International Financial Reporting Standards (IFRS) accounting principles. The Central Bank is also engaged in active reserve management, which is motivated by gaining profits. The Central Bank's activity is comparable to a commercial bank in this aspect, while the accounting principles along with disclosure requirements as necessitated by the IFRS, are adhered to closely.

4. Basic Principles Underlying the Financial Statements as per the IASB

The International Accounting Standards Board's (IASB) conceptual framework identifies *relevance* and *faithful representations* as the fundamental qualitative characteristics of useful financial information.

Relevant financial information is imperative in making a difference in the decisions made by users. Faithful representation seeks to maximize the underlying characteristics of completeness, neutrality and freedom from error. Comparability, verifiability, timeliness and understandability are qualitative characteristics that enhance the usefulness of information that is relevant and faithfully represented.

The information concerned should be *material enough* to warrant a separate disclosure. Materiality is an entity-specific aspect of relevance based on the nature or magnitude (or both) of the items, to which, the information relates in the context of an individual entity's financial report, making a difference in the decisions made by users.

These qualitative characteristics are applicable to the financial reporting of a central bank as well.

4.1 Underlying Assumption

The IFRS Framework states that the going concern assumption is an underlying assumption. The financial statements are normally prepared on the assumption that an entity is a going concern and will continue in operation for the foreseeable future. Hence, it is assumed that the entity has neither the intention nor the need to liquidate or curtail materially, the scale of its operations. If such an intention or need exists, the financial statements may have to be prepared on a different basis, and the basis used is disclosed (IASB Conceptual Framework, 2010).

Financial statements of the CBSL are also prepared on a going concern basis, although it is not specifically disclosed in the financial statements, unlike financial statements of a commercial entity.

5. Accounting Framework of the Central Bank of Sri Lanka

The CBSL adopted the IFRS framework in 2002 voluntarily, on the recommendation of the IMF Safeguard Mission, considering the long-term benefits of following such standards which include the easily comparable financial statements, gaining of global recognition on the compliance with international best practices and high transparency resulting in favorable recognition by the foreign lenders/investors.

In Chapter 5 of the IMF Safeguards Assessment Policy of the Accounting Standards for Central Banks by PricewaterhouseCoopers, Catsambas and Hemus (2003) identifies the requirement of adopting an international accounting framework for the countries under the safeguard assessment policy as follows:

"…A fundamental requirement of the safeguards policy is that central banks of borrowing member countries must publish annual financial statements, which should be independently audited by an auditor external to the central bank in accordance with internationally acceptable standards…"

The International Monetary Fund Safeguards Assessments: Review of Experience,[5] prepared by the Finance Department of the Central Bank of Sri Lanka in consultation with relevant Central Bank Departments, highlighted an updated ELRIC Framework[6] that identifies the importance of international accounting framework as "Financial Reporting Framework - Adequate financial reporting principles and practices are essential elements of effective central bank operations that encompass the provision of financial information to both central bank management and to external parties, the latter typically through published interim and annual financial statements. For such information to be useful, it must be relevant, reliable, timely, readily available, consistent in presentation over time, and based upon recognized standards, such as IFRS. Non-adherence to accepted international practices could indicate a lack of transparency or accountability. The objective of assessing financial reporting is to ensure that the central bank adheres to international good practices in the adoption of accounting principles for internal reporting to management, and the published annual and interim financial statements."

Before adopting the IFRS, CBSL's financial statements did not adopt local accounting standards. However, the financial statements were in compliance with the provisions of the Monetary Law Act. During this period, the local Generally Accepted Accounting Principles (GAAPS) under the name of Sri Lanka Accounting Standards (SLAS) were recognized as not being on par with the IAS/IFRS. Hence, the Central Bank adopted international accounting standards to have a globally acceptable accounting framework.

6. The Process of Achieving Full Compliance with IFRS

Achieving full compliance status in the IFRS accounting standards was a gradual process. The Central Bank prepared its first set of financial statements under the IAS basis for the financial year 2001 and the financial statements were qualified in the requirements of many

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[5] As approved by Andrew Tweedie, 1 July 2010, Available at: https://www.imf.org/external/np/pp/eng/2010/070110.pdf

[6] ELRIC Framework is an acronym for E - External audit mechanism, L -Legal structure and independence, R-Financial reporting, I -Internal audit requirement and C – System of internal controls (referred to in "The Accounting Standards for Central Banks of PricewaterhouseCoopers," by Thanos Catsambas and Chris Hemus).

standards. The Bank was able to obtain full compliance in 2004. In this process, the Central Bank had to take a number of actions to achieve full compliance status including disposal of its investments in subsidiaries and associate companies, improve the processes that generate the disclosure requirements of certain standards, prepare the cash flow statement, etc. Currently, some of the international accounting standards applicable to the Central Bank are listed below.

IAS 1	*Presentation of Financial Statements*	IAS 24	*Related Party Disclosures*
IAS 7	*Statement of Cash Flows*	IAS 32	*Financial Instruments: Presentation*
IAS 8	*Accounting Policies, Changes in Accounting Estimates and Errors*	IAS 36	*Impairment of Assets*
IAS 10	*Events after the Reporting Period*	IAS 37	*Provisions, Contingent Liabilities and Contingent Assets*
IAS 16	*Property, Plant and Equipment*	*IAS 38*	*Intangible Assets*
IAS 17	*Leases*	IAS 39	*Financial Instruments: Recognition and Measurement* Superseded by IFRS 9 effective 1 January 2018
IAS 19	*Employee Benefits*	IAS 40	*Investment Property*
IAS 21	*The Effects of Changes in Foreign Exchange Rates*	IFRS 7	*Financial Instruments: Disclosures*
IAS 20	*Accounting for Government Grants and Disclosure of Government Assistance*	FRS 9	*Financial Instruments* *effective 1 January 2018*
		IFRS 13	*Fair Value Measurement*

The main issues encountered and the resolutions are as follows.

6.1 IAS 21 and Exchange Revaluation Gains/Losses

It was observed that the requirements of IAS 21, the Effects of Changes in Foreign Exchange Rates, and Section 41 of MLA are contradictory. As per IAS 21, “Exchange differences arising when monetary items are settled or when monetary items are translated at rates different from those at which they were translated when initially recognized or in previous financial statements are reported in profit or loss in the period."

Section 41 of MLA reads;

> *"(1) Profits or losses arising from any revaluation of the Central Bank's net asset or liabilities in gold or foreign currencies as a result of changes in the par value of the Sri Lanka rupee or of changes in the parities or exchange rates of foreign currencies with respect to the Sri Lanka rupee, or profits or losses assumed by the Central Bank in accordance with the provisions of section 79, shall not be included in the computation of the annual profits and losses of the Central Bank.*
> *(2) All such profits or losses shall be carried in a special account, which shall be named "International Reserve Revaluation Account," and the net balance of which shall appear either among the liabilities or among the assets of the Central Bank, according as the revaluations have produced net profits or net losses.*
> *(3) The International Reserve Revaluation Account shall be neither credited nor debited for any purposes other than those specifically mentioned in this section."*

Adoption of the above section verbatim would have ended up in a violation of the IFRS framework as this balance does not represent an 'asset' or a 'liability' as defined by the IFRS. This issue was faced by other central banks around the world that have adopted IFRS. To comply with the spirit of the above requirement and to be in compliance with IFRS, central banks using IFRS have adopted what is known as the "income approach" where the difference is routed through the income statement and then removed from the retained earnings and considered as a reserve. The CBSL has consistently followed this method since the adoption of the IFRS in 2002. The Reserve Bank of Australia, Reserve Bank of New Zealand, Bank of Canada, Bank of Mauritius are several other IFRS compliant central banks that follow this method.

In practice, this contradictory provision is overcome by the CBSL in the following manner:

Exchange revaluation gains/losses are taken into the income statement and thereby meet the requirement of IAS 21. Once the net profit inclusive of the exchange gains/losses are transferred to Retained Earnings, such gains/losses are removed and transferred to a special account, thus avoiding the distribution of such book profits. However, as per IAS, the net balance of the revaluation cannot be included among assets or liabilities since it does not meet the definition of assets or liabilities as per IAS. The expectation of this section is to avoid distribution of book profits i.e., exchange gains. Hence, it was decided to include the special account balance among reserves as it does not violate the true essence of the section of the MLA. i.e., prevent distribution of book profits. Therefore, as explained above, the Bank simultaneously meet the contradictory requirements while maintaining full compliance with IAS/IFRS.

Kurtzig (2003)[7] provides the way a central bank can overcome the key area in which IAS appear to in conflict with central banks. Inclusion of unrealized gains on foreign exchange revaluation as per IAS could be inflationary as the profits are monetized through government spending for which the central bank has to take sterilization operations. He further states that the distribution of unrealized gains removing the buffer against future reversal of currency movements, may result in the erosion of capital. The preferred option is to report according to the IAS rather than taking such gains directly into reserves and then appropriate such gains into a separate reserve. To do this, supporting provisions must be made in the central bank law to require profit transfers to the government to not include unrealized gains. In this way, the central bank can overcome a key obstacle in improving transparency by adopting an internationally recognized framework.

6.2 Extraordinary Expenses

As per Section 40 of MLA, it is allowed to exclude all or any part of any extraordinary expenses of the following description which may have been incurred during that year.

(i) The costs of any extraordinary coin or note issue;
(ii) Expenditures incurred in the issue and placing of, and the payment of interest on, the securities to which reference is made in Section 91; and,
(ii) Interest paid on bank reserves in accordance with Section 95.

However, according to IAS/IFRS, there is no concept of extraordinary expenses and thus deferring of such expense is not allowed.

During 2010-2012 and in 2014, the CBSL had to incur a large amount of interest expenses to mop up excess liquidity in the market and this expense was considered for deferral. However, it was concluded that as per IAS, the deferral of expense is not possible and if the

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[7] Kurtzig, Joshua, (2003), “Coping with Accounting Standards and Central Bank Transparency,” Accounting Standards for Central Banks, Central Banking Publications: London, pp. 311-317.

Bank does not take any action, it should be reflected from its results. Therefore, it was decided not to defer the expenses and to give an additional disclosure on the expenses incurred by the Bank in its activities to absorb the excess liquidity in the market.

6.3 Marking to Market Gains/Losses

The provisions of the MLA reflect the market conditions prevailing during the period it was drafted. Marking-to-market of financial instruments came into effect with the subsequent introduction of IAS 25 and IAS 39 and hence there was no provision in the MLA on how it should be dealt with. Therefore, it has been decided by the Monetary Board of the Central Bank to eliminate such marking-to-market gains from the distributable profit, thereby building up a reserve, named the Market Valuation Reserve – Trading Securities (MRR). However, subsequent to the reduction of gold prices in the world market, the Central Bank incurred a considerable amount of mark-to-market losses during 2013-2014. In line with the previous Board's decision, the mark-to-market losses were eliminated and profits were paid to the Government. This has resulted in a negative retained earnings position, eroding equity. This situation necessitated the Central Bank to take appropriate actions to safeguard the depletion of equity while staying within the IFRS framework. Improving disclosure notes on the financial statements for distributable profits, while having clear distribution policy addressing the possible unrealized gains/losses scenarios and the required amendment to MLA in line with the current environment, are being considered for implementation by the Central Bank.

Sullivan (2003)[8] identifies the adoption of internationally credible accounting frameworks with the growth of fair value measurement and increased unrealized elements in the profit needed to separate the criteria for measuring profits from those for determining the dividends. It is important for central bank independence that they are able to balance the demands on their dividends and maintain sufficient reserves to cover the risks they face.

6.4 Loans Granted to the Government by Central Bank of Sri Lanka

The Central Bank of Sri Lanka's balance sheet carries assets which are receivable from the Government and a revolving loan facility to the Government, As per IFRS, these assets are considered for impairment. Loans granted to the Government are generally not impaired and consider having recoverability even under IFRS (sovereign debt). Government securities held by the Bank which are used for monetary policy operations are classified as "loans and receivables"

[8] Sullivan, Kenneth Roy, (2003), "Profits, Dividends and Capital - Considerations for Central Banks," Accounting Standards for Central Banks, Central Banking Publications: London.

under IAS 39 and thus valued at amortized cost. Impairing government loans may have other implications such as downgrading the country's credit ratings, loss of investor confidence, etc.

6.5 Gold

The Central Bank holds gold as part of the reserve assets and is engaged in the buying and selling of gold. Some of the gold transactions are backed by allocating physical quantities while, in other transactions, there is no movement in physical gold quantity (paper gold).

Sermon's (2005)[9] study on gold as an investment instrument requires gold to be market to market and unrealized gains/losses taken into income. The IFRS consider paper gold as financial instrument and thus the requirements of IAS 39 apply. Physical gold, which is backed by the movement of the quantity, is classified as non-financial asset but fair valued and resultant gains/losses are taken into income. The majority of the Bank's gold is in physical form.

7. Governance of Accounting Standards Setting in the Central Bank

The adoption of the IAS/IFRS framework was the result of series of remedies recommended by the IMF Safeguard Mission to improve the financial reporting system. After careful consideration of the long-term benefits of adopting the IAS/IFRS in financial reporting, the Bank has adopted the said framework with the approval of the Board.

With that, the Bank follows the requirements of such standards to obtain unqualified audit opinion. The accounting issues were resolved by having a dialogue with the external audit firm which was subcontracted by the Government Auditor (Auditor General) and the Audit Committee as the financial reporting system was overseen by the Audit Committee up to 2012.

8. Why Central Banks Need a Globally Accepted Accounting Framework?

Due to the unique nature of its objectives and the partial non-commercial activities of a central bank, the international accounting standards, which have been created for the commercial entities are not well suited for a central bank. However, central bank specific globally accepted accounting standards, which ensure the achievement of its objectives, have not been developed

[9] Sermon, Chris, (2005), "Accountancy's Golden Puzzle," *Central Banking Journal*, August.

as yet. Therefore, central banks have to apply the IFRS framework to ensure transparency and international best practices of accounting.

Further, the increasing worldwide demand for transparency in financial reporting of central banks triggered by the financial crisis require that both accounting and governance frameworks remain key components when it comes to the understanding of a central bank's financial situation. On the other hand, the "increasing accountability pressures on the public sector have forced government organizations to develop and improve the quality, timeliness and efficiency of their reporting. With globalization, business is now global in nature, particularly in financial services. External and internal audiences need reports and measures that they can compare across institutions and between countries.

Modern reserve management activities of most central banks involve a wide array of financial instruments and dealing with various counterparties including foreign central banks. Therefore, in order to understand the performance of such activities and financial position, a more harmonized treatment in financial reporting is essential.

Financial market development has resulted in markets continually devising new forms of activities that create new risks. This rapid evolution makes demands for increasing disclosures to assess and report such risks.

Central banks as regulators promote the adoption of international reporting standards for financial institutions that it supervises. This reiterates the need for CBSL to adopt a similar reporting requirement to address increasing levels of risks to enhance its credibility as the legislator of those financial institutions. Due to numerous scandals arising from the application of "creative accounting" techniques, stakeholders are much more interested in economic and financial information, especially in considering the implications it has for the establishment of quality comparisons among financial statements.

Since central bank actions are highly sensitive to political situations, financial reporting frameworks need to be transparent, comparable and sufficiently standardized while having the financial independence and room to protect and portray its unique functionality.

International agencies such as the IMF, in particular, are insisting on compliance with international standards as part of their economic programs and assistance to developing countries.

9. Conclusion

A central bank of a country is mandated with national welfare and therefore, its performance cannot be determined solely by the financial results at the end of its financial year. The Central Bank of Sri Lanka, as an apex institution of the country, has the mandate to maximize the productive resource development of the economy, more specifically to achieve economic and price stability as well as financial system stability. This is apart from its prime role as issuer of currency for the country. The Central Bank of Sri Lanka also engages in active reserve management with a profit motive.

These activities of the Central Bank of Sri Lanka would, at times, be reflected in the financial statements as a cost to the Central Bank (i.e., mark-to-market losses in reserve management, currency printing/minting costs, interest costs in open market operations, liquidity absorption exercises, sterilization losses, etc.). Furthermore, a transparent financial statement should fully reflect steps taken during a period of external shock that may necessitate a buffer. Apart from these functions, the disclosure requirements recognized by the IFRS would accommodate the Central Bank's agency functions and related activities.

In this context, the ideal financial management tool should be a very powerful and an effective one, flexible in reflecting the unique functions undertaken by central banks. However, the costs for such a tool could be high. However, if using the tool results in minimizing inflationary impact on the markets, maximizing available resources, improving employment and productivity, improving overall quality of life for the public, the costs would be justified by the end results. As stated above, a central bank is functionally and objectively different from a commercial bank, and therefore, a system such as the IFRS may have limitations supporting the entire gamut of objectives of a central bank. Such limitations could be overcome by giving additional disclosures and establishing necessary buffers before profit distributions.

Globally, central banks need to improve their financial reporting to be harmonized with international best practices on enhancing transparency. In the absence of central bank specific global acceptable financial reporting standards, the IAS/IFRS is an appropriate choice. However, more disclosures are always recommended along with establishing sufficient buffers by way of reserves before distribution of profits in order to withstand any capital erosion.

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