NOTE 19

Realized and unrealized revaluation gains and losses

Business Context

Realized gains and losses are profits or losses arising from completed transactions. Unrealized revaluation gains and losses refer to profits or losses that have occurred more commonly known as 'on paper', but the relevant closing out transactions have not been completed. IFRS provides guidance on how organization shall treat revaluation gains and losses under most circumstances. Nevertheless, the distinction between realized and unrealized gains or losses from foreign currency exchange rate revaluations and monetary gold price revaluations are two common exceptions not specifically addressed under IFRS.

ACCOUNTING POLICY – REALIZED AND UNREALIZED REVALUATION GAINS AND LOSSES

Realized revaluation gains and losses primarily represent amounts realized when assets or liabilities have been derecognised. Realized gain/loss includes transaction costs, which are expensed as incurred. Transaction costs are defined as all costs directly attributable to the completed transaction. Unrealized gain/loss represents changes in fair value for the period for the related balance sheet line item.

For foreign reserve assets and liabilities, foreign currency exchange rate revaluation gains and losses are considered realized when i) the foreign currency is converted to LC for use in LC, ii) when used to settle a third-party foreign currency obligation, whether for the Bank or on behalf of the Government of Utopia.

Monetary gold price revaluations, and revaluations for financial assets at FVPL are considered realized when the gold or financial instrument is sold.

Statement of Judgements and Estimates

Gains and losses on financial instruments are due to changes in the price of the instrument (before foreign exchange gains and losses) and changes in foreign currency exchange rates (foreign exchange gains and losses). These are presented separately in the income statement. The method for allocating total gains and losses in LC to a security element and a foreign exchange rate revaluation element is described below. Different methods will result in different estimates. (NB)

i) Foreign exchange element

Unrealised gains or losses due to changes in foreign exchange rates are calculated based on the weighted average original cost of the holding in local currency and the change in the foreign currency exchange rate from the time of purchase until the balance sheet date. If the holding has been purchased in a previous period, gains and losses recognised in the income statement in previous periods are deducted to arrive at the gain or loss for the current period. For realised gains or losses, the weighted average historical costs and the foreign exchange rate on the date of sale is used for calculating realised gains or losses, and previously recognized unrealised gains or losses for the holding are reversed in the current period. (NB) *ii) Security element*

Unrealised gains or losses from changes in the security, derivative, or monetary gold price are calculated based on the change in the instrument's price from the purchase date to the balance sheet date and the closing exchange rate at the balance sheet date. If the holding was acquired in a previous period, gains and losses recognized in the income statement in previous periods are deducted to arrive at the gain or loss from security prices for the current period. When the holding is sold, the holding's selling price is used for calculating realised gains or losses, and previously recognized unrealized gains or losses for the holding are reversed in the current period. (NB)

DISCLOSURE – REALIZED AND UNREALIZED REVALUATION GAINS AND LOSSES

The Bank manages the foreign reserves for Utopia; which comprise foreign currency financial instruments and monetary gold. Foreign reserve assets are subject to foreign currency exchange rate and price revaluations. Revaluation gains and losses are considered unrealized until the underlying position is derecognized.

User Guidance

Whether as a separate note disclosure or included in other notes, the central bank should be transparent on how it assesses whether a foreign currency exchange rate or monetary gold price revaluation is realized or not. These amounts can be quite material for many central banks and can draw significant interest of politicians and the public; often calling for the release (e.g. distribution) of the unrealized portions.

The distribution of these unrealized revaluations gains effectively monetizes the amount in local currency while the underlying foreign currency remains open. If the exchange rate or prices then revert, the central bank will be exposed to negative equity, weakening its credibility as a financial sector backstop.

See also CBSL; MMA