Box 2: Simplification of the Sanctioning Framework for Monetary and Foreign Exchange Operations[1]

Introduction

After conducting a comprehensive review of the sanctioning regimes applicable to foreign exchange and monetary operations, *Banco de la República (BanRep)* introduced a new framework of consequences for addressing non-compliance within the context of open market operations (OMOs), liquidity operations aimed at ensuring the normal functioning of the payment system, and foreign exchange intervention operations. In this context, in August 2025, the Auction System Regulations (the System) were published. The system is administered by *BanRep* through the Office for Monetary Operations and International Investments (SGMII in Spanish) and applies both to the Bank as the administrator and to the Participating Entities.

The new regime aims to simplify the framework of pecuniary consequences and preserve the incentives for compliance in operations with *BanRep*. At the same time, it seeks to promote discipline in the markets by encouraging orderly and transparent behavior that prevents sanctions and mitigates reputational or financial risks for participating entities.

Pecuniary consequences remain proportional to the risks and are based on the principle of indifference, according to which sanctions must ensure that the benefits of compliance outweigh the potential gains from non-compliance. This approach is adapted to the severity of the breach and to the associated risks related to market efficiency, as well as operational and legal risks.

On the other hand, this framework operates within the applicable legal framework, which remains robust and continues to provide regulatory certainty in advance to the participating entities, by clearly describing the sanctionable conducts and the corresponding consequences.

In addition, the new framework incorporates the recommendations made by the International Monetary Fund (IMF) formulated during its most recent technical assistance mission[2]. After holding meetings with various financial institutions and evaluating *BanRep's* regulations on foreign exchange intervention operations, the IMF recommended streamlining (progressive fines) and simplifying the sanctioning structure, considering that excessive penalties may create distortions in incentives, thereby discouraging both market development and the implementation of appropriate risk-management policies by entities.

The implementation of the new framework and the entry into force of the Auction System Regulations required adjustments to several resolutions and external circulars issued by *BanRep*, including External Resolution (ER) 01 of 2018, ER 02 of 2019, ER 05 of 2022, as well as External

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[2] Technical Assistance Report- Colombia – FX Market Development and Regulatory Framework Review. December 2024. By: Istvan Mak, Meryem Rhouzlane, and Paulo Muniz (external expert).

Regulatory Circulars (ERC) DEFI-354, DOAM-143, DOAM-141, DOAM-148, and DGOF-481.

Additionally, the new sanctioning framework included the development of standard adhesion contracts to formalize contractual relationships between *BanRep* and the OMOs Placement Agents (OPAs) or the Foreign Exchange Market Intermediaries (**FXIs**).

This box presents the main modifications introduced to the sanctioning framework of *BanRep's* monetary and foreign exchange operations. Its content is for informational purposes only and does not replace or constitute part of the current regulations.

Monetary Operations

Pecuniary consequences on monetary operations apply to defaults in OMOs and to operations aimed at facilitating the normal functioning of the payment system carried out by OPAs. OMOs include expansionary and contractionary operations, both outright and temporary, as well as TES Non-Delivery Forward contract operations (NDFs)[3]. In turn, operations aimed at facilitating the normal functioning of the payment system include overnight repos resulting from the conversion of intraday repos and overnight repos for clearing purposes. All these operations are included in ER 05 of 2022 issued by the Board of Directors of *Banco de la República* (BDBR). The scheme applies exclusively to operations conducted by OPAs.

The new pecuniary consequences framework for monetary operations contemplates four types of non-compliance or delays[4]**:** *i)* non-compliance of an offer and execution of the initial operation*, ii)* non-compliance with margin calls and/or substitution of securities, *iii)* delay at maturity, and *iv)* default at maturity. These apply to monetary operations, except for TES NDFs contract operations, which are only subject to late payment interests as described below.

The new framework unified the deadline for the payment of pecuniary consequences and standardized the treatment applicable to repo operations with promissory notes. Previously, there were different rules depending on the type of operation, and some pecuniary consequences were not applicable to repo operations with promissory notes. Under the new regime, it is established that pecuniary consequences must be paid before the closing of the CUD funds transfer service on the business day following the declaration of the delay or default. Likewise, the framework presented applies uniformly to all monetary operations, including repo operations with promissory notes.

The new framework introduced the concept of a minimum economic consequence and late payment interests for delays in the payment of pecuniary consequences or outstanding balances. For all types of default or delay, a minimum pecuniary consequence equivalent to 28 Tax Value Units (UVT in Spanish) was established. Additionally, starting from the business day following the default of the transaction or the payment of the pecuniary consequence, late payment interests will accrue at

[3] TES Non-Delivery Forwards contract operations (NDFs) are derivative instruments through which the parties commit to buy or sell, at a future date, Colombian government debt securities denominated in local currency (TES) at a price agreed upon on the contract's negotiation date. These contracts are generally executed between a local counterparty and a foreign counterparty. Most of the local counterparties in these operations are part of the commercial banking group. For more information, see Box 1 of the Financial Markets Report for the first quarter of 2025.

[4] The conditions under which defaults or delays occur, and the instructions for calculating the pecuniary consequence in each case, are set forth in Table 2 of Section 16.1 of the Auction System Regulations.

the maximum legally permitted rate, equivalent to Current Banking Interest Rate (IBC in Spanish)[5]× 1.5 per day of delay on the amount owed to *BanRep*, both for pecuniary consequences and the outstanding balance of the obligation (principal and interest), as stablished in *BanRep's* External Regulatory Circulars. These late payment interests also apply to defaults in TES NDFs contract operations.

Operational procedures were also defined to clarify the collection process and the return of surpluses. In particular, the procedures detail: *i)* the collection process for matured operations and for pecuniary consequences, which consolidates the rules and schedules for executing a series of debit attempts by *BanRep* to carry out such collections, and *ii*) the return of surpluses in cases of default, specifying the timeframe and conditions under which such surpluses must be returned to the rightful party.

The framework also incorporates non-pecuniary consequences applicable to certain types of non-compliances. These include reporting to the Financial Superintendency of Colombia (SFC in Spanish) in cases of delay or default at maturity of monetary operations, as well as for non-compliance in the payment of pecuniary consequences. Additionally, the System may report these breaches to the Securities Market Self-Regulator (AMV in Spanish). Finally, it was established that if an entity defaults on a transaction at maturity, it will lose its OPA status and be suspended from carrying out foreign exchange intervention operations, as indicated in ER 01 of 2018[6].

Foreign Exchange Operations

The pecuniary consequences of foreign exchange operations apply to defaults in the foreign exchange intervention transactions carried out by *BanRep*, in accordance with the provisions of BDBR ER 01 of 2018 and CRE DOAM-143. *Banrep* may intervene in the foreign exchange market through: *i)* the purchase or sale of foreign currency at market rates; *ii)* the sale of put or call options at market rates, through an auction mechanism; *iii)* the sale of spot foreign currency through FX swap contracts, at rates set by *BanRep*, using either auction or window mechanisms; and *iv)* the sale of foreign currency through non-deliverable forward (NDF) contracts at market rates, through the auction mechanism.

The pecuniary consequences framework for foreign exchange operations includes three types of breaches or delays[7]: *i)* delay in the settlement of the operation; *ii)* default on payments that must be made at the start of the operation (on the auction or window date); and *iii)* default on payments that must be made at the maturity of the operation.

The pecuniary consequences for delayed settlements were modified to incorporate the cost equivalent to the return foregone by *BanRep's* funds in foreign accounts, plus an additional premium intended to encourage timely fulfillment of obligations. Consequently, the delayed fulfillment window schedule

[5] Current Banking Interest in the consumption and ordinary modality effective on the day of default and published by the Financial Superintendency of Colombia.

[6] The new scheme maintains the previous rule that the OPA status is also lost if the payment of pecuniary consequences is not made, or if definitive operations under TES NDF contracts are not fulfilled.

[7] The conditions under which defaults or delays occur, and the instructions for calculating the pecuniary consequence in each case, are set forth in Table 3 of Section 16.2 of the Auction System Regulations.

was adjusted, taking into account the time required for transferring resources to foreign accounts.[8] Specifically, the delay window was set between 2:30 p.m. and 3:30 p.m. for all instruments, except for NDF operations, for which the schedule was established between 11:00 a.m. and 11:30 a.m., in order to align the timing with the settlement of monetary operations.

On the other hand, the amount of pecuniary consequences applicable to breaches in submitted offers was reduced. In NDF operations, the charge was lowered from 2.0% to 1.5%, and for other foreign exchange intervention operations, from 5.0% to 3.0%. This new framework incorporates potential daily variations in the exchange rate and maintains an appropriate balance between the effectiveness of incentives for operation compliance and the proportionality of pecuniary consequences, providing *BanRep* with a sufficient level of certainty regarding the execution of operations.

Finally, the new framework extends the application of behavioral consequences to errors occurring in the auctions of all foreign exchange intervention instruments. These consequences are determined based on the number of errors accumulated over a twelve-month (12) period in the auctions. This measure aims to encourage greater operational discipline and promote the adoption of internal controls and verification mechanisms that reduce the likelihood of errors, for example, in the placement of bids, which could cause distortions in the determination of the cut-off rate and affect the efficiency of operations with *BanRep.*

Conclusion

In summary, *BanRep* implemented a new sanctionatory framework for monetary and foreign exchange operations, with the purpose of simplifying the rules applicable to breaches and maintaining clear incentives for financial institutions to comply. This regime promotes discipline and transparency in the markets by establishing economic and non-economic consequences for non-compliance, such as minimum fines, late payment interests, and operational restrictions.

The new framework is also aligned with IMF recommendations, updates operational and regulatory procedures, and strengthens consistency across different types of operations managed by *BanRep.* This aims to ensure that entities act responsibly and efficiently, thereby contributing to the stability and proper functioning of the Colombian financial system.

[8] The schedules for foreign exchange operations are detailed in Section 15.1.2.2 of the Auction System Regulations.