



CENTRAL BANK OF SOLOMON ISLANDS

**ANNUAL STATEMENT OF ACCOUNTS
FOR THE YEAR ENDED 31 DECEMBER 2013**

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Central Bank of the Solomon Islands

Directors' report

The Directors present their report together with the financial statements of the Central Bank of the Solomon Islands ("the Bank") for the year ended 31 December 2013 and the auditors' report thereon.

Directors

The Directors in office during the financial year and at the date of this report were:

Denton Rarawa (Chairman and Governor)
Gane Simbe
Shardrach Fanega
Katululu Maepioh
Loyley Ngira
Lily Lomulo
Tele Bartlett (appointed 17 July 2013)
Primo Afeau (appointed 17 July 2013)
John Usuramo (appointed 18 December 2013)
Dr. Steve Aumanu (resigned 2 December 2013)
Leslie Teama (resigned 3 March 2013)

State of affairs

In the opinion of the Directors:

- there were no significant changes in the state of affairs of the Bank during the financial year under review not otherwise disclosed in this report or the financial statements;
- the accompanying statement of financial position gives a true and fair view of the state of affairs of the Bank as at 31 December 2013 and the accompanying statement of comprehensive income, statement of changes in equity and statement of cash flows give a true and fair view of the results, changes in equity and cash flows of the Bank for the year then ended.

Principal activities

The Bank's role as a central bank, as defined in the Central Bank of Solomon Islands Act, 2012 is:

- (a) to achieve and to maintain domestic price stability;
- (b) to foster and to maintain a stable financial system;
- (c) to support the general economic policies of the government.

Trading results

The net loss of the Bank for the year ended 31 December 2013 was \$165.10m (2012: net profit of \$71.35m).

Reserves

The Board approved the following transfers of reserves in the statement of comprehensive income during the year:

- \$0.61m (2012: \$5.68m) to the asset revaluation reserve;
- (\$150.55m) (2012: \$67.35m) to the foreign exchange assets revaluation reserve;
- (\$15.17m) (2012: (\$1,688m)) to the general reserve.

Provisions

There were no material movements in provisions during the year apart from the normal amounts set aside for such items as doubtful debts, depreciation and employee entitlements.

Central Bank of the Solomon Islands

Directors' report

Assets

The Directors took reasonable steps before the Bank's financial statements were made out to ascertain that the assets of the Bank were shown in the accounting records at a value equal to or below the value that would be expected to be realised in the ordinary course of business.

At the date of this report, the Directors were not aware of any circumstances which would render the values attributable to the assets in the financial statements misleading.

Directors' benefit

No director of the Bank has, since the last financial year, received or become entitled to receive a benefit (other than a benefit included in the total amount of emoluments received or due and receivable by directors shown in the Bank's financial statements) by reason of a contract made with the Bank or a related corporation with the director or with a firm of which he is a member, or in a Bank in which he has a substantial financial interest.

Events subsequent to balance date

There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Bank, to affect significantly the operations of the Bank, the results of those operations, or the state of affairs of the Bank, in future financial years.

Other circumstances

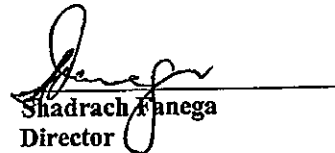
At the date of this report, the Directors are not aware of any circumstances not otherwise dealt with in this report or financial statements which render amounts stated in the financial statements misleading.

Dated at Honiara this 27th of May 2014.

Signed in accordance with a resolution of the Board of Directors:



Denton Rarawa
Chairman of the Board and Governor


Shadrach Tanega
Director

Central Bank of Solomon Islands

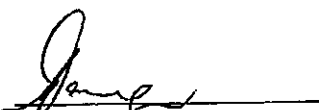
Statement by Directors

In the opinion of the Directors:

- (a) the accompanying statement of comprehensive income is drawn up so as to give a true and fair view of the results of the Bank for the year ended 31 December 2013;
- (b) the accompanying statement of changes in equity is drawn up so as to give a true and fair view of the changes in equity of the Bank for the year ended 31 December 2013;
- (c) the accompanying statement of financial position is drawn up so as to give a true and fair view of the state of affairs of the Bank as at 31 December 2013;
- (d) the accompanying statement of cash flows is drawn up so as to give a true and fair view of the cash flows of the Bank for the year ended 31 December 2013;
- (e) at the date of this statement there are reasonable grounds to believe the Bank will be able to pay its debts as and when they fall due;
- (f) all related party transactions have been adequately recorded in the books of the Bank, and
- (g) the financial statements have been properly prepared in accordance with International Financial Reporting Standards ("IFRS").

For and on behalf of the Board of Directors by authority of a resolution of the Directors this.....^{27th} of May 2014.


Denton Rarawa
Chairman of the Board and Governor


Shadrach Fanega
Director



Independent auditor's report to the Board of the Central Bank of Solomon Islands

Report on the Financial Statements

I have in joint consultation with the Board of the Bank pursuant to Section 60(1) of the *Central Bank of Solomon Islands Act 2012* contracted KPMG Fiji which is part of the KPMG International network to assist me to audit the accompanying financial statements of the Central Bank of Solomon Islands, which comprise the statement of financial position as at 31 December 2013, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and Notes 1 to 27 comprising of a summary of significant accounting policies and information.

Board's and Management's Responsibility for the Financial Statements

The Board and Management are responsible for the preparation of financial statements that give a true and fair view in accordance with the requirements of the *Central Bank of Solomon Islands Act 2012* and International Financial Reporting Standards and for such internal control as the Board and Management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. The audit has been conducted in accordance with International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for Qualified Opinion

Currency in circulation

As at 31 December 2013, currency in circulation is recorded in the financial statements at \$617.57m.

I was unable to obtain sufficient appropriate audit evidence regarding the completeness, existence and accuracy of this balance at year end as the movements of this account cannot be reconciled to the closing balance as at 31 December 2013. Accordingly, I am not able to ascertain what adjustments, if any, might be necessary to the amounts recorded in the financial statements.

Currency Inventory

Prior to 1 January 2013 currency inventory comprising notes and coins that were purchased and not yet circulated were expensed to profit and loss when purchased or received in accordance with the Bank's accounting policy. Section 57(3) of the *Central Bank of Solomon Islands Act, 2012* which became effective 1 January 2013, now requires that all notes and coins purchased and not circulated be accounted for as inventory and expensed to profit or loss when it is issued into circulation.

I could not obtain sufficient appropriate audit evidence over the existence and accuracy of the restated currency inventory as at 31 December 2012 following the change in the Bank's accounting policy and given that the balance of currency in circulation cannot be substantiated as at 31 December 2013, I am unable to apply alternative audit procedures to verify the balance of currency inventory as at 1 January 2013.

.Qualified Opinion

In my opinion, except for the effect if any, of the matters described in the Basis for Qualified Opinion paragraphs above, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2013 and of its financial performance, changes in equity and cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

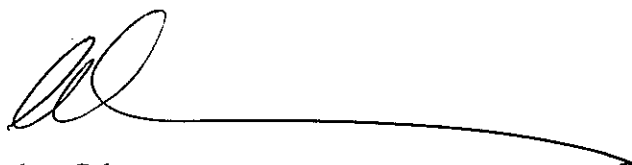
As at 31 December 2013, the Bank's total assets amounted to \$4.30 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which totalled \$4.34 billion.

Under Section 56 of the *Central Bank of Solomon Islands Act 2012*, the Bank will be required to inform the Minister for Finance within 30 days of this report of the reasons for this shortfall and request a capital contribution to remedy the shortfall.

Report on Other Legal and Regulatory Requirements

International auditing standards require the auditor to report on certain other matters which may arise in relation to compliance with legal and regulatory requirements applicable to the Central Bank of Solomon Islands.

I draw attention to the fact that the Bank has not complied with Section 58 of the *Central Bank of Solomon Islands Act 2012* which requires audited financial statements and the auditor's report thereon to be presented to the Minister for Finance within four months of the end of the financial year. The management signed financial statements were not presented to me until today. The Bank did inform the Minister for Finance prior to the due date that it expected the audited statements to be delayed.



Robert Cohen
Acting Auditor-General

27 May, 2014

Office of the Auditor-General
Honiara, Solomon Islands

Central Bank of Solomon Islands
Statement of comprehensive income
For the year ended 31 December 2013

| | Note | 2013 \$000 | Restated 2012 \$000 |
|--|------|------------------|---------------------------|
| Income | | | |
| Interest income | 4(a) | 41,737 | 59,790 |
| Fees and commission income | 4(b) | 8,958 | 9,771 |
| Other income | 4(c) | 2,738 | 3,265 |
| Change in fair value of investment properties | 10 | 612 | 5,682 |
| Net unrealized foreign exchange revaluation gain | | <u>-</u> | <u>67,353</u> |
| Total income | | <u>54,045</u> | <u>145,861</u> |
| Expenses | | | |
| Interest expense | 4(d) | 7,149 | 9,531 |
| Fees and commission expense | | 1,047 | 540 |
| Administration expenses | 4(e) | 32,579 | 32,549 |
| Other expenses | 4(f) | 27,823 | 31,894 |
| Net unrealized foreign exchange revaluation loss | | <u>150,548</u> | <u>-</u> |
| Total expenses | | <u>219,146</u> | <u>74,514</u> |
| Net operating (loss)/profit | | <u>(165,101)</u> | <u>71,347</u> |
| Other comprehensive losses | | | |
| Net change in fair value (available - for - sale financial assets) | | (77,935) | (3,248) |
| Net change in revaluation (property, plant and equipment) | | <u>-</u> | <u>29,125</u> |
| Total other comprehensive (loss)/income | | <u>(77,935)</u> | <u>25,877</u> |
| Total comprehensive (loss)/ income | | <u>(243,036)</u> | <u>97,224</u> |

This statement of comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

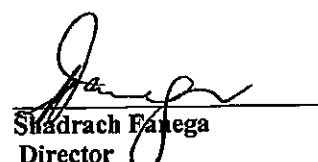
Central Bank of Solomon Islands
Statement of financial position
As at 31 December 2013

| | Note | 2013 \$000 | Restated 2012 \$000 | Restated 1 January 2012 \$000 |
|---|-------|------------------|---------------------------|--|
| Foreign currency assets | | | | |
| Cash at bank | 20 | 732,680 | 764,448 | 1,031,645 |
| Accrued interest | | 9,167 | 9,593 | 9,924 |
| Held-to-maturity investments | 5 | 2,753,823 | 2,555,104 | 1,879,953 |
| Available-for-sale investments | 6 | 213,073 | 217,502 | - |
| International Monetary Fund | 7 | 217,009 | 216,765 | 252,449 |
| Total foreign currency assets | | 3,925,752 | 3,763,412 | 3,173,971 |
| Local currency assets | | | | |
| Cash on hand | 20 | 300 | 456 | 98 |
| Loans and advances | 8 | 81,278 | 87,174 | 107,828 |
| Currency inventory | 9 | 39,859 | 39,380 | 31,110 |
| Investment properties | 10 | 11,935 | 11,323 | - |
| Property, plant and equipment | 12 | 138,140 | 134,675 | 97,538 |
| Other assets | 11 | 98,529 | 46,192 | 47,550 |
| Total local currency assets | | 370,041 | 319,200 | 284,124 |
| Total assets | | 4,295,793 | 4,082,612 | 3,458,095 |
| Foreign currency liabilities | | | | |
| International Monetary Fund | 7 | 356,595 | 354,561 | 414,056 |
| Demand deposits | 13(a) | 43,890 | 86,103 | 11,331 |
| Total foreign currency liabilities | | 400,485 | 440,664 | 425,387 |
| Local currency liabilities | | | | |
| Demand deposits | 13(b) | 2,601,955 | 2,361,956 | 2,047,933 |
| Currency in circulation | 14 | 617,570 | 599,669 | 527,702 |
| Fixed deposits | 15 | 611,932 | 367,888 | 239,763 |
| SIG monetary operations account | 16 | 33,604 | 38,387 | 43,271 |
| Employee entitlements | 17 | 11,009 | 9,368 | 9,078 |
| Other liabilities | 18 | 9,402 | 11,808 | 9,313 |
| Total local liabilities | | 3,885,472 | 3,389,076 | 2,877,060 |
| Total liabilities | | 4,285,957 | 3,829,740 | 3,302,447 |
| Net assets | | 9,836 | 252,872 | 155,648 |
| Capital and reserves | | | | |
| Paid up capital | 21 | 50,000 | 20,000 | 20,000 |
| General reserve | 22(a) | 37,869 | 83,034 | 84,722 |
| Foreign exchange revaluation reserve | 22(b) | (145,572) | 4,976 | (62,377) |
| Premises and equipment assets revaluation reserve | 22(c) | 86,847 | 86,235 | 51,428 |
| Gold revaluation reserve | 22(d) | (81,183) | (3,248) | - |
| Capital asset reserve | 22(e) | 61,875 | 61,875 | 61,875 |
| Total capital and reserves | | 9,836 | 252,872 | 155,648 |

Signed in accordance with the resolution of the Board of Directors:



Denton Rarawa
Chairman of the Board and Governor



Shadrach Fanega
Director

The statement of financial position is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

Central Bank of Solomon Islands
Statement of changes in equity
For the year ended 31 December 2013

| | Issued & paid up capital \$000 | Gold revaluation reserve \$000 | General reserve \$000 | Foreign exchange assets revaluation reserve \$000 | Asset revaluation reserve \$000 | Capital assets reserve \$000 | Total \$000 |
|---|---|---|-----------------------------|--|--|---------------------------------------|----------------|
| Balance as at 1 January 2012 | 20,000 | - | 58,707 | (51,002) | 51,428 | 61,877 | 141,010 |
| Impact of change in accounting policy (Note 2(e)) | - | - | 31,110 | - | - | - | 31,110 |
| Impact of prior period errors (Note 2(f) & (g)) | - | - | (5,095) | (11,375) | - | (2) | (16,472) |
| Restated balance as at 1 January 2012 | 20,000 | - | 84,722 | (62,377) | 51,428 | 61,875 | 155,648 |
| Total comprehensive income for the year | | | | | | | |
| Profit (loss) for the year (Note 19) | - | - | (1,688) | 67,353 | 5,682 | - | 71,347 |
| <u>Other comprehensive income/(losses)</u> | | | | | | | |
| Fair value gains – gold | - | (3,248) | - | - | - | - | (3,248) |
| Gains on revaluation | - | - | - | - | 29,125 | - | 29,125 |
| <u>Total other comprehensive income/(losses)</u> | - | (3,248) | - | - | 29,125 | - | 25,877 |
| Total comprehensive income/(losses) | - | (3,248) | (1,688) | 67,353 | 34,807 | - | 97,224 |
| | 20,000 | (3,248) | 83,034 | 4,976 | 86,235 | 61,875 | 252,872 |
| <u>Transaction with owners, recorded directly in equity</u> | - | - | - | - | - | - | - |
| Restated balance as at 31 December 2012 | 20,000 | (3,248) | 83,034 | 4,976 | 86,235 | 61,875 | 252,872 |
| Balance at 1 January 2013 | 20,000 | (3,248) | 83,034 | 4,976 | 86,235 | 61,875 | 252,872 |
| Total comprehensive income for the year | | | | | | | |
| Profit (loss) for the year (Note 19) | - | - | (15,165) | (150,548) | 612 | - | (165,101) |
| <u>Other comprehensive income/(losses)</u> | | | | | | | |
| Fair value losses – gold | - | (77,935) | - | - | - | - | (77,935) |
| <u>Total other comprehensive income/(losses)</u> | - | (77,935) | - | - | - | - | (77,935) |
| Total comprehensive income/(losses) | - | (77,935) | (15,165) | (150,548) | 612 | - | (243,036) |
| | 20,000 | (81,183) | 67,869 | (145,572) | 86,847 | 61,875 | 9,836 |
| <u>Transaction with owners, recorded directly in equity</u> | | | | | | | |
| Equity contribution | 30,000 | - | (30,000) | - | - | - | - |
| Balance as at 31 December 2013 | 50,000 | (81,183) | 37,869 | (145,572) | 86,847 | 61,875 | 9,836 |

The statement of changes in equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

Central Bank of Solomon Islands
Statement of cash flows
For the year ended 31 December 2013

| | Note | 2013 \$000 | Restated 2012 \$000 |
|---|------|------------------|---------------------------|
| Operating activities | | | |
| Interest received | | 42,160 | 60,122 |
| Cash received from other income | | 11,515 | 12,901 |
| Interest paid | | (2,625) | (5,008) |
| Cash paid to suppliers and employees | | (54,791) | (60,709) |
| Net movement in held to maturity investments | 5 | (198,719) | (675,151) |
| Net movement in International Monetary Fund accounts | 7 | 3 | (1,778) |
| Net movement in other receivables | | (52,335) | (6,431) |
| Net movement in other payables | | 7,497 | 7,809 |
| Cash flows (used in) operating activities | | <u>(247,295)</u> | <u>(668,245)</u> |
| Investing activities | | | |
| Acquisition of property, plant and equipment | 12 | (10,720) | (18,360) |
| Proceeds from sale of premises, plant and equipment | | 181 | 368 |
| Net movement in available-for-sale investments | | (74,096) | (220,750) |
| Net movement in loan to government | | 7,214 | 21,161 |
| Net movement in loans and advances to staff | | (1,318) | (507) |
| Cash flows (used in) investing activities | | <u>(78,739)</u> | <u>(218,088)</u> |
| Financing activities | | | |
| Net movement in currency in circulation | | 10,634 | 66,724 |
| Net movement in demand deposits | | 36,406 | 306,426 |
| Net movement in fixed deposits received | | 400,613 | 200,665 |
| Solomon Islands government monetary operations | | (4,782) | 359 |
| Net movement in International Monetary Fund credit facilities | 7 | 1,786 | (22,033) |
| Cash flows from financing activities | | <u>444,657</u> | <u>552,141</u> |
| Net effect of exchange rates | | <u>(150,548)</u> | <u>67,353</u> |
| Net decrease in cash | | <u>(31,925)</u> | <u>(266,839)</u> |
| Cash at the beginning of the financial year | | <u>764,904</u> | <u>1,031,743</u> |
| Cash and cash equivalents of the financial year | 20 | <u>732,980</u> | <u>764,904</u> |

The statement of cash flows is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

1. Principal activities and principal place of operations

The Central Bank of Solomon Islands ("the Bank") operates under the Central Bank of Solomon Islands Act, 2012. The Bank is an independent legal entity wholly owned by, and reporting to, the Government of the Solomon Islands. The Bank's primary objective as defined in the Central Bank of Solomon Islands Act, 2012, Section 8 is:

- (a) to achieve and to maintain domestic price stability;
- (b) to foster and to maintain a stable financial system;
- (c) to support the general economic policies of the government.

The Bank's principal place of operations is located at Mud Alley Street, Honiara, Solomon Islands.

2. Basis of preparation

(a) Statement of compliance

The financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards ('IFRS') and the Central Bank of Solomon Islands Act, 2012, except where the Central Bank of Solomon Islands Act, 2012 requires different treatment in which case the Central Bank of Solomon Islands Act, 2012 takes precedence.

As at 31 December 2013, the Bank's total assets amounted to \$4.30 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which totalled \$4.34 billion.

Section 56 of the Central Bank of Solomon Islands Act 2012 requires that in the event the total assets of the Bank falls below the sum of the Bank's monetary liabilities and its unimpaired authorized capital, the Bank will be required to inform the Minister for Finance of the reasons for this shortfall and request a capital contribution to remedy the shortfall within 30 days of this report.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis and do not take into account changes in money values except for the following material items in the statement of financial position.

- Available-for-sale financial assets are measured at fair value.
- Held to maturity financial assets are measured at amortised cost.
- Land and Buildings classified as Property, plant and equipment are measured at fair value.
- Investment properties are measured at fair value.

(c) Functional and presentation currency

The financial statements are presented in Solomon Islands Dollars, which is the Bank's functional currency. All financial information presented in Solomon Islands Dollars has been rounded to the nearest thousand except when otherwise indicated.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

2. Basis of preparation (continued)

(d) Use of estimates and judgement

The preparation of the financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revision to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

The estimates and assumptions that have a significant risk of causing material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed in the following paragraphs;

Impairment of financial assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Bank on terms that the Bank would not consider otherwise, indications that a debtor or issuer will enter into bankruptcy, adverse changes in the payment status of borrowers or issuers in the Bank, economic conditions that correlate with defaults or the disappearance of an active market for a security.

(e) Changes in accounting policy

During the financial year, the Directors resolved to change the accounting policies previously adopted for the accounting of the following:

New notes and coins purchased and yet to be circulated

Prior to 1 January 2013 notes and coins were expensed when purchased or received. The directors resolved that in accordance with the gazette of the Central Bank of Solomon Islands Act., 2012, which became effective 1 January 2013, all notes and coins purchased and not circulated will be accounted for as inventory and expensed to profit or loss when issued into circulation.

The effect of the changes in accounting policy on new notes and coins is stated below:

| | Currency inventory \$000 | General reserve \$000 |
|---|---|--------------------------------------|
| Balance as at 1 January 2012, as previously reported | - | 58,707 |
| Impact of the change in accounting policy | 31,110 | 31,110 |
| Restated balance at 1 January 2012 | <u>31,110</u> | <u>89,817*</u> |
| Balance as at 31 December 2012, as previously reported | - | 58,707 |
| Impact of the change in accounting policy at 1 January 2012 | 31,110 | 31,110 |
| Impact of the change in accounting policy | 8,270 | 8,270 |
| Restated balance at 31 December 2012 | <u>39,380</u> | <u>98,087*</u> |

*General reserve balance had there been no prior period errors

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

2. Basis of preparation (continued)

(e) Change in accounting policy (continued)

Gold bullion

The Bank purchased gold bullion in 2012 and treated it as a commodity for accounting purposes recording it in the Bank's financial statements as at 31 December 2012 at cost.

The Bank's intention at the outset was always to hold gold bullion as part of its foreign reserve management. Accordingly, the gold Bullion should be treated as a financial asset and recorded as available-for sale in the Bank's financial statements.

The CBSI Board notes that the previous treatment of gold bullion does not reflect the Bank's intention and resolved to treat gold bullion as a financial asset and record it as available-for sale in the Bank's financial statements effective 31 December 2013.

The effect of the changes in accounting policy on gold bullion is stated below:

| | Available for sale investments \$000 | Gold revaluation reserve \$000 |
|--|---|---|
| Balance as at 31 December 2012, as previously reported | 218,628 | (2,122) |
| Impact of the change in accounting policy | (1,126) | (1,126) |
| Restated balance at 31 December 2012 | <u>217,502</u> | <u>(3,248)</u> |

(f) Prior period error

During the financial year, the following material prior period errors were identified and prior period comparatives were restated. The effect of the restatement on the financial statements is summarized below:

i) International Monetary Fund (IMF)

All IMF asset and liability accounts were not brought to account in the Bank's financial statements. For accounts that were recorded in the financial statements, incorrect exchange rates were used in determining the Solomon Island dollar equivalent as at reporting date.

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|--|----------------------------|----------------------------|
| <i>Increase/ (decrease) in profit</i> | | |
| (Decrease)/increase in net unrealized foreign revaluation gains | <u>23,519</u> | <u>(19,383)</u> |
| <i>Increase/(decrease) in net assets</i> | | |
| Increase in Reserve tranche position | (1,043) | 374 |
| Increase in Currency subscription | (17,314) | 6,705 |
| (Decrease)/ increase in Special drawing rights | (18,673) | 16,014 |
| (Increase) in Securities account | 18,673 | (6,705) |
| Decrease/ (increase) in Stand by credit facility | 23,346 | (18,631) |
| Decrease/ (increase) in Special drawing rights allocation | 18,480 | (17,140) |
| Decrease/ (increase) in Extended credit facility | 50 | - |
| (Increase)/decrease in equity (Foreign currency translation reserve) | <u>23,519</u> | <u>(19,383)</u> |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

2. Basis of preparation (continued)

(f) Prior period error (continued)

ii) Early retirement benefit

Early retirement benefit in the previous reported financial years was not in accordance with IAS 19 "Employee benefits".

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|---|----------------------------|----------------------------|
| <i>Increase/(decrease) in profit</i> | | |
| (Increase) in staff cost | <u>(1,052)</u> | <u>(2,342)</u> |
| <i>Increase/(decrease) in net assets</i> | | |
| (Increase) in provision for employee entitlements | <u>(1,052)</u> | <u>(2,342)</u> |

iii) Interest on government deposits

Interest of 1.25%, payable on the SIG consolidated account has not been accrued or paid since the account was opened in 2010.

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|--|----------------------------|----------------------------|
| <i>Increase/(decrease) in profit</i> | | |
| (Increase) in interest expense | <u>(1,754)</u> | <u>(986)</u> |
| <i>Increase/(decrease) in net assets</i> | | |
| (Increase) in Solomon Islands Government demand deposits | <u>(1,754)</u> | <u>(986)</u> |

iv) Foreign currency assets - Bonds

The Bank's holding of financial instruments in bonds were not accounted for in accordance with IAS 39 "Financial Instruments: Recognition and Measurement". This resulted in the Bank's interest revenue and assets been overstated in reported prior period financial results.

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|---|----------------------------|----------------------------|
| <i>Increase/(decrease) on profit</i> | | |
| (Decrease) in interest revenue | <u>(4,341)</u> | <u>(1,275)</u> |
| <i>Increase/(decrease) in net assets</i> | | |
| (Decrease) in Foreign currency assets – bonds | <u>(4,341)</u> | <u>(1,275)</u> |

iv) Numismatic coins

Numismatic coins purchased in the financial period ended 31 December 2012 was incorrectly recorded in the 31 December 2013 financial period.

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|--------------------------------------|----------------------------|----------------------------|
| <i>Increase/(decrease) in profit</i> | | |
| (Increase) in currency expenses | <u>(1,990)</u> | <u>-</u> |
| <i>Increase/(decrease) in equity</i> | | |
| (Decrease) in other liabilities | <u>(1,990)</u> | <u>-</u> |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

2. Statement of significant accounting policies (continued)

(f) Prior period error (continued)

v) Other

Property, plant and equipment - Depreciation for certain property, plant and equipment had not been calculated and this resulted in no depreciation recorded for these assets in the reported prior financial periods.

Accruals and prepayments - It was identified that accrual and prepayment of expenses were not properly accounted for and reported in prior period financial statements. This had the following impact:

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|---|----------------------------|----------------------------|
| <i>Increase/ (decrease) in profit</i> | | |
| (Increase) in depreciation expense | (534) | (1,343) |
| Decrease in interest expense | - | 855 |
| Decrease in repairs and maintenance expense | 446 | - |
| | <u>(88)</u> | <u>(488)</u> |
| <i>Increase/(decrease) in equity</i> | | |
| (Decrease) in Property, plant and equipment | (534) | (1,343) |
| Decrease in other liabilities | - | 855 |
| Increase in other assets | 446 | - |
| (Decrease) in other liabilities | <u>(88)</u> | <u>(488)</u> |

(g) Summary impact on general reserve due to change in accounting policies and errors

Following the impact of changes in accounting policies and restatement of material prior period errors, general reserve is restated as follows:

| | Effect on 2012 \$000 | Effect on 2011 \$000 |
|---|----------------------------|----------------------------|
| Balance as previously reported | 63,652 | 58,707 |
| Impact of change in accounting policy | 39,380 | 31,110 |
| Impact of prior period errors 1 January 2012 | (5,091) | - |
| Impact of prior period errors (Note 2(f) ii – vi) | (9,225) | (5,091) |
| Reclassifications* | <u>(5,682)</u> | <u>(4)</u> |
| Restated balance as 31 December | <u>83,034</u> | <u>84,722</u> |

*Reclassifications are made to correct the presentation between reserves. In the financial period ended 31 December 2012, \$5.68m relating to revaluation of investment property was required to be transferred to the asset revaluation reserve in accordance with the CBSI Act but had remained in the general reserve.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

3. Statement of significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in the financial statement except for the change in accounting policy as explained in Note 2 (e).

(a) Foreign currency

Transactions in foreign currencies are translated into the functional currency of the Bank at the spot exchange rates at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in foreign currency translated at the spot exchange rate at the end of the year.

Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of transaction.

Foreign currency differences arising on retranslation are recognised in profit or loss.

(b) Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes all transaction costs and fees paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the statement of comprehensive income include:

- Interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis; and
- Interest on available-for-sale investments securities calculated on effective interest basis.

(c) Fees and commission

Fees and commission income and expense relate mainly to transaction and service fees, which are expensed as the services are received.

(d) Tax expense

The Bank is exempted from income tax under the Income Tax (Central Bank of Solomon Islands) (Exemption) Order of 21st June 1976 as provided for under Section 16 (2) of the Income Tax Act (CAP 123).

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

3. Statement of significant accounting policies (continued)

(e) Financial assets and financial liabilities

i. Recognition

The Bank initially recognises loans and advances, deposits and debt securities on the date that they are originated. All other financial assets and liabilities are recognised initially on the trade date, which is the date that the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

ii. Classification

Financial assets

The Bank classifies its financial assets in one of the following categories:

- loans and advances;
- held to maturity;
- available-for-sale.

Financial liabilities

The Bank classifies its financial liabilities as measured at amortised cost.

iii. Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in such transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

Financial liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

iv. Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

v. Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

The Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and present actual and regularly occurring market transactions on an arm's length basis.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

3. Statement of significant accounting policies (continued)

(e) Financial assets and financial liabilities

v. Fair value measurement (continued)

Assets are measured at a bid price, while liabilities are measured at an asking price. Fair values reflect the credit risk of the instrument and include adjustments to take account of credit risk of the Bank.

(f) Cash and cash equivalents

Cash and cash equivalents include notes and coins held by the Bank, teller's cash, current accounts with a maturity of three months or less from the acquisition date and other short term highly liquid term deposits.

Cash and cash equivalents are carried at amortised costs in the statement of financial position.

(g) Held-to-maturity

Held-to-maturity investments are non-derivative assets with fixed or determinable payment and fixed maturity that the Bank has the positive intent and ability to hold to maturity. Held-to-maturity investments comprise of fixed term deposits, short term commercial papers and bonds.

Held-to-maturity investments are carried at amortised costs using the effective interest method less any impairment losses. A sale or reclassification of more than an insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available for sale, and would prevent the Bank from classifying investment securities as held to maturity for the current and the following two financial years.

(h) Available-for-sale

Available-for-sale investments are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. Available-for-sale investments comprise of gold holdings and are carried at fair value.

Fair value changes other than impairment losses are recognized in other comprehensive income and presented in the Gold Revaluation Reserve in equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to profit or loss. Impairment losses are recognized in profit or loss.

(i) Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. Loans and advances comprise of loans and advances to Solomon Islands Government and staff loans.

Loans and advances are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised costs using the effective interest method.

(j) Currency Inventory

Currency inventory are recognized in the statement of financial position at cost.

Currency inventory relates to notes and coins purchased for circulation. The amount expensed in profit or loss is based on the cost of notes and coins that are issued into circulation.

(k) Currency in circulation

Currency issued by the Bank represents a claim on the Bank in favour of the holder. Currency in circulation comprises notes and coins issued by the Bank and the liability for currency in circulation is recorded at face value in the statement of financial position.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

3. Statement of significant accounting policies (continued)

(l) Property, plant and equipment

Recognition and measurement

Certain items of property, plant and equipment are initially measured at cost less accumulated depreciation and any accumulated impairment losses. Land and buildings are initially recognized at cost less accumulated depreciation and subsequently revalued to fair value.

Costs includes expenditures that is directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Any gain or loss on disposal of property, plant and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the asset at the time of disposal) is recognized within other income in profit or loss.

Subsequent costs

Subsequent expenditure is capitalized only when it is probable that the future economic benefits of the expenditure will flow to the Bank. Ongoing repairs and maintenance are expensed as incurred.

Depreciation

Items of property, plant and equipment are depreciated from the date they are available for use. Depreciation is charged on a straight line basis over the estimated useful lives of the assets. The rates of depreciation used are based on the following estimated useful lives:

| | |
|--------------------------------|--------------|
| Buildings | 4 - 55 years |
| Computers | 3 years |
| Furniture, plant and equipment | 3 - 5 years |
| Motor vehicles | 4 years |

Periodic revaluation

The Board has determined that apart from land and buildings, the remaining fixed assets of the Bank are recorded at values approximating recoverable market values. With Board approval, a three year periodical revaluation of its land and buildings was firstly done in 2006 and recently done in 2012. This included a review of the asset classes, estimated useful lives and depreciation rates, and current market values where deemed appropriate. The basis of this valuation is the open market value, that is, the highest and best value the property would expect to be realized if put for sale on private treaty. The Board proposes to have such assets revaluation every three years. The next revaluation will be done in 2015.

(m) Investment property

Investment property, is property held either to earn rentals or for capital appreciation or for both. Investment property is initially measured at cost and subsequently at fair value with any change therein recognised in profit or loss. Costs include expenditures that are directly attributable to the acquisition of the investment property.

Any gain or loss on disposal of an investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognized in profit or loss. When an investment property that was previously classified as property, plant and equipment is sold, any related amount included in the revaluation reserve is transferred to retained earnings.

When the use of the property changes such that it is reclassified as property, plant and equipment, its fair value at the date of the reclassification becomes its cost for subsequent accounting.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

3. Statement of significant accounting policies (continued)

(n) Demand deposits

Demand deposits represent funds placed with the Bank by financial institutions and other organizations. Demand deposits are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method. These deposits are at call.

(o) Employee entitlements

Short-term employee benefits

Short-term employee benefits comprises of accrued wages and salaries, annual leave and entitlement to Solomon Islands National Provident Fund are measured on an undiscounted basis and are expensed as the related service is provided.

Liabilities recognised in respect of short-term employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Long-term employee benefits

Long-term employee benefits comprises of long service leave and early retirement benefit.

Liabilities recognised in respect of long-term employee benefits which are not expected to be settled within 12 months are measured at the present value of the estimated future cash outflows to be made resulting from employee's service provided to balance date, based on staff turnover history and is discounted using the rates attaching to external Bonds portfolio.

(p) Impairment

The carrying amounts of the Bank's assets are reviewed at balance date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated. An impairment loss is recognized whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

(q) Comparative figures

Where necessary, comparative figures have been changed to conform to changes in presentation in the current year.

(r) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2013, and have not been applied in preparing these financial statements. None of these is expected to have a significant effect on the financial statements of the Bank, except for IFRS 9 Financial Instruments, which becomes mandatory for the Bank's 2015 financial statements and could change the classification and measurement of financial assets. The Bank does not plan to adopt this standard early and the extent of the impact has not been determined.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

| | 2013 \$000 | Restated 2012 \$ 000 |
|---|---------------|----------------------------|
| 4. Income and expenses | | |
| (a) Interest income | | |
| Overseas investments | 39,913 | 57,669 |
| Local investments | 1,824 | 2,121 |
| | <u>41,737</u> | <u>59,790</u> |
| (b) Fees and commission income | | |
| Foreign dealings | 7,784 | 9,244 |
| Local dealings | 1,174 | 527 |
| | <u>8,958</u> | <u>9,771</u> |
| (c) Other income | | |
| Gain on disposal of fixed assets | 181 | 134 |
| Rent received | 934 | 1,028 |
| Sale of numismatic coins | 139 | 355 |
| Gains on foreign currency exchange | 614 | 492 |
| Royalties on numismatics | 649 | 807 |
| Others | 221 | 449 |
| | <u>2,738</u> | <u>3,265</u> |
| (d) Interest expense | | |
| Foreign liabilities | 82 | 179 |
| Local liabilities | 7,067 | 9,352 |
| | <u>7,149</u> | <u>9,531</u> |
| (e) Administration expenses | | |
| Staff costs | 23,306 | 22,605 |
| Telecommunication | 1,783 | 1,408 |
| Utilities | 2,442 | 2,131 |
| Repairs and maintenance | 2,217 | 3,218 |
| Insurance | 345 | 253 |
| Consumables | 834 | 579 |
| Stationery, printing and postage | 710 | 677 |
| Consultancy | 39 | 620 |
| Other | 903 | 1,058 |
| | <u>32,579</u> | <u>32,549</u> |
| (f) Other expenses | | |
| Board of directors remunerations and expenses | 529 | 403 |
| Currency expenses | 17,913 | 25,504 |
| Depreciation | 7,255 | 4,474 |
| Auditors remuneration | 309 | 641 |
| Loss on realization of gold instrument | 590 | - |
| Other | 1,227 | 872 |
| | <u>27,823</u> | <u>31,894</u> |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

| | 2013 \$000 | Restated 2012 \$000 |
|--|------------------|---------------------------|
| 5. Held-to-maturity investments | | |
| Fixed term deposits | 2,454,535 | 2,355,235 |
| Short term commercial paper | 128,914 | - |
| Bonds | 170,374 | 199,869 |
| | <u>2,753,823</u> | <u>2,555,104</u> |
| 6. Available-for-sale investments | | |
| Unallocated gold - at fair value | 103,281 | 143,320 |
| Gold bullion - at fair value | 109,792 | 74,182 |
| | <u>213,073</u> | <u>217,502</u> |

7. International Monetary Fund

The Solomon Islands is a member of the International Monetary Fund (IMF) and the Central Bank of Solomon Islands has been designated as the Government of the Solomon Islands' fiscal agency (through which the Government deals with the IMF) and as the depository for the IMF's holding in Solomon Islands dollars.

The Solomon Islands subscription to the IMF has been met by:

- (i) payment to the IMF out of Central Bank external assets which have been reimbursed by the Government of the Solomon Islands by issue of non-interest bearing securities;
- (ii) the funding of accounts in favor of the IMF in the books of the Central Bank by the Government of the Solomon Islands.
- (iii) The liabilities to the IMF include subscriptions which are maintained in the IMF No.1 and IMF No. 2 accounts, are disclosed together as capital subscription. The IMF maintains such balances in their accounts in both Special Drawing Rights (SDR) and Solomon Islands dollar equivalents; the Bank balances are maintained only in Solomon Islands dollars.

Standby credit facility with IMF commenced in 2010 with first disbursement received 23rd June 2010. The final disbursement was transacted on the 1st of December 2011.

The extended credit facility with IMF was approved and drawn down on 11 December 2012

IMF related assets and liabilities

| | 2013 \$000 | Restated 2012 \$000 |
|-------------------------------------|----------------|---------------------------|
| Foreign currency assets | | |
| - Reserve tranche position | 6,029 | 6,022 |
| - Special drawing rights | 103,031 | 102,917 |
| - Currency subscription | 107,949 | 107,826 |
| | <u>217,009</u> | <u>216,765</u> |
| Foreign currency liabilities | | |
| - Standby credit facility | 136,774 | 136,618 |
| - Special drawing rights allocation | 108,590 | 108,466 |
| - Extended credit facility | 3,257 | 1,626 |
| - Securities | 107,059 | 106,936 |
| - Capital subscription | 915 | 915 |
| | <u>356,595</u> | <u>354,561</u> |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

| | 2013 \$000 | Restated 2012 \$000 |
|--|---------------|---------------------------|
| 8. Loans and advances | | |
| <i>Solomon Islands Government</i> | | |
| Loans and advances | 46 | 2,402 |
| Development bonds | 27 | 27 |
| Treasury bills | 483 | 40 |
| Other securities | 4,936 | 4,936 |
| Amortizing bonds | 69,391 | 74,691 |
| | <u>74,883</u> | <u>82,096</u> |
| <i>Staff loans</i> | | |
| Staff housing loans | 4,947 | 3,887 |
| Management car loans | 391 | 348 |
| Personal loans | 1,057 | 843 |
| | <u>6,395</u> | <u>5,078</u> |
| | <u>81,278</u> | <u>87,174</u> |
| 9. Currency inventory | | |
| Notes | 20,406 | 19,855 |
| Coins | 19,453 | 19,525 |
| | <u>39,859</u> | <u>39,380</u> |
| 10. Investment properties | | |
| Balance at beginning of financial year – at fair value | 11,323 | 5,641 |
| Changes in fair value | 612 | 5,682 |
| Balance at end of financial year – at fair value | <u>11,935</u> | <u>11,323</u> |
| 11. Other assets | | |
| Commercial bank clearing | 97,905 | 45,194 |
| Others | 624 | 998 |
| | <u>98,529</u> | <u>46,192</u> |

Central Bank of Solomon Islands

Notes to and forming part of the financial statements

For the year ended 31 December 2013

12. Property, plant and equipment

| | Land and buildings \$000 | Plant, equipment and furniture \$000 | Motor vehicles \$000 | Computer \$000 | Work in Progress \$000 | Total \$000 |
|---|-----------------------------|---|-------------------------|-------------------|---------------------------|----------------|
| <i>Cost/valuation</i> | | | | | | |
| Restated balance at 1 January 2012 | 48,481 | 19,322 | 2,531 | 4,609 | 37,653 | 112,596 |
| Acquisitions | - | 3,294 | 348 | 797 | 13,921 | 18,360 |
| Transfers | 48,466 | - | - | - | (48,466) | - |
| Disposals | (2770) | (51) | (723) | - | - | (3,544) |
| Revaluation increment | 29,125 | - | - | - | - | 29,125 |
| Restated balance at 31 December 2012 | 123,302 | 22,565 | 2,156 | 5,406 | 3,108 | 156,537 |
| Acquisitions | - | 2,050 | 437 | 997 | 7,236 | 10,720 |
| Transfers | 5,932 | - | - | - | (5,932) | - |
| Disposals | - | (13) | (351) | - | - | (364) |
| Balance at 31 December 2013 – cost | 5,923 | 24,602 | 2,242 | 6,403 | 4,412 | 160,961 |
| Balance at 31 December 2013 - valuation | 123,302 | - | - | - | - | 123,302 |
| Balance at 31 December 2013 | 129,234 | 24,602 | 2,242 | 6,403 | 4,412 | 166,893 |
| <i>Accumulated depreciation</i> | | | | | | |
| Restated balance at 1 January 2012 | 2,603 | 14,006 | 1,387 | 2,702 | - | 20,698 |
| Depreciation charge for the year | - | 2,843 | 569 | 1,062 | - | 4,474 |
| Disposals | (2,603) | (39) | (668) | - | - | (3,310) |
| Restated balance at 31 December 2012 | - | 16,810 | 1,288 | 3,764 | - | 21,862 |
| Depreciation charge for the year | 3,288 | 2,288 | 473 | 1,206 | - | 7,255 |
| Disposals | - | (13) | (351) | - | - | (364) |
| Balance at 31 December 2013 | 3,288 | 19,085 | 1,410 | 4,970 | - | 28,753 |
| <i>Carrying amount</i> | | | | | | |
| At 1 January 2012 (restated) | 45,878 | 5,316 | 1,144 | 1,907 | 37,653 | 91,898 |
| At 31 December 2012 (restated) | 123,302 | 5,755 | 868 | 1,642 | 3,108 | 134,675 |
| At 31 December 2013 | 125,946 | 5,517 | 832 | 1,433 | 4,412 | 138,140 |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

13. Demand deposits

| | 2013 | Restated |
|--|-------|----------|
| | \$000 | 2012 |
| | | \$000 |

(a) Foreign currency demand deposits

| | | |
|-----------------|--------|--------|
| Demand deposits | 43,890 | 86,103 |
|-----------------|--------|--------|

Demand deposits from international organizations such as the Asian Development Bank (ADB), European Development Bank (EDB), International Fund for Agricultural Development (IFAD), International Development Association.

| | 2013 | Restated |
|---|------------------|------------------|
| | \$000 | 2012 |
| | | \$000 |
| (b) Local currency demand deposits | | |
| Commercial banks | 1,423,680 | 1,446,496 |
| Solomon Islands Government | 1,161,336 | 903,933 |
| Other financial corporations | 10,664 | 8,369 |
| Other | 6,275 | 3,158 |
| | <u>2,601,955</u> | <u>2,361,956</u> |

14. Currency in circulation

| | | |
|-------|----------------|----------------|
| Notes | 596,429 | 583,107 |
| Coins | 21,141 | 16,562 |
| | <u>617,570</u> | <u>599,669</u> |

15. Fixed deposits

| | | |
|--------------|---------|---------|
| Bokolo bills | 611,932 | 367,888 |
|--------------|---------|---------|

Bokolo bills are short term discount securities issued and backed by the Central Bank of Solomon Islands. The instrument is used by the Bank for its monetary operations.

| | 2013 | Restated |
|--|--------|----------|
| | \$000 | 2012 |
| | | \$000 |
| 16. SIG monetary operations account | | |
| SIG monetary operations account | 33,604 | 38,387 |

17. Employee entitlements

| | | |
|--------------------------|---------------|--------------|
| Gratuity | 329 | 309 |
| Long service leave | 508 | 459 |
| Early retirement benefit | 10,172 | 8,600 |
| | <u>11,009</u> | <u>9,368</u> |

18. Other liabilities

| | | |
|--------------------------|--------------|---------------|
| Unpresented bank cheques | 7,149 | 7,205 |
| Other liabilities | 2,253 | 4,603 |
| | <u>9,402</u> | <u>11,808</u> |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

19. Determination of distributable profit

Profits of the Bank are determined and dealt with in accordance with Section 54 and 55 of the Central Bank of Solomon Islands Act., 2012 as follows:

- a) Section 54(2)(a) states that unrealized revaluation gains shall be deducted from the net profits and shall not be available to be distributed but allocated to the respective unrealized revaluation reserve account;
- b) The realized gains from previous years shall be deducted from the appropriate revaluation reserve account and adding to the distributable earnings as determined in section 54(2)(a).

| | 2013 \$000 | Restated 2012 \$000 |
|---|-----------------|---------------------------|
| <i>Net profit distribution according to CBSI Act 2012</i> | | |
| Net operating (loss)/profit | (165,101) | 71,347 |
| Add/(less) net unrealized foreign exchange loss/(gain) | 150,548 | (67,353) |
| (Less) changes in fair value in investment properties | (612) | (5,682) |
| Net losses to be recorded in general reserve | (15,165) | (1,688) |

Section 55(3) of the Central Bank of Solomon Islands Act., 2012 states that negative distributable earnings shall first be charged to the general reserve account and subsequently applied to authorized capital.

20. Cash and cash equivalents

Cash and cash equivalents included in the statement of cash flows comprise of the following:

| | 2013 \$000 | Restated 2012 \$000 |
|--|----------------|---------------------------|
| Cash on hand – local currency | 300 | 456 |
| Cash and cash equivalents – foreign currency | 732,680 | 764,448 |
| | 732,980 | 764,904 |

21. Share capital

Section 6 (1) of the CBSI Act, states that the authorized and paid up capital of the bank shall be an amount equivalent to \$50 million dollars (2012: \$20 million). The capital is fully subscribed by the Government of Solomon Islands.

| | 2013 \$000 | Restated 2012 \$000 |
|--|---------------|---------------------------|
| Balance at the beginning of the year | 20,000 | 20,000 |
| Transfer from General Reserve according to Section 6(1) of CBSI Act., 2012 | 30,000 | - |
| Balance at the end of the year | 50,000 | 20,000 |

22. Reserves

Under Section 53(2) of the CBSI Act., 2012, the Bank shall maintain the following reserves. Their purpose and method of operation are to be as follows:

a) General reserve

The general reserve was established under Section 53(1) as a reserve for the purposes of covering losses sustained by the Bank.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

22. Reserves (continued)

b) Foreign exchange asset revaluation reserve

Unrealised gains and losses on revaluation of foreign exchange balances are recognized in the profit and loss under other comprehensive income and are transferred to the foreign exchange asset revaluation reserve at the end of the accounting period.

c) Asset revaluation reserve

The asset revaluation reserve reflects the impact of changes in the market value of property.

d) Gold revaluation reserve

The unallocated and allocated gold is valued at current quoted market prices. Gold is accounted for as an available for sale financial asset. Unrealized gains and losses arising from revaluation are recognized in the gold revaluation reserve at end of the accounting period.

e) Capital asset reserve

The capital asset reserve is used to strengthen the Bank's equity position in relation to future major capital investment in buildings and equipment.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

23. Financial risk and management policies

(a) Introduction and overview

The structure of the Bank's statement of financial position is primarily determined by the nature of its statutory functions. International Financial Reporting Standards (IFRS) 7 – (Financial Instrument Disclosures) requires disclosure of information relating to financial instruments, their significance, performance, accounting policy, terms and conditions, fair values and the bank's policies for controlling risks and exposures relating to the financial instruments.

The Bank's risk management framework differs from the risk management framework for most other financial institutions. The main financial risks that the Bank faces include;

- Liquidity risk
- Credit risk
- Market risk
- Operational risk

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and procedures for measuring and managing risk.

Risk management framework

Like most central banks, the nature of the Bank's operations creates exposures to a range of operational and reputational risks. The Board of Directors has overall responsibility of the establishment and oversight of the Bank's risk management framework.

The Bank's management seeks to ensure that strong and effective risk management and control systems are in place for assessing, monitoring and managing risk exposure. The Board of Directors and the Management are responsible for managing and monitoring the business strategy, risks and performance of the Bank.

Internal Audit forms part of the Bank's risk management framework. This function reports to the Governor and the Board Audit Committee on internal audit and related issues. All areas in the Bank are subject to periodic internal audit review.

The Bank is subject to an annual audit by an external auditor. Auditing arrangements are overseen by an Audit Committee of the Board to monitor the financial reporting and audit functions within the Bank and the committee reviews the internal audit functions as well. The committee reports to the Board of Directors on its activities.

The overall risk management framework is designed to strongly encourage the sound and prudent management of the Bank's risk. The Bank seeks to ensure the risk management framework is consistent with financial market best practice.

The risk tables in this note are based on the Bank portfolio as reported in its statement of financial position.

(b) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

Management of liquidity risk

To limit the liquidity risk, the Bank maintains an adequate level of reserves and taking into consideration the transaction demand on foreign exchange, ensures that an acceptable amount is maintained in current accounts at all times. The Bank invests in high quality instruments, including commercial paper and debt issued by Governments and Supranationals, all of which are easily converted to cash (refer to maturity analysis on liquidity).

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

23. Financial risk and management policies (continued)

(b) Liquidity risk (continued)

Maturity analysis as at 31 December 2013

The maturity analysis noted below includes all financial assets and liabilities as at 31 December 2013.

| | On Demand \$000 | 0-3 Months \$000 | 3-6 Months \$000 | 6-12 Months \$000 | Over 1 year \$000 | Undefined Maturity \$000 | Total \$000 |
|---|-----------------------|------------------------|------------------------|-------------------------|-------------------------|--------------------------------|------------------|
| Foreign currency financial assets | | | | | | | |
| Money on demand | 732,680 | - | - | - | - | - | 732,680 |
| Accrued interest | - | - | 9,167 | - | - | - | 9,167 |
| Fix term deposits | - | 1,329,093 | 1,036,891 | 88,551 | - | - | 2,454,535 |
| Holding of special drawing rights | - | - | - | - | - | 103,031 | 103,031 |
| Reserve tranche | - | - | - | - | - | 6,029 | 6,029 |
| Subscription | - | - | - | - | - | 107,949 | 107,949 |
| Gold investment | - | - | - | - | - | 213,073 | 213,073 |
| Bonds | - | - | - | 32,701 | 137,673 | - | 170,374 |
| Short term commercial paper | - | - | 128,914 | - | - | - | 128,914 |
| | 732,680 | 1,329,093 | 1,174,972 | 121,252 | 137,673 | 430,082 | 3,925,752 |
| Local currency financial assets | | | | | | | |
| Cash on hand | 300 | - | - | - | - | - | 300 |
| Other receivables | - | - | 97,905 | - | - | - | 97,905 |
| Loans and advances | - | - | - | - | 81,278 | - | 81,278 |
| | 300 | - | 97,905 | - | 81,278 | - | 179,483 |
| Total financial assets | 732,980 | 1,329,093 | 1,272,877 | 121,252 | 218,951 | 430,082 | 4,105,235 |
| Foreign currency financial liabilities | | | | | | | |
| Demand deposits | 43,890 | - | - | - | - | - | 43,890 |
| IMF standby credit facility | - | 136,774 | - | - | - | - | 136,774 |
| IMF special drawing rights | - | - | - | - | - | 108,590 | 108,590 |
| Allocations | - | - | - | - | - | 3,257 | 3,257 |
| IMF extended credit facility | - | - | - | - | - | 107,059 | 107,059 |
| IMF securities | - | - | - | - | - | 915 | 915 |
| Capital subscriptions | - | - | - | - | - | - | - |
| | 43,890 | 136,774 | - | - | - | 219,821 | 400,485 |
| Local currency financial liabilities | | | | | | | |
| Demand deposits | 2,601,955 | - | - | - | - | - | 2,601,955 |
| Currency in circulation | - | - | - | - | - | 617,570 | 617,570 |
| SIG monetary operations account | - | 33,604 | - | - | - | - | 33,604 |
| Fixed deposits | - | - | 611,932 | - | - | - | 611,932 |
| Employee entitlements | - | - | - | - | 11,009 | - | 11,009 |
| Other liabilities | 7,149 | 2,253 | - | - | - | - | 9,402 |
| | 2,609,104 | 35,857 | 611,932 | - | 11,009 | 617,570 | 3,885,472 |
| Total financial liabilities | 2,652,994 | 172,631 | 611,932 | - | 11,009 | 837,391 | 4,285,957 |
| Net assets/ (liabilities) | (1,920,014) | 1,156,462 | 660,945 | 121,252 | 207,942 | (407,309) | (180,722) |

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23. Financial risk and management policies (continued)

(b) Liquidity risk (continued)

Maturity analysis as at 31 December 2012

The maturity analysis noted below includes all financial assets and liabilities as at 31 December 2012.

| | On Demand \$000 | 0-3 Months \$000 | 3-6 Months \$000 | 6-12 Months \$000 | Over 1 year \$000 | Undefined Maturity \$000 | Total \$000 |
|---|--------------------|------------------------|------------------------|-------------------------|-------------------------|--------------------------------|------------------|
| Foreign currency financial assets | | | | | | | |
| Money on demand | 764,448 | - | - | - | - | - | 764,448 |
| Accrued interest | - | - | 9,593 | - | - | - | 9,593 |
| Fix term deposits | - | 637,970 | 1,717,265 | - | - | - | 2,355,235 |
| Holding of special drawing rights | - | - | - | - | - | 102,917 | 102,917 |
| Reserve tranche | - | - | - | - | - | 6,022 | 6,022 |
| Subscription | - | - | - | - | - | 107,826 | 107,826 |
| Gold investment | - | - | - | - | - | 217,502 | 217,502 |
| Bonds | - | - | - | - | 199,869 | - | 199,869 |
| | 764,448 | 637,970 | 1,726,858 | - | 199,869 | 434,267 | 3,763,412 |
| Local currency financial assets | | | | | | | |
| Cash on hand | - | 456 | - | - | - | - | 456 |
| Other receivables | - | 45,194 | - | - | - | - | 45,194 |
| Loans and advances | - | - | 2,403 | - | 84,771 | - | 87,174 |
| | - | 45,650 | 2,403 | - | 84,771 | - | 132,824 |
| Total financial assets | 764,448 | 683,620 | 1,729,261 | - | 284,640 | 434,267 | 3,896,236 |
| Foreign currency financial liabilities | | | | | | | |
| Demand deposits | 86,103 | - | - | - | - | - | 86,103 |
| IMF standby credit facility | - | 136,618 | - | - | - | - | 136,618 |
| IMF special drawing rights allocation | - | - | - | - | - | 108,466 | 108,466 |
| IMF extended credit facility | - | - | - | - | - | 1,626 | 1,626 |
| IMF securities | - | - | - | - | - | 106,936 | 106,936 |
| Capital subscriptions | - | - | - | - | - | 915 | 915 |
| | 86,103 | 136,618 | - | - | - | 217,943 | 440,664 |
| Local currency financial liabilities | | | | | | | |
| Demand deposits | 2,361,956 | - | - | - | - | - | 2,361,956 |
| Currency in circulation | - | - | - | - | - | 599,669 | 599,669 |
| SIG monetary operations Account | - | 38,387 | - | - | - | - | 38,387 |
| Fixed deposits | - | - | 367,888 | - | - | - | 367,888 |
| Employee entitlements | - | - | - | - | 9,368 | - | 9,368 |
| Other liabilities | 7,205 | 4,603 | - | - | - | - | 11,808 |
| | 2,369,161 | 42,990 | 367,888 | - | 9,368 | 599,669 | 3,389,076 |
| Total financial liabilities | 2,455,264 | 179,608 | 367,888 | - | 9,368 | 817,612 | 3,829,740 |
| Net assets/ (liabilities) | (1,690,816) | 504,012 | 1,361,373 | - | 275,272 | (383,345) | 66,496 |

Central Bank of Solomon Islands
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23. Financial risk and management policies (continued)

(c) Credit risk

Credit risk is the risk of loss arising from a counterparty to a financial contract failing to discharge its obligations.

Selection of a counterparty is made based on their respective credit rating. Investment decisions are based on the credit rating of the particular issuer, country limits and counterparty limits in place to control exposure risks.

The Bank uses Standard and Poor's, Moody's and Fitch credit ratings for assessing the credit risk of foreign counterparties. The credit ratings of counterparties are closely monitored and are updated as new market information is available. Foreign exchange limits per bank are imposed for all currency dealings.

Concentration of credit exposure

The Bank's significant end-of-year concentrations of credit exposure by portfolio type were as follows:

| | 2013 \$000 | 2012 \$000 |
|--------------------------------|------------------|------------------|
| Foreign currency assets | | |
| Cash at bank | 732,680 | 764,448 |
| Held to maturity investment | 2,753,823 | 2,555,104 |
| International monetary fund | 217,009 | 216,765 |
| | <u>3,703,512</u> | <u>3,536,317</u> |
| Local currency assets | | |
| Loans and advances | 81,278 | 87,174 |
| | <u>3,784,790</u> | <u>3,623,491</u> |

The Bank monitors credit risk by currency and sector. An analysis of concentrations of credit risk is shown below:

| | 2013 | | 2012 | |
|----------------------------------|------------------|------------|------------------|------------|
| | \$000 | % | \$000 | % |
| Concentration by currency | | | | |
| USD | 1,558,082 | 41 | 1,396,115 | 39 |
| AUD | 1,154,698 | 31 | 1,184,546 | 33 |
| EURO | 240,474 | 6 | 252,103 | 7 |
| SDR | 217,009 | 6 | 216,768 | 6 |
| NZD | 163,088 | 4 | 159,291 | 4 |
| SGD | 64,702 | 2 | 66,578 | 2 |
| STG | 305,459 | 8 | 260,916 | 7 |
| SBD | 81,278 | 2 | 87,174 | 2 |
| Total financial assets | <u>3,784,790</u> | <u>100</u> | <u>3,623,491</u> | <u>100</u> |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

23. Financial risk and management policies (continued)

(c) Credit risk (continued)

Concentration of credit exposure (continued)

| | 2013 | | 2012 | |
|--|-------------------------|------------|-------------------------|------------|
| | \$000 | % | \$000 | % |
| Concentration by sector | | | | |
| Foreign currency assets | | | | |
| Central banks | 732,680 | 20 | 764,448 | 22 |
| Commercial banks | 2,753,823 | 74 | 2,555,104 | 72 |
| International Monetary Fund | 217,009 | 6 | 216,765 | 6 |
| | <u>3,703,512</u> | <u>100</u> | <u>3,536,317</u> | <u>100</u> |
| Local currency assets | | | | |
| Solomon Islands Government loan and advances | 74,883 | 92 | 82,096 | 94 |
| Staff loan and advances | 6,395 | 8 | 5,078 | 6 |
| | <u>81,278</u> | <u>100</u> | <u>87,174</u> | <u>100</u> |
| Total financial assets | <u>3,784,790</u> | | <u>3,623,491</u> | |

(d) Market risk

Market risk is the risk that changes in market prices, such as interest rates and foreign exchange rates will affect the Bank's income or the value of its holding of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters while optimising the return on risk.

Interest rate risk management

The principal risk to which trading portfolios are exposed is the risk of loss from fluctuations in future cash flows or fair value of financial instruments because of a change in market interest rates. The Bank limits interest rate risk by modified duration targets. The duration of the portfolio is re-balanced regularly to maintain the targeted duration. Operations are largely money market focused.

Foreign exchange risk management

Exchange rate risk relates to the risk of loss of foreign reserves arising from changes in the exchange rates against the Solomon Islands dollar. The Bank has adopted a currency risk management policy, which maintains the Solomon Islands dollar value of the foreign reserves and manages the fluctuations in the revaluation reserve account. While the effect of fluctuations in foreign exchange are recorded in profit or loss, foreign exchange fluctuations are not included as part of profit distribution but transferred to the revaluation reserve for monitoring purposes.

In accordance with the CBSI Act., 2012, the task of maintaining the safety and liquidity of foreign reserve assets, as well as the returns from reserves asset management, are achieved through diversification of investment by entering into transactions in international capital and money markets. Analysis of risks is the process of managing the currency reserves by comparing factual risk levels with set limits.

The Bank's exposure to foreign exchange risk, based on carrying amounts, was as follows:

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23. Financial risk and management policies (continued)

(d) Market risk (continued)

2013 foreign currency risk

| | On Demand \$000 | 0-3 Months \$000 | 3-6 Months \$000 | 6-12 Months \$000 | Over 1 year \$000 | Undefined Maturity \$000 | Total \$000 |
|---|-----------------------|------------------------|------------------------|-------------------------|-------------------------|--------------------------------|------------------|
| Foreign currency financial assets | | | | | | | |
| Money on demand | 732,680 | - | - | - | - | - | 732,680 |
| Accrued interest | - | - | 9,167 | - | - | - | 9,167 |
| Term deposits | - | 1,329,093 | 1,036,891 | 88,551 | - | - | 2,454,535 |
| Holding of special drawing rights | - | 103,031 | - | - | - | - | 103,031 |
| Reserve tranche | - | 6,029 | - | - | - | - | 6,029 |
| Subscription | - | 107,949 | - | - | - | - | 107,949 |
| Gold investment | - | - | - | - | - | 213,073 | 213,073 |
| Bonds | - | - | - | 32,701 | 137,673 | - | 170,374 |
| Short term commercial paper | - | - | 128,914 | - | - | - | 128,914 |
| Total | 732,680 | 1,546,102 | 1,174,972 | 121,252 | 137,673 | 213,073 | 3,925,752 |
| Foreign currency financial liabilities | | | | | | | |
| Demand deposits | 43,890 | - | - | - | - | - | 43,890 |
| IMF standby credit facility | - | 136,774 | - | - | - | - | 136,774 |
| IMF special drawing rights allocations | - | - | - | - | - | 108,590 | 108,590 |
| IMF extended credit facility | - | 3,257 | - | - | - | - | 3,257 |
| IMF securities | - | 107,059 | - | - | - | - | 107,059 |
| Capital subscriptions | - | 915 | - | - | - | - | 915 |
| Total | 43,890 | 248,005 | - | - | - | 108,590 | 400,485 |
| Net foreign currency assets | 688,790 | 1,298,097 | 1,174,972 | 121,252 | 137,673 | 104,483 | 3,525,267 |

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23. Financial risk and management policies (continued)

(d) Market risk (continued)

2012 foreign currency risk

| | On Demand \$000 | 0-3 Months \$000 | 3-6 Months \$000 | 6-12 Months \$000 | Over 1 year \$000 | Undefined Maturity \$000 | Total \$000 |
|---|-----------------------|------------------------|------------------------|-------------------------|-------------------------|--------------------------------|------------------|
| Foreign currency financial assets | | | | | | | |
| Money on demand | 764,448 | - | - | - | - | - | 764,448 |
| Accrued interest | - | - | 9,593 | - | - | - | 9,593 |
| Fixed deposits | - | 637,970 | 1,717,265 | - | - | - | 2,355,235 |
| Holding of special drawing rights | - | 102,917 | - | - | - | - | 102,917 |
| Reserve Tranche | - | 6,022 | - | - | - | - | 6,022 |
| Subscription | - | 107,826 | - | - | - | - | 107,826 |
| Gold investment | - | - | - | - | - | 217,502 | 217,502 |
| Bonds | - | - | - | - | 199,869 | - | 199,869 |
| | 764,448 | 854,735 | 1,726,858 | - | 199,869 | 217,502 | 3,763,412 |
| Foreign currency financial liabilities | | | | | | | |
| Demand deposits | 86,103 | - | - | - | - | - | 86,103 |
| IMF standby credit facility | - | 136,618 | - | - | - | - | 136,618 |
| IMF special drawing rights allocation | - | - | - | - | - | 108,466 | 108,466 |
| IMF extended credit facility | - | 1,626 | - | - | - | - | 1,626 |
| IMF securities | - | 106,936 | - | - | - | - | 106,936 |
| Capital subscriptions | - | 915 | - | - | - | - | 915 |
| | 86,103 | 246,095 | - | - | - | 108,466 | 440,664 |
| Net foreign currency assets | 678,345 | 608,640 | 1,726,858 | - | 199,869 | 109,036 | 3,322,748 |

Concentration of foreign exchange

The Bank's net holdings of foreign exchange (excluding its holding of Special Drawing Rights) were distributed as follows as at 31 December 2013:

| | 2013 | | 2012 | |
|------|------------------|------------|------------------|------------|
| | (\$000's) | % | (\$000's) | % |
| USD | 1,558,081 | 45 | 1,396,116 | 42 |
| AUD | 1,154,698 | 33 | 1,184,544 | 36 |
| EURO | 240,474 | 7 | 252,103 | 8 |
| NZD | 163,087 | 5 | 159,291 | 5 |
| JPY | 4 | 0 | 4 | 0 |
| SGD | 64,702 | 2 | 66,578 | 2 |
| STG | 305,457 | 8 | 260,916 | 7 |
| | 3,486,503 | 100 | 3,319,552 | 100 |

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

23. Financial risk and management policies (continued)

(d) Market risk (continued)

The following significant exchange rates were used at year end to convert foreign currency balances to the Solomon Island dollar equivalent.

Reporting date spot rate

| | 2013 | 2012 |
|------|-------------|-------------|
| AUD | 0.1529 | 0.1309 |
| USD | 0.1359 | 0.1362 |
| NZD | 0.1663 | 0.1661 |
| GBP | 0.0824 | 0.0846 |
| EURO | 0.0986 | 0.1030 |
| JPY | 14.29 | 11.5896 |
| SGD | 0.1723 | 0.1666 |
| SDR | 0.0913 | 0.0914 |

Sensitivity to foreign exchange rate risk

| | 2013 | 2012 |
|---|-------------|-------------|
| | \$M | \$M |
| Change in profit/equity due to a 2 per cent appreciation in the reserves - weighted value of the Solomon Islands dollar | (77) | (65) |
| Change in profit/equity due to a 2 per cent depreciation in the reserves - weighted value of the Solomon Islands dollar | 82 | 66 |

(e) Operational risk management

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure and from external factors other than liquidity, credit and market risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risk arises from all of the Bank's operations.

Managing operational risk in the Bank is an integral part of day-to-day operations and oversight. This includes adherence to Bank wide corporate policies. There is also an active internal audit function carried out on a quarterly basis.

Operating loss is the risk of loss from breakdown of internal controls. The Bank has established an internal audit function which will exercise monitoring and control over accounting policies and procedures, and the effective functioning of the system of internal controls at the Bank.

Operating risk relating to the activities of foreign currency reserves management is controlled by a number of internal instructions, and there is clear segregation of front office and back office activity. The latter is one of the mechanisms for managing operating risk.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

24. Fair value of financial assets and liabilities

The fair value of an instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arms length transaction. Quoted market values represent fair value when a financial instrument is traded in an organized and liquid market that is able to absorb a significant transaction without moving the price against the trader.

Valuation of financial instruments

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active market for similar instruments; quoted market prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation techniques include inputs not based on observable data and the unobservable inputs have a significant impact on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The table below analyses financial instruments measured at fair value at the end of the reporting period.

| | Level 1 \$000 | Level 2 \$000 | Level 3 \$000 | Total \$000 |
|--|------------------|------------------|------------------|----------------|
| 31 December 2013 | | | | |
| <i>Foreign currency assets</i> | | | | |
| Available-for-sale financial assets at quoted market price | 213,073 | - | - | 213,073 |
| 31 December 2012 | | | | |
| <i>Foreign currency assets</i> | | | | |
| Available-for-sale financial assets at quoted market price | 217,502 | - | - | 217,502 |

During the financial period ended 31 December 2013, there were no transfers in and out of the fair value hierarchy levels mentioned above.

Central Bank of Solomon Islands

Notes to and forming part of the financial statements

For the year ended 31 December 2013

25. Related parties

The Bank has related party relationships with the Board of Directors, the Executive Management and the Solomon Islands Government.

The Board of Directors during the year were:

Denton Rarawa (Chairman and Governor)
Gane Simbe
Shardrach Fanega
Katululu Maepioh
Loyley Ngira
Lily Lomulo
Tele Bartlett (appointed 17 July 2013)
Primo Afeau (appointed 17 July 2013)
John Usuramo (appointed 18 December 2013)
Dr. Steve Aumanu (resigned 2 December 2013)
Leslie Teama (resigned 3 March 2013)

Directors' fees and emoluments

Amounts paid to directors during the year are disclosed in Note 4 (f). No other emoluments were paid or are due to the directors at year end.

Related Party Disclosures requires the disclosure of information relating to aggregate compensation of key management personnel. The key management personnel of the Bank are members of the Bank Board and senior staff who have responsibility for planning, directing and controlling the activities of the Bank. Fees of the non-executive members of the Board are determined by the Minister of Finance. The Governor and Deputy Governor contracts are subject to mid-term review by the Minister of Finance and annually in terms of Bank policies. The Board of Directors determines the remuneration of the Chief Managers.

During the year the following persons were the executives identified as key management personnel, with the greatest authority and responsibility for planning and controlling the activities of the Bank:

| | |
|------------------|---|
| Denton Rarawa | Governor |
| Gane Simbe | Deputy Governor |
| Raynick Aquillah | Chief Manager International |
| Daniel Haridi | Chief Manager Currency and Banking Operations |
| Michael Kikiolo | Chief Manager Economics Research and Statistics |
| Bella Simiha | Chief Manager HR and Corporate Services |
| Emmanuel Gela | Chief Manager Finance and Accounts |
| Raynold Moveni | Chief Manager Financial Market Supervision |
| Edward Manedika | Chief Manager Information Technology |

The remuneration of the Bank's key management personnel, included in 'personnel expenses' was as follows:

| | 2013 | 2012 |
|------------------------------|--------------|--------------|
| | \$000 | \$000 |
| Short-term employee benefits | 3,124 | 2,826 |
| Long-term benefits | 952 | 258 |
| | <u>4,076</u> | <u>3,084</u> |

Short-term benefits include cash salary, and in the case of staff, annual leave, motor vehicle benefits, health benefits and the fringe benefits of tax paid or payable on these benefits.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2013

25. Related parties (continued)

Long-term benefits include long service leave and early retirement benefits.

As at 31 December 2013 loans by the Bank to key management personnel are as follows:

| | 2013 | 2012 |
|---------------------|--------------|--------------|
| | \$000 | \$000 |
| Housing loan | 1,073 | 1,024 |
| Personal loan | 106 | 68 |
| Management car loan | 74 | - |
| | <u>1,253</u> | <u>1,092</u> |

There were no other related party transactions with Board members; transactions with director-related entities which occurred in the normal course of the Bank's operations were conducted on the terms no more favorable than similar transactions with other employees or customers.

Transactions with the Solomon Islands Government

The transactions with the Solomon Islands government include banking services, foreign exchange transactions, registry transactions and purchase of government securities. During the year, the Bank received \$1.7 million (2012: \$2.0 million) of interest income relating to their investments in government securities. The Bank also paid \$2.4 million (2012: \$2.6 million) to the government in accordance with Section 34 of the CBSI Act, 2012. The balance of the Bank's investment in Government securities at year end amounted to \$74.8 million (2012: \$82.1 million).

26. Commitments and contingent liabilities

The Bank has guaranteed staff housing loans with the commercial banks to the sum of \$0.67 million as at 31 December 2013 (2012: \$0.8 million). The guarantee scheme was no longer applied to staff since 2011 and is valid for eligible staff until the date of cessation of employment with the Bank.

In 2007 the Solomon Islands Government introduced and provided \$10 million for the establishment of the Small Business Finance Guarantee Scheme to be administered by CBSI. As at 31 December 2013, a total of 59 loans with a net guarantee of \$5.28 million (2012: \$3.95 million) have been administered under the scheme.

27. Events subsequent to balance date

There has not been any matter or circumstance that has arisen since the end of the financial year that has significantly affected, or may significantly affect, the operations of the Bank, the results of those operations, or the state of affairs of the Bank in future financial years.