



CENTRAL BANK OF SOLOMON ISLANDS

**ANNUAL STATEMENT OF ACCOUNTS
FOR THE YEAR ENDED 31 DECEMBER 2016**

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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 2016 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 (Deputy Governor)
Harry D Kuma (appointed 13 May 2015)
Sir Thomas Ko Chan (appointed on 3 August 2015)
Loyley Ngira (contract end on 5 February 2016)
Lily Lomulo (contract end on 5 February 2016)
John Usuramo (appointed on 18 December 2013)
Tele Bartlett (contract end on 17 July 2016)
Primo Afeau (contract end on 17 July 2016)
David K C Quan (appointed on 17 August 2016)
Leslie Teama (appointed on 17 August 2016)

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 2016 and the accompanying statement of profit and loss and other comprehensive income, statement of changes in equity and statement of cash flows give a true and fair view of the results 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.

Results

The net loss of the Bank for the year ended 31 December 2016 was \$42.5m (2015: \$44.31m profit).

Reserves

The Board approved the following transfers of reserves in the statement of profit and loss and other comprehensive income during the year:

- (\$66.35m) (2015: \$26.10m) to the foreign exchange revaluation reserve; and
- \$23.84m (2015: \$17.61m) 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 depreciation and employee entitlements.

Going Concern

The Board believes that the Bank will continue to operate as a going concern.

Central Bank of the Solomon Islands

Directors' report (continued)

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.

Unusual transactions

Apart from these matters and other matters specifically referred to in the financial statements, in the opinion of the Directors the results of the operations of the Bank during the financial year were not substantially affected by any item, transaction or event of a material unusual nature, nor has there arisen between the end of the financial year and the date of this report any item, transaction or event of a material unusual nature likely, in the opinion of the Directors, to affect substantially the results of the operations of the Bank in the current financial year.

Events subsequent to balance date

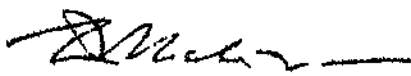
There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Bank, to affect significantly the operations of the Bank, the results of those operations, 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 20th of April 2017.

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



Denton Rarawa
Chairman of the Board and Governor



Harry D Kuma
Director

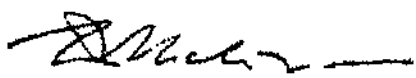
Central Bank of Solomon Islands

Statement by Directors

In the opinion of the Directors:

- (a) the accompanying statement of profit and loss and other 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 2016;
- (b) 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 2016;
- (c) 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 2016;
- (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 2016;
- (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") and Central Bank Solomon Islands Act 2012 ("Act 2012").

For and on behalf of the Board of Directors by authority of a resolution of the Directors this 20th of April 2017.



Denton Rarawa
Chairman of the Board and Governor



Harry D Kuma
Director



INDEPENDENT AUDITOR'S REPORT TO THE BOARD OF DIRECTORS OF CENTRAL BANK OF SOLOMON ISLANDS

Report on the Financial Statements

Opinion

I have in joint consultation with the Board of Directors ("the Board") of the Bank pursuant to section 60(1) of the *Central Bank of the 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 the Solomon Islands ("the Bank"), which comprise the statement of financial position as at 31 December 2016, the statements of profit and loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information as set out in notes 1 to 27.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2016, and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards (IFRS).

Emphasis of matter

As at 31 December 2016, the Bank's total assets amounted to \$4.666 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which total \$4.727 billion. These conditions have arisen from the Bank's large open position in foreign currency which is subject to foreign exchange rate movements.

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

Without further modifying my opinion, I draw attention to Note 2 (b) in the financial statements which indicates that the Bank had a deficiency in net assets of \$11.4m as at 31 December 2016. These conditions indicate the existence of a material uncertainty which the Bank must address under Section 56 of the Central Bank of the Solomon Islands Act 2012 through a request to the Minister of Finance and Treasury for a capital contribution by the Government to remedy the deficit and maintain reputable going concern.

Basis for Opinion

I conducted the audit in accordance with International Standard on Auditing (ISAs). My responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of my report. I am independent of the Bank in accordance to the ethical requirements that are relevant to my audit of the financial statements and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statement

Management are responsible for the preparation and fair presentation of the Financial Statements in accordance with International Financial Reporting Standards, and for such internal control as the management determine is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error

In preparing the financial statements, management are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

My objectives is to obtain reasonable assurance about whether the Financial Statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not guarantee that an audit conducted in accordance with International Standard on Auditing (ISAs) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or aggregate, they could reasonably be expected to influence the economic decisions of users taken on basis of the financial statements. As part of an audit in accordance with ISA, I exercise professional judgement and maintain professional scepticism throughout the audit. I also:

- Identify and access the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Bank's internal control.
- Evaluate the appropriateness of accounting policy used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the bank's ability to continue as going concern. If I conclude that material uncertainty exist, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures, are inadequate, to modify my opinion. My conclusion is based on the audit evidence obtained up to the date of our auditor's report.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statement represent the underline transactions and events in a manner that achieves fair presentation.

I communicate with those charge with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identified during my audit.

Report on Other Legal and Regulatory Requirements

I have obtained all the information and explanation which, to the best of my knowledge and belief, were necessary for the purpose of my audit.

In my opinion:

i) proper books of account have been kept by the Bank, sufficient to enable financial statements to be prepared, so far as it appears from my examination of those books; and

ii) to the best of my knowledge and according to the information and explanations given to me the financial statements give the information required by the Central Bank of Solomon Islands Act 2012, in the manner so required.



Peter Lokay
Auditor-General
25 April, 2017

Office of the Auditor-General
Honiara, Solomon Islands

Central Bank of Solomon Islands
Statement of profit and loss and other comprehensive income
For the year ended 31 December 2016

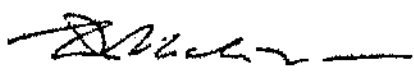
	Note	2016 \$'000	2015 \$'000
Income			
Interest income	4(a)	41,444	39,844
Fees and commission income	4(b)	38,859	43,898
Other income	4(c)	6,153	4,695
Change in fair value of investment properties	10	-	600
Net unrealised foreign exchange revaluation gain		-	26,101
Total income		<u>86,456</u>	<u>115,138</u>
Expenses			
Interest expense	4(d)	5,058	12,463
Fees and commission expense		1,684	1,221
Administrative expenses	4(e)	33,999	34,919
Other expenses	4(f)	21,873	22,227
Net unrealised foreign exchange revaluation loss		66,346	-
Total expenses		<u>128,960</u>	<u>70,830</u>
Net operating (loss)/profit		<u>(42,504)</u>	<u>44,308</u>
Other comprehensive income/(loss)			
Items that will not be reclassified to profit or loss			
Net change in fair value (property, plant and equipment)		-	14,626
Net change in fair value (available - for - sale financial assets)		17,869	(26,890)
Total other comprehensive income/(loss)		<u>17,869</u>	<u>(12,264)</u>
Total comprehensive (loss)/income		<u>(24,635)</u>	<u>32,044</u>

This statement of profit and loss and other 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 39.

Central Bank of Solomon Islands
Statement of financial position
As at 31 December 2016

	Note	2016 S'000	2015 S'000
Foreign currency assets			
Cash at bank	20	1,048,532	781,517
Accrued interest		5,320	6,495
Held-to-maturity investments	5	2,859,056	3,094,483
Available-for-sale investments	6	225,460	206,921
International Monetary Fund	7	263,467	206,302
Total foreign currency assets		4,401,835	4,295,718
Local currency assets			
Cash on hand	20	202	196
Loans and advances	8	12,261	11,629
Currency inventory	9	36,116	36,623
Investment properties	10	13,262	13,262
Property, plant and equipment	12	149,644	150,180
Other assets	11	52,334	4,516
Total local currency assets		263,819	216,406
Total assets		4,665,654	4,512,124
Foreign currency liabilities			
International Monetary Fund	7	390,348	324,646
Demand deposits	13(a)	59,202	16,240
Total foreign currency liabilities		449,550	340,886
Local currency liabilities			
Demand deposits	13(b)	2,519,783	2,573,231
Currency in circulation	14	868,395	776,640
Fixed deposits	15	761,658	721,677
SIG monetary operations account	16	51,359	58,422
Employee entitlements	17	15,671	17,000
Other liabilities	18	10,628	11,025
Total local liabilities		4,227,494	4,157,995
Total liabilities		4,677,044	4,498,881
Net assets		(11,392)	13,243
Capital and reserves			
Paid up capital	21	50,000	50,000
General reserve	22(a)	77,021	53,179
Foreign exchange revaluation reserve	22(b)	(214,677)	(148,331)
Asset revaluation reserve	22(c)	104,318	104,318
Gold revaluation reserve	22(d)	(89,929)	(107,798)
Capital asset reserve	22(e)	61,875	61,875
Total capital and reserves		(11,392)	13,243

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


Denton Rarawa
Chairman of the Board and Governor


Harry Kuma
Director

The statement of financial position is to be read in conjunction with the notes to and forming part of

Central Bank of Solomon Islands

Statement of changes in equity

For the year ended 31 December 2016

	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 at 1 January 2015	50,000	(80,908)	35,572	(174,432)	89,092	61,875	(18,801)
Total comprehensive income for the year							
Profit (loss) for the year (Note 19)	-	-	17,607	26,101	600	-	44,308
<u>Other comprehensive income/(losses)</u>							
Fair value losses – gold	-	(26,890)	-	-	-	-	(26,890)
Fair value gains – Property, plant and equipment	-	-	-	-	14,626	-	14,626
Total other comprehensive income/(losses)	-	(26,890)	17,607	26,101	15,226	-	32,044
Balance as at 31 December 2015	50,000	(107,798)	53,179	(148,331)	104,318	61,875	13,243
Balance at 1 January 2016	50,000	(107,798)	53,179	(148,331)	104,318	61,875	13,243
Total comprehensive income for the year							
Profit (loss) for the year (Note 19)	-	-	23,842	(66,346)	-	-	(42,504)
<u>Other comprehensive income/(losses)</u>							
Fair value losses – gold	-	17,869	-	-	-	-	17,869
Fair value gains – Property, plant and equipment	-	-	-	-	-	-	-
Total other comprehensive income/(losses)	-	17,869	23,842	(66,346)	-	-	(24,635)
Balance as at 31 December 2016	50,000	(89,929)	77,021	(214,677)	104,318	61,875	(11,392)

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 39.

Central Bank of Solomon Islands
Statement of cash flows
For the year ended 31 December 2016

	Note	2016 S'000	2015 S'000
Operating activities			
Interest received		42,666	38,500
Cash received from other income		45,013	48,494
Interest paid		(4,943)	(12,427)
Cash paid to suppliers and employees		(55,549)	(57,050)
Net movement in held to maturity investments		235,427	(209,933)
Net movement in International Monetary Fund accounts		33,759	(1,160)
Net movement in other receivables		(45,819)	38,990
Net movement in other payables		-	4,945
Cash flows from/(used in) operating activities		250,554	(149,641)
Investing activities			
Acquisition of property, plant and equipment		(4,803)	(2,777)
Proceeds from sale of premises, plant and equipment		-	99
Net movement in available-for-sale investments		(670)	(12,443)
Net movement in loan to government		(27)	63,950
Net movement in loans and advances to staff		(652)	(280)
Cash flows (used in)/from investing activities		(6,152)	48,549
Financing activities			
Net movement in currency in circulation		91,754	82,297
Net movement in demand deposits		(10,485)	96,270
Net movement in fixed deposits received		39,981	99,948
Solomon Islands government monetary operations		(7,063)	28,207
Net movement in International Monetary Fund credit facilities		(25,222)	(26,965)
Cash flows from financing activities		88,965	279,757
Net effect of exchange rates		(66,346)	26,101
Net increase in cash		267,021	204,766
Cash and cash equivalents at the beginning of the financial year		781,713	576,947
Cash and cash equivalents at the end of the financial year	20	1,048,734	781,713

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 39.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

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.

The financial statements were authorised for issue by the Board of Directors on 20th April 2017.

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.

The Bank will comply with the requirements of the Central Bank of Solomon Islands Act (Section 56) which requires that in the event that the value of its assets falls below the sum of its monetary liabilities and its unimpaired authorised capital, then –

- (a) The Board, with the advice of the external audit of the Bank, shall assess the situation and prepare a report on the causes and extent of the shortfall and assess the situation within a period of no more than 30 calendar days;
- (b) If the Board approves the report under paragraph (a), the Bank shall request the Minister of Finance for a capital contribution to be made by the Government to remedy the deficit; and
- (c) Upon receipt of this request the Government shall, within a period of no more than 30 calendar days, transfer to the Bank the necessary amount in currency or in negotiable debt instruments with a specified maturity issued at market-related interest rates prevailing in Solomon Islands.

As at 31 December 2016, the Bank's total assets amounted to \$4.67 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which totalled \$4.73 billion. The Bank had requested the Ministry of Finance for a capital contribution during the year to remedy the prior year deficit but the request had been repudiated. An emphasis of matter has been included in the audit report relating to this matter.

(b) Going concern basis of accounting

The financial statements have been prepared on a going concern basis, and as at 31 December 2016 the Bank had a deficiency in net assets of \$11.4 million.

The Bank's deficiency in net assets had implicate materialy on its going concern and requires reliable support of the Solomon Islands Government. These conditions indicate the existence of a material uncertainty which the Bank will address to maintain a reputable going concern.

The Board consider it appropriate to prepare these financial statements on a going concern basis and as provided for by section 56 of the Central Bank of Solomon Islands Act 2012 the Bank will again request through the Minister of Finance for capital contribution by the Government to remedy the deficit.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

2. Basis of preparation (continued)

(b) Going concern basis of accounting (continued)

The financial statements do not include any adjustments relating to the recoverability or classification of recorded asset amounts and classification of liabilities that might be necessary should the Bank be unable to continue as a going concern.

(c) 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.

(d) 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.

(e) 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 recognised 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.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

3. Statement of significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in the financial statements.

(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 profit and loss and other 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 recognised as revenue when services are rendered or expensed as the services are received.

(d) Other income

Other income are brought to account on an accrual basis.

(e) 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 2016

3. Statement of significant accounting policies (continued)

(f) 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.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

3. Statement of significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

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.

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.

(g) 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.

(h) 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 prior to maturity 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.

(i) 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 recognised 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 recognised in profit or loss.

(j) 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 the 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.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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3. Statement of significant accounting policies (continued)

(k) Currency inventory

Currency inventory are recognised 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.

(l) 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.

(m) 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 recognised at cost less accumulated depreciation and subsequently revalued to fair value.

Costs includes expenditure 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 recognised within other income in profit or loss.

Subsequent costs

Subsequent expenditure is capitalised 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 first done in 2012 and recently done in 2015. 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 realised for, 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 2018.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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3. Statement of significant accounting policies (continued)

(n) 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 expenditure that is 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 recognised 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.

(o) Demand deposits

Demand deposits represent funds placed with the Bank by financial institutions and other organisations. 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.

(p) Employee entitlements

Short-term employee benefits

Short-term employee benefits comprising 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 the external bonds portfolio.

(q) 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 recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in profit or loss.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

3. Statement of significant accounting policies (continued)

(r) Comparative figures

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

(s) New standards and interpretations not yet adopted

IFRS 9 'Financial instruments', published in July 2014, replaces the existing guidance in IAS 39 'Financial Instruments: Recognition and Measurement'. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and de-recognition of financial instruments from IAS 39. The standard is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

IFRS 16 'Leases', removes the classification of leases as either operating leases or finance leases – for the lessee – effectively treating all leases as finance leases. Short-term leases (less than 12 months) and leases of low-value assets (such as personal computers) are exempt from the lease accounting requirements. There are also changes in accounting over the life of the lease. In particular, companies will now recognise a front-loaded pattern of expense for most leases, even when they pay constant annual rentals. Lessor accounting remains similar to current practice – i.e. lessors continue to classify leases as finance and operating leases. The standard is effective for annual reporting periods beginning on or after 1 January 2019, with early adoption permitted.

IFRS 15 Revenue from Contracts with Customers was issued in 2014 by IASB. The standard is not mandatorily effective for the Bank until 1 January 2018. IFRS 15 contains new requirements for the recognition of revenue and additional disclosures about revenue. It is expected that a significant proportion of the Bank's revenue will be outside the scope of IFRS 15.

Central Bank of Solomon Islands
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For the year ended 31 December 2016

	2016 \$'000	2015 \$000
4. Income and expenses		
(a) Interest income		
Overseas investments	41,214	38,371
Local investments	230	1,473
	<u>41,444</u>	<u>39,844</u>
(b) Fees and commission income		
Foreign dealings	38,283	43,249
Local dealings	576	649
	<u>38,859</u>	<u>43,898</u>
(c) Other income		
Gain on disposal of fixed assets	1	99
Rent received	882	1,075
Sale of numismatic coins	78	80
Gains on foreign currency exchange	-	1,016
Royalties on numismatics	4,239	2,301
Others	953	124
	<u>6,153</u>	<u>4,695</u>
(d) Interest expense		
Foreign liabilities	66	57
Local liabilities	4,992	12,406
	<u>5,058</u>	<u>12,463</u>
(e) Administrative expenses		
Staff costs	23,516	25,012
Telecommunication	1,785	1,727
Utilities	2,101	1,801
Repairs and maintenance	3,021	2,304
Insurance	516	441
Consumables	424	430
Stationery, printing and postage	490	478
Consultancy	452	1,351
Other	1,694	1,375
	<u>33,999</u>	<u>34,919</u>
(f) Other expenses		
Board of directors remunerations and expenses	161	326
Currency expenses	11,569	14,952
Depreciation	5,339	5,335
Auditors remuneration	300	330
Other	4,504	1,284
	<u>21,873</u>	<u>22,227</u>

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

	2016 S'000	2015 S'000
5. Held-to-maturity investments		
Fixed term deposits	2,680,828	2,828,000
Short term commercial paper	57,990	175,294
Bonds	120,238	91,189
	<u>2,859,056</u>	<u>3,094,483</u>
6. Available-for-sale investments		
Unallocated gold - at fair value	109,285	100,299
Gold bullion - at fair value	116,175	106,622
	<u>225,460</u>	<u>206,921</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 Solomon Island's 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 the Central Bank's external assets which have been reimbursed by the Government of 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 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.

The 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

	2016 S'000	2015 S'000
Foreign currency assets		
- Reserve tranche position	34,155	5,981
- Special drawing rights	37,944	93,243
- Currency subscription	191,368	107,078
	<u>263,467</u>	<u>206,302</u>
Foreign currency liabilities		
- Standby credit facility	73,069	101,753
- Special drawing rights allocation	109,918	107,714
- Extended credit facility	11,537	8,076
- Securities	190,895	102,388
- Capital subscription	4,929	4,715
	<u>390,348</u>	<u>324,646</u>

Central Bank of Solomon Islands
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For the year ended 31 December 2016

	2016 \$'000	2015 \$000
8. Loans and advances		
<i>Solomon Islands Government</i>		
Loans and advances	46	46
Development bonds	27	27
Treasury bills	10	30
Other securities	4,936	4,936
	<u>5,019</u>	<u>5,039</u>
<i>Staff loans</i>		
Staff housing loans	5,780	5,093
Management car loans	512	453
Personal loans	950	1,044
	<u>7,242</u>	<u>6,590</u>
	<u>12,261</u>	<u>11,629</u>
9. Currency inventory		
Notes	11,164	11,339
Coins	24,952	25,284
	<u>36,116</u>	<u>36,623</u>
10. Investment properties		
Balance at beginning of financial year – at fair value	13,262	12,662
Add: Changes in fair value	-	600
Balance at end of financial year – at fair value	<u>13,262</u>	<u>13,262</u>

Investment property comprises of a commercial and a residential property that are leased to third parties. Each lease contains a lease period of 3 and 2 years respectively with annual rental subject to increase upon renewal indexed to the Honiara retail price index. Subsequent renewals are negotiated with the lessee.

When rent reviews or lease renewals have been pending with anticipated reversionary increases, all notices, when appropriate counter-notices, have been served validly and within the appropriate time.

Rental income from investment properties of \$881,845 (2015: \$1,075,000) has been recognised in other income.

Fair value hierarchy

The fair value of investment property and land and building (refer to note 12) was determined by an external, independent property valuer, having appropriate recognised professional qualifications and recent experience in the location and category of the property being valued. The independent valuer provides the fair value of the Bank's investment property portfolio on a regular basis.

The fair value of the Bank's investment property are categorised into Level 3 of the fair value hierarchy.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

10. Investment properties (continued)

Valuation techniques and significant unobservable inputs

The following table shows the valuation technique used in measuring the fair value of investment properties, as well as significant unobservable inputs used.

Valuation technique	Significant unobservable inputs	Inter-relationship between key unobservable inputs and fair value measurement
Replacement cost method: where the improvements are valued using current replacement cost and an allowance for depreciation and obsolescence plus the freehold value of the land (notable sales of comparable vacant sites within Honiara are noted).	<ul style="list-style-type: none"> • Depreciation rate applied. • Locality of the property • Proximity to civic amenities • Topography/geographical feature of the land • Demand for the land 	<p>The estimated fair value would increase (decrease) if:</p> <ul style="list-style-type: none"> • depreciation rate were lower (higher); • the property located in urban locality; • closer to civic amenities; • the higher the demand for the land.

	2016 \$000	2015 \$000
11. Other assets		
Commercial bank clearing	49,274	696
Others	3,060	3,820
	<u>52,334</u>	<u>4,516</u>

Central Bank of Solomon Islands

Notes to and forming part of the financial statements

For the year ended 31 December 2016

12. Property, plant and equipment

<i>Cost/valuation</i>	Land and buildings \$000	Plant, equipment and furniture \$000	Motor vehicles \$000	Computer \$000	Work in Progress \$000	Total \$000
Balance at 1 January 2015	135,274	25,325	2,191	7,066	2,301	172,157
Transfer from investment property	5,670	-	-	-	-	5,670
Acquisitions	-	162	237	570	1,808	2,777
Transfers	28	465	-	1,670	(2,163)	-
Disposals	-	(1,863)	(523)	(1,093)	-	(3,479)
Balance at 31 December 2015	140,972	24,089	1,905	8,213	1,946	177,125
Acquisitions	-	-	-	-	4,803	4,803
Transfers	-	643	-	1,194	(1,837)	-
Disposals	-	(122)	-	-	-	(122)
Balance at 30 December 2016	140,972	24,610	1,905	9,407	4,912	181,806

Accumulated depreciation

Balance at 1 January 2015	6,039	20,583	1,524	5,895	-	34,041
Depreciation charge for the year	2,932	1,199	388	816	-	5,335
Disposals	(8,956)	(1,863)	(523)	(1,089)	-	(12,431)
Balance at 31 December 2015	15	19,919	1,389	5,622	-	26,945
Depreciation charge for the year	2,963	784	293	1,299	-	5,339
Disposals	-	(122)	-	-	-	(122)
Balance at 30 December 2016	2,978	20,581	1,682	6,921	-	32,162

Carrying amount

At 1 January 2015	129,235	4,742	667	1,171	2,301	138,116
At 31 December 2015	140,957	4,170	516	2,591	1,946	150,180
At 30 December 2016	137,994	4,029	223	2,486	4,912	149,644

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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13. Demand deposits

	2016 \$000	2015 \$000
(a) Foreign currency demand deposits		
Demand deposits	<u>59,202</u>	<u>16,240</u>

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

	2016 \$000	2015 \$000
(b) Local currency demand deposits		
Commercial banks	1,747,864	1,510,974
Solomon Islands Government	759,033	1,050,278
Other financial corporations	4,809	5,077
Other	<u>8,077</u>	<u>6,902</u>
	<u>2,519,783</u>	<u>2,573,231</u>

14. Currency in circulation

Notes	837,146	748,548
Coins	<u>31,249</u>	<u>28,092</u>
	<u>868,395</u>	<u>776,640</u>

15. Fixed deposits

Bokolo bills	<u>761,658</u>	<u>721,677</u>
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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.

	2016 \$000	2015 \$000
16. SIG monetary operations account		
SIG monetary operations account	<u>51,359</u>	<u>58,422</u>
17. Employee entitlements		
Gratuity	1,080	1,096
Long service leave	631	1,404
Early retirement benefit	<u>13,960</u>	<u>14,500</u>
	<u>15,671</u>	<u>17,000</u>
18. Other liabilities		
Unpresented bank cheques	6,913	6,258
Other liabilities	<u>3,715</u>	<u>4,767</u>
	<u>10,628</u>	<u>11,025</u>

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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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 unrealised revaluation gains shall be deducted from the net profits and shall not be available to be distributed but allocated to the respective unrealised revaluation reserve account;
- b) The realised gains from previous years shall be deducted from the appropriate revaluation reserve account and added to the distributable earnings as determined in section 54(2)(a).

	2016 S'000	2015 S'000
<i>Net profit distribution according to CBSI Act 2012</i>		
Net operating profit /(loss)	(42,504)	44,308
Add/(less) - net unrealised foreign exchange loss/(gain)	66,346	(26,101)
- changes in fair value in investment properties	-	(600)
Net gain/(loss) to be recorded in general reserve	23,842	17,607

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 authorised capital.

20. Cash and cash equivalents

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

	2016 S'000	2015 S'000
Cash on hand – local currency	202	196
Cash and cash equivalents – foreign currency	1,048,532	781,517
	<u>1,048,734</u>	<u>781,713</u>

21. Share capital

Section 6 (1) of the CBSI Act, states that the authorised and paid up capital of the bank shall be an amount equivalent to \$50 million dollars (2014: \$50 million). The capital is fully subscribed by the Government of Solomon Islands.

	2016 S'000	2015 S'000
Balance at the beginning of the year	50,000	50,000
Transfer from General Reserve according to Section 6(1) of CBSI Act., 2012	-	-
Balance at the end of the year	50,000	50,000

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
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22. Reserves (continued)

b) Foreign exchange asset revaluation reserve

Unrealised gains and losses on revaluation of foreign exchange balances are recognised 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. Unrealised gains and losses arising from revaluation are recognised 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
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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 for 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 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
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23. Financial risk and management policies (continued)

(b) Liquidity risk (continued)

The Central Bank of Solomon Islands Act (Section 56) requires that in the event that the value of its assets falls below the sum of its monetary liabilities and its unimpaired authorised capital, then –

- (a) The Board, with the advice of the external audit of the Bank, shall assess the situation and prepare a report on the causes and extent of the shortfall and assess the situation within a period of no more than 30 calendar days;
- (b) If the Board approves the report under paragraph (a), the Bank shall request the Minister of Finance for a capital contribution to be made by the Government to remedy the deficit; and
- (c) Upon receipt of this request the Government shall, within a period of no more than 30 calendar days, transfer to the Bank the necessary amount in currency or in negotiable debt instruments with a specified maturity issued at market-related interest rates prevailing in Solomon Islands.

As at 31 December 2016, the Bank's total assets amounted to \$4.67 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which totalled \$4.73 billion.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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23. Financial risk and management policies (continued)

(b) Liquidity risk (continued)

Maturity analysis as at 31 December 2016

The maturity analysis noted below includes all financial assets and liabilities as at 31 December 2016.

	On Demand \$000s	0-3 Months \$000s	3-6 Months \$000s	6-12 Months \$000s	Over 1 Year \$000s	Undefined Maturity \$000s	Total \$000s
Foreign currency financial assets							
Money on demand	1,048,532	-	-	-	-	-	1,048,532
Fixed term deposits	-	1,929,862	743,184	17,606	-	-	2,690,652
Holding of special drawing rights	-	-	-	-	-	37,944	37,944
Reserve tranche	-	-	-	-	-	34,155	34,155
Subscription	-	-	-	-	-	191,368	191,368
Gold investment	-	-	-	-	-	225,460	225,460
Bonds	-	31,828	655	61,666	35,044	-	129,193
Short term commercial paper	-	-	29,121	29,121	-	-	58,242
	1,048,532	1,961,690	772,960	108,393	35,044	488,927	4,415,546
Local currency financial assets							
Cash on hand	202	-	-	-	-	-	202
Other receivables	-	49,215	59	-	-	-	49,274
Loans and advances	-	-	-	-	12,261	-	12,261
	202	49,215	59	-	12,261	-	61,737
Total financial assets	1,048,734	2,010,905	773,019	108,393	47,305	488,927	4,477,283
Foreign currency financial liabilities							
Demand deposits	59,202	-	-	-	-	-	59,202
IMF standby credit facility	-	-	-	-	-	73,069	73,069
IMF special drawing rights allocations	-	-	-	-	-	109,918	109,918
IMF extended credit facility	-	-	-	-	-	11,537	11,537
IMF securities	-	-	-	-	-	190,895	190,895
Capital subscriptions	-	-	-	-	-	4,929	4,929
	59,202	-	-	-	-	390,348	449,550
Local currency financial liabilities							
Demand deposits	2,519,784	-	-	-	-	-	2,519,784
Currency in circulation	-	-	-	-	-	868,395	868,395
SIG monetary operations account	-	51,359	-	-	-	-	51,359
Fixed deposits	-	750,771	11,258	-	-	-	762,029
Employee entitlements	-	-	-	-	15,670	-	15,670
Other liabilities	6,913	3,344	-	-	-	-	10,257
	2,526,697	805,474	11,258	-	15,670	868,395	4,227,493
Total financial liabilities	2,585,899	805,474	11,258	-	15,670	1,258,743	4,677,043
Net assets/(liabilities)	(1,537,165)	1,205,431	761,761	108,393	31,635	(769,816)	(199,761)

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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23. Financial risk and management policies (continued)

(b) Liquidity risk (continued)

Maturity analysis as at 31 December 2015

The maturity analysis noted below includes all financial assets and liabilities as at 31 December 2015.

	On Demand \$000s	0-3 Months \$000s	3-6 Months \$000s	6-12 Months \$000s	Over 1 Year \$000s	Undefined Maturity \$000s	Total \$000s
Foreign currency financial assets							
Money on demand	781,517	-	-	-	-	-	781,517
Accrued interest	-	5,959	536	-	-	-	6,495
Fixed term deposits	-	2,083,482	744,518	-	-	-	2,828,000
Holding of special drawing rights	-	-	-	-	-	93,248	93,248
Reserve tranche	-	-	-	-	-	5,981	5,981
Subscription	-	-	-	-	-	107,078	107,078
Gold investment	-	-	-	-	-	206,921	206,921
Bonds	-	-	-	-	91,189	-	91,189
Short term commercial paper	-	175,294	-	-	-	-	175,294
	781,517	2,264,735	745,054	-	91,189	413,223	4,295,718
Local currency financial assets							
Cash on hand	196	-	-	-	-	-	196
Other receivables	-	-	696	-	-	-	696
Loans and advances	-	-	-	-	11,629	-	11,629
	196	-	696	-	11,629	-	12,521
Total financial assets	781,713	2,264,735	745,750	-	102,818	413,223	4,308,239
Foreign currency financial liabilities							
Demand deposits	16,240	-	-	-	-	-	16,240
IMF standby credit facility	-	-	-	-	-	101,753	101,753
IMF special drawing rights allocations	-	-	-	-	-	107,714	107,714
IMF extended credit facility	-	-	-	-	-	8,076	8,076
IMF securities	-	-	-	-	-	102,389	102,389
Capital subscriptions	-	-	-	-	-	4,716	4,716
	16,240	-	-	-	-	324,645	340,886
Local currency financial liabilities							
Demand deposits	2,573,231	-	-	-	-	-	2,573,231
Currency in circulation	-	-	-	-	-	776,640	776,640
SIG monetary operations account	-	58,422	-	-	-	-	58,422
Fixed deposits	-	710,432	11,245	-	-	-	721,677
Employee entitlements	-	-	-	-	17,000	-	17,000
Other liabilities	6,258	4,766.87	-	-	-	-	11,025
	2,579,489	773,621	11,245	-	17,000	776,640	4,157,995
Total financial liabilities	2,595,729	773,621	11,245	-	17,000	1,101,285	4,498,881
Net assets/(liabilities)	(1,814,016)	1,491,114	734,505	-	85,818	(688,063)	(190,642)

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:

	2016 \$000	2015 \$000
Foreign currency assets		
Cash at bank	1,048,532	781,517
Held to maturity investment	2,859,056	3,094,483
International monetary fund	263,467	206,302
Gold investment	225,460	206,921
	<u>4,396,515</u>	<u>4,289,233</u>
Local currency assets		
Loans and advances	12,261	11,629
	<u>4,408,776</u>	<u>4,300,852</u>

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

	2016 \$'000	%	2015 \$'000	%
Concentration by currency				
USD	2,436,841	56	2,293,297	53
AUD	986,192	23	841,733	20
EURO	129,059	3	214,842	5
SDR	263,468	6	206,302	5
NZD	232,219	5	267,494	6
SGD	154,076	3	155,461	4
STG	194,074	4	310,091	7
SBD	12,261	-	11,629	-
JPY	3	-	3	-
CNY	583	-	-	-
Total financial assets	<u>4,408,776</u>	<u>100</u>	<u>4,300,852</u>	<u>100</u>

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

(c) Credit risk (continued)

Concentration of credit exposure (continued)

	2016		2015	
	\$'000	%	\$000	%
Concentration by sector				
Foreign currency assets				
Central banks	1,226,178	28	1,048,000	24
Commercial banks	2,906,870	66	3,034,921	71
International Monetary Fund	263,467	6	206,302	5
	<u>4,396,515</u>	<u>100</u>	<u>4,289,223</u>	<u>100</u>
Local currency assets				
Solomon Islands Government loan and advances	5,019	41	5,039	43
Staff loan and advances	7,242	59	6,590	57
	<u>12,261</u>	<u>100</u>	<u>11,629</u>	<u>100</u>
Total financial assets	<u>4,408,776</u>		<u>4,300,852</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.

At the reporting date the interest rate profile of the Bank's interest-bearing financial instruments was:

	Carrying amount	
	2016	2015
	\$000	\$000
Fixed rate instruments		
Cash at Bank (Financial assets)	575,273	581,341
Held-to-maturity investments (Financial assets)	2,859,056	3,094,483
Loans and advances (Financial assets)	12,261	11,629
Demand deposits (Financial liabilities)	-	(340,603)
SIG monetary operations account (Financial liabilities)	-	(37,923)
Fixed deposits (Financial liabilities)	(761,658)	(721,677)
	<u>2,684,932</u>	<u>2,587,250</u>
Variable rate instruments		
Cash at Bank (Financial assets)	267,896	192,180
International Monetary Fund (Financial assets)	37,944	93,243
International Monetary Fund (Financial liabilities)	(107,430)	(107,714)
	<u>198,410</u>	<u>177,709</u>

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

(d) Market risk (continued)

Interest rate risk management (continued)

Fair value sensitivity analysis for fixed instruments

The Bank does not account for any fixed rate financial assets and liabilities at fair value through profit and loss. Therefore a change in interest rates at the reporting date would not affect the profit or loss.

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points (bp) in interest rates at the reporting date would have increased (decreased) equity and the profit or loss by amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

	Profit or loss	
	100bp increase	100bp decrease
31 December 2016	\$000's	\$000's
Variable rate instruments	<u>1,984</u>	<u>(1,984)</u>
31 December 2015		
Variable rate instruments	<u>1,777</u>	<u>(1,777)</u>

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.

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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23. Financial risk and management policies (continued)

(d) Market risk (continued)

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

2016 foreign currency risk

Foreign currency financial asset	USD \$000	NZD \$000	AUD \$000	EURO \$000	STG \$000	Others \$000	Total \$000
Money on demand	575,273	-	267,313	129,059	76,300	587	1,048,532
Fixed Term deposit	1,636,108	232,219	540,650	-	117,773	154,076	2,680,826
Holding on Special drawing rights	-	-	-	-	-	37,944	37,944
Reserve Tranche	-	-	-	-	-	34,155	34,155
Subscription	-	-	-	-	-	191,368	191,368
Gold Investment	225,460	-	-	-	-	-	225,460
Bonds	-	-	120,238	-	-	-	120,238
Short term commercial paper	-	-	57,990	-	-	-	57,990
Total	2,436,841	232,219	986,191	129,059	194,073	418,130	4,396,513
Foreign currency financial liability							
Demand deposits	59,202	-	-	-	-	-	59,202
IMF standby credit facility	-	-	-	-	-	73,069	73,069
IMF Special drawing rights allocation	-	-	-	-	-	109,918	109,918
IMF extended credit facility	-	-	-	-	-	11,537	11,537
IMF securities	-	-	-	-	-	190,895	190,895
Capital subscription	-	-	-	-	-	4,929	4,929
Total	59,202	-	-	-	-	390,348	449,550
Net foreign currency asset	2,377,639	232,219	986,191	129,059	194,073	27,782	3,946,963

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
For the year ended 31 December 2016

23. Financial risk and management policies (continued)

(d) Market risk (continued)

2015 foreign currency risk

Foreign currency financial asset	USD \$000	NZD \$000	AUD \$000	EURO \$000	SGD \$000	Others \$000	Total \$000
Money on demand	581,342	-	41,067	151,112	7,993	3	781,517
Fixed Term deposit	1,505,034	267,494	534,183	63,730	302,098	155,461	2,828,000
Holding on Special drawing rights	-	-	-	-	-	93,243	93,243
Reserve Tranche	-	-	-	-	-	5,981	5,981
Subscription	-	-	-	-	-	107,078	107,078
Gold Investment	206,921	-	-	-	-	-	206,921
Bonds	-	-	91,189	-	-	-	91,189
Short term commercial paper	-	-	175,294	-	-	-	175,294
Total	2,293,297	267,494	841,733	214,842	310,091	361,766	4,289,223
Foreign currency financial liability							
Demand deposits	16,240	-	-	-	-	-	16,240
IMF standby credit facility	-	-	-	-	-	101,753	101,753
IMF Special drawing rights allocation	-	-	-	-	-	107,714	107,714
IMF extended credit facility	-	-	-	-	-	8,076	8,076
IMF securities	-	-	-	-	-	102,389	102,389
Capital subscription	-	-	-	-	-	4,716	4,716
Total	16,240	-	-	-	-	324,648	340,888
Net foreign currency asset	2,277,057	267,494	841,733	214,842	310,091	37,118	3,948,335

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 2016:

Central Bank of Solomon Islands
Notes to and forming part of the financial statements
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23. Financial risk and management policies (continued)

(d) Market risk (continued)

	2016		2015	
	(\$000)	%	(\$000)	%
USD	2,377,639	58	2,277,057	56
AUD	986,191	24	841,733	21
EURO	129,059	3	214,842	5
NZD	232,219	6	267,494	7
SGD	154,076	4	155,461	4
STG	194,073	5	310,091	8
JPY	3	-	3	-
CNY	583	-	-	-
	4,073,843	100	4,066,681	100

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

	2016	2015
AUD	0.1717	0.1701
USD	0.1236	0.1240
NZD	0.1780	0.1810
STG	0.1010	0.0837
EURO	0.1182	0.1135
JPY	14,4836	14,9382
SGD	0.1792	0.1753
SDR	0.0922	0.0920
CNY	0.8594	

Sensitivity to foreign exchange rate risk

Impact of a:	2016	2015
	\$M	\$M
Change in profit/equity due to a 2 per cent appreciation in the reserves - weighted value of the Solomon Islands dollar	82	(78)
Change in profit/equity due to a 2 per cent depreciation in the reserves - weighted value of the Solomon Islands dollar	(78)	80

(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.

Operational 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 operational risk.

Central Bank of Solomon Islands
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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 organised 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.

If the inputs used to measure the fair value of an asset might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

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

31 December 2016	Note	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
<i>Investment securities</i>					
Available for sale financial assets (Gold)	6	225,460			225,460
Investment Property	10			13,262	13,262
31 December 2015	Note	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
<i>Investment securities</i>					
Available for sale financial assets (Gold)	6	206,921			206,921
Investment Property	10			13,262	13,262
Property, plant and equipment (only land & buildings)	12			140,957	140,957

Refer to note 10 and note 12 which shows a reconciliation from the opening balances to the closing balances for the Level 3 fair values above.

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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 (Deputy Governor)
 Harry Kuma
 Thomas Ko Chan
 Loyley Ngira (contract end on 5 February 2016)
 Lily Lomulo (contract end on 5 February 2016)
 John Usuramo
 Tele Burtilet (contract end on 17 July 2016)
 Primo Afeau (contract end on 17 July 2016)
 David Quan (appointed on 17 August 2016)
 Leslie Teama (appointed on 17 August 2016)

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 contracts of the Governor and Deputy Governor are subject to mid-term review by the Minister of Finance and annually in accordance with Bank policy. 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
Luke Forau	Advisor to Governors
Ali Homelo	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:

	2016	2015
	\$000	\$000
Short-term employee benefits	2,647	2,568
Long-term benefits	1,120	785
	<u>3,767</u>	<u>3,353</u>

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25. Related parties (continued)

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

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

As at 31 December 2016 loans by the Bank to key management personnel are as follows:

	2016 \$000	2015 \$000
Housing loan	1,631	1,494
Personal loan	59	62
Management car loan	180	126
	<u>1,870</u>	<u>1,682</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 \$nil (2015: \$1.3m) of interest income relating to their investments in Government securities. The Bank also paid \$0.3 million (2015: \$8.3m) 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 \$4.9 million (2015: \$4.9m).

26. Commitments and contingent liabilities

The Bank has guaranteed staff housing loans with the commercial banks to the sum of \$0.79 million as at 31 December 2016 (2015: \$0.79m). The guarantee scheme was no longer available 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 2016, a total of 5 (2015: 64) loans with a net guarantee of \$0.678m (2015: \$5.53m) 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.