

Bank of South Pacific Limited and Subsidiaries

Financial Statements

For the year ended

31 December 2013



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Directors' Report

for the Year Ended 31 December 2013

The Directors take pleasure in presenting the Financial Statements of the Bank of South Pacific Limited and its subsidiaries (Bank and the Group) for the year ended 31 December 2013. In order to comply with the provision of the Companies Act 1997, the directors report as follows:

Principal activities

The principal activity of the Bank of South Pacific Limited (BSP) is the provision of commercial banking and finance services. The Group's activities includes the provision of commercial banking and finance services, stock broking and fund management and life business services throughout Papua New Guinea and the Pacific region. BSP is a Bank listed on the Port Moresby Stock Exchange (POMSoX), incorporated under the Companies Act of Papua New Guinea, and is an authorised Bank under the Banks and Financial Institutions Act of Papua New Guinea. The Bank and the Group are licensed to operate in Solomon Islands, Fiji and Niue. The registered office is at Douglas Street, Port Moresby.

Review of operations

For the year ended 31 December 2013, the Bank's profit after tax was K424.762 million (2012: K399.588 million). The Group's profit after tax was K436.828 million (2012: K407.744 million).

Dividends

Dividend payments totaling K271.686 million were paid in 2013 (2012: K258.994 million). A detailed breakup of this is provided in note 23.

Directors and officers

The following were directors of the Bank of South Pacific Limited at the year ended 31 December 2013:

Mr. K Constantinou, OBE	Mr R Fleming	Mr. G Robb, OAM
Mr. G Aopi, CBE	Mr. T E Fox, OBE	Ms. F Talao
Sir. N Bogan	Mr. C C Procter	Dr. I Temu
Mr E B Gangloff		

Details of directors' tenure and directors and executives' remuneration during the year are provided in Note 27 of the Notes to the Consolidated Financial Statements. Mr Ernest B Gangloff was appointed to the board on 28 November 2013. The CEO Robin Fleming remains the only executive director in the composition of the board.

The company secretary is Mary Johns.

Independent Audit Report

The financial statements have been audited and should be read in conjunction with the independent audit report on page 50. Details of amounts paid to the auditors for audit and other services are shown in Note 41 of the Notes to the Financial Statements.

Donations

Donations and sponsorship by the Group during the year amounted to K9,267,141 (2012: K4,192,404).

Directors' Report

for the Year Ended 31 December 2013

Interests Register

Transactions recorded in the Interests Register are disclosed in Note 30 of the Notes to the Financial Statements.

Change in accounting policies

No changes in accounting policies occurred during the year.

For, and on behalf of, the Directors.

Dated and Signed in accordance with a resolution of the Directors in Port Moresby this 26th day of March 2014.


Kostas Constantinou, OBE
Chairman
Robin Fleming
Group Chief Executive Officer/Director

Statement by the Director

for the Year Ended 31 December 2013

The directors declare that:

- (a) in the Directors' opinion, there are reasonable grounds to believe that the Bank and the Group will be able to pay their debts as and when they become due and payable; and
- (b) in the Directors' opinion, the attached financial statements and notes thereto are in accordance with the PNG Companies Act 1997, including compliance with accounting standards and give a true and fair view of the financial position and performance of the Bank and the Group.

Additional Statutory Information

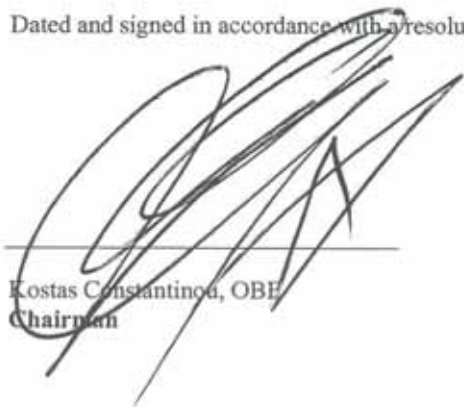
The results of the Bank and the Group's operations during the financial year have, in the opinion of the Directors, not been materially affected by items of an abnormal nature, other than those disclosed in the financial statements.

In the opinion of the Directors, no circumstances have arisen that make adherence to the existing method of valuation of assets or liabilities of the Bank and the Group misleading or inappropriate.

At the date of this report the Directors are not aware of any circumstances that would render the values attributed to current assets in the financial statements misleading.

No contingent liability other than that disclosed in the notes to the attached financial statements has become enforceable, or is likely to become enforceable, within a period of twelve months from the date of this report, that will materially affect the Bank and the Group in its ability to meet obligations as and when they fall due.

Dated and signed in accordance with a resolution of the directors at Port Moresby this 26th day of March 2014.


Kostas Constantinou, OBE
Chairman
Robin Fleming
Group Chief Executive Officer/Director

Statement of Comprehensive Income

for the Year Ended 31 December 2013

	Note	Consolidated		Bank	
		2013	2012	2013	2012
<i>All amounts are expressed in K'000</i>					
Interest income	2	794,807	743,086	793,877	743,145
Interest expense	2	(53,950)	(61,532)	(53,474)	(61,619)
Net interest income		740,857	681,554	740,403	681,526
Banking fee and commission income	3	285,594	253,869	281,028	251,462
Other banking income	4	400,176	273,178	400,311	273,849
Net banking operating income		1,426,627	1,208,601	1,421,742	1,206,837
Net insurance premium income		179,313	144,823	-	-
Increase (decrease) in policy liabilities		(22,025)	(20,347)	-	-
Claims, surrender and maturities		(61,841)	(47,742)	-	-
Net insurance operating income		95,447	76,734	-	-
Total net operating income before impairment and operating expenses		1,522,074	1,285,335	1,421,742	1,206,837
Impairment expense	13	(78,573)	(70,952)	(78,573)	(70,952)
Impairment of subsidiary	8	(14,967)	-	(14,967)	-
Operating expenses	5	(833,849)	(680,257)	(735,326)	(600,448)
Profit before income tax		594,685	534,126	592,876	535,437
Income tax expense	6	(170,127)	(137,552)	(168,114)	(135,849)
Net profit after income tax		424,558	396,574	424,762	399,588
Non-controlling interests	9	12,270	11,170	-	-
Net profit for the year		436,828	407,744	424,762	399,588
Other comprehensive income					
Exchange difference on translation of foreign operations	24	(4,133)	3,487	(6,741)	(1,053)
Net value gain on revaluation of share options	24	(4,526)	1,288	(4,526)	1,289
Net movement in asset revaluation	24	-	9,810	-	9,810
Other comprehensive income for the year, net of tax		(8,659)	14,585	(11,267)	10,046
Total comprehensive income for the year		428,169	422,329	413,495	409,634
Earnings per share – basic & diluted (toea)	23	93.1	86.9	90.5	85.2

The attached notes form an integral part of these financial statements.

Statement of Financial Position

for the year ended at 31 December 2013

<i>All amounts are expressed in K'000</i>	Note	Consolidated		Bank	
		2013	2012	2013	2012
ASSETS					
Cash and balances with Central Bank	10	2,030,800	1,806,597	1,992,970	1,764,275
Treasury & Central Bank bills	11	3,283,432	3,237,517	3,283,432	3,237,517
Amounts due from other banks	12	1,445,199	327,563	1,445,199	327,563
Loans and advances to customers	13	5,306,362	4,804,626	5,244,188	4,750,793
Property, plant and equipment	14	623,360	744,292	589,623	718,279
Assets subject to operating lease	14	61,505	69,226	61,505	69,226
Other financial assets	16	2,170,798	1,557,950	1,924,536	1,354,659
Investment in associates and joint ventures	9	116,821	96,441	43,690	43,275
Investment in subsidiaries	8	-	-	96,929	107,377
Intangibles	7	133,399	5,369	133,198	3,126
Investment properties	15	65,429	56,755	-	-
Asset held for sale	15	-	3,706	-	-
Deferred tax assets	6	134,372	111,141	127,151	110,401
Other assets	17	437,313	511,919	381,737	434,107
Total assets		15,808,790	13,333,102	15,324,158	12,920,598
LIABILITIES					
Amounts due to other banks	18	786,035	72,775	786,035	90,828
Amounts due to customers	19	12,200,999	10,860,522	12,296,226	10,920,691
Subordinated debt securities	20	75,525	75,525	75,525	75,525
Other liabilities	21	936,369	714,735	435,124	285,157
Provision for income tax	6	33,395	13,112	33,222	13,022
Deferred tax liabilities	6	47,370	34,560	38,698	28,358
Other provisions	22	110,037	95,980	105,016	91,198
Total liabilities		14,189,730	11,867,209	13,769,846	11,504,779
SHAREHOLDERS EQUITY					
Ordinary shares	23	381,498	384,814	381,498	384,814
Retained earnings	24	1,035,290	870,148	991,368	838,292
Other reserves	24	202,272	210,931	181,446	192,713
Total shareholders' equity		1,619,060	1,465,893	1,554,312	1,415,819
Total equity and liabilities		15,808,790	13,333,102	15,324,158	12,920,598

The attached notes form an integral part of these financial statements.

Statement of Changes in Shareholders' Equity

for the year ended at 31 December 2013

Bank	Notes	Share capital	Assigned Capital	Reserves	Retained earnings	Total
<i>All amounts are expressed in K'000</i>						
Balance as at 1 January 2012	23 & 24	426,444	24,883	250,579	697,698	1,399,604
Net profit	24	-	-	-	399,588	399,588
Dividend paid	23	-	-	-	(258,994)	(258,994)
Elimination of Fiji Bank Investment	23	-	(24,883)	(67,912)	-	(92,795)
Share buyback	23	(41,630)	-	-	-	(41,630)
Other comprehensive income		-	-	10,046	-	10,046
Balance at 31 December 2012	23 & 24	384,814	-	192,713	838,292	1,415,819
Net profit	24	-	-	-	424,762	424,762
Final dividend paid for 2012	23	-	-	-	(178,001)	(178,001)
Interim dividend for 2013	23	-	-	-	(93,685)	(93,685)
Share buyback	23	(3,316)	-	-	-	(3,316)
Other comprehensive income		-	-	(11,267)	-	(11,267)
Balance at 31 December 2013	23 & 24	381,498	-	181,446	991,368	1,554,312
Group						
Balance as at 1 January 2012	23 & 24	426,444	-	196,346	721,398	1,344,188
Net profit	24	-	-	-	407,744	407,744
Dividend paid	23	-	-	-	(258,994)	(258,994)
Share buyback	23	(41,630)	-	-	-	(41,630)
Other comprehensive income		-	-	14,585	-	14,585
Balance at 31 December 2012	23 & 24	384,814	-	210,931	870,148	1,465,893
Net profit	24	-	-	-	436,828	436,828
Final dividend paid for 2012	23	-	-	-	(178,001)	(178,001)
Interim dividend for 2013	23	-	-	-	(93,685)	(93,685)
Share buyback	23	(3,316)	-	-	-	(3,316)
Other comprehensive income		-	-	(8,659)	-	(8,659)
Balance at 31 December 2013	23 & 24	381,498	-	202,272	1,035,290	1,619,060

The attached notes form an integral part of these financial statements

Statement of Cash Flow

for the year ended 31 December 2013

All amounts are expressed in K'000	Notes	Consolidated		Bank	
		2013	2012	2013	2012
CASH FLOW FROM OPERATING ACTIVITIES					
Interest received		793,338	740,819	792,272	739,443
Fees and other income		824,729	638,579	680,650	524,618
Interest paid		(64,232)	(71,974)	(63,615)	(70,626)
Amounts paid to suppliers and employees		(653,712)	(565,607)	(489,745)	(452,221)
Operating cash flow before changes in operating assets	28	900,123	741,817	919,562	741,214
Increase in loans		(558,746)	(571,582)	(571,969)	(585,771)
Decrease/(increase) in bills receivable and other assets		8,361	(257,224)	13,532	(239,171)
Increase in deposits		1,280,731	1,465,780	1,375,536	1,474,302
Increase in bills payable and other liabilities		189,562	57,261	147,016	57,377
Net cash flow from operations before income tax		1,820,031	1,436,052	1,883,677	1,447,951
Income taxes paid		(156,953)	(238,675)	(156,634)	(233,720)
Net cash flow from operating activities		1,663,078	1,197,377	1,727,043	1,214,231
CASH FLOW FROM INVESTING ACTIVITIES					
Decrease/(decrease) for government securities		(599,553)	(70,246)	(615,794)	(6,965)
Expenditure on property, plant & equipment		(212,647)	(218,027)	(203,484)	(213,096)
Proceeds from disposal of property, plant & equipment		7,760	3,822	7,615	3,818
Proceeds from other investments		34,653	25,215	-	-
Proceeds from share trading activities		3,446	8,252	-	-
Net cash flow from investing activities		(766,341)	(250,984)	(811,663)	(216,243)
CASH FLOW FROM FINANCING ACTIVITIES					
Share buyback	23	(3,316)	(41,630)	(3,316)	(41,630)
Client management trust		(3,902)	(7,243)	-	-
Dividends paid	23	(271,686)	(258,994)	(271,686)	(258,994)
Net cash flow from financing activities		(278,904)	(307,867)	(275,002)	(300,624)
Net Increase/(decrease) in cash and cash equivalents		617,833	638,526	640,378	697,364
Effect of exchange rate movements on cash and cash equivalents		10,746	(710)	10,746	(710)
Cash and cash equivalents at the beginning of the year		2,061,385	1,423,569	2,001,010	1,304,356
Cash and Cash Equivalents at the end of the year	28	2,689,964	2,061,385	2,652,134	2,001,010

The attached notes form an integral part of these financial statements

Notes to the Financial Statements

for the year ended 31 December 2013

1. Accounting Policies

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below:

A. Basis of presentation and general accounting policies

The consolidated financial statements of the Bank of South Pacific Limited (the Bank) and the Group are prepared in accordance with International Financial Reporting Standards and interpretations of these standards issued by the International Financial Reporting Interpretations Committee. They are prepared on the basis of the historical cost convention, as modified by the revaluation of certain non-current assets and financial instruments.

Estimates and assumptions have been used to achieve conformity with generally accepted accounting principles in the preparation of these consolidated financial statements. These assumptions and estimates affect balances of assets and liabilities, contingent liabilities and commitments at the end of the reporting period, and amounts of revenues and expenses during the reporting period. Whilst the estimates are based on management's best knowledge of current events and conditions, actual results may ultimately differ from those estimates.

There are no new standards and interpretations being adopted in these financial statements.

The consolidated financial statements are presented in Papua New Guinea Kina, expressed in thousands of Kina.

B. Consolidation

The consolidated financial statements incorporate the assets and liabilities of all controlled entities of the Bank and the Group as at 31 December 2013, and their results for the year then ended.

Controlled entities are those over which the Group has the power to govern financial and operating policies, generally accompanied by a shareholding that commands the majority of voting rights, and are commonly referred to as subsidiaries.

Subsidiaries are accounted for at acquisition under the acquisition method of accounting, where:

- acquisition cost is measured at fair value of assets transferred, equity issued, liabilities assumed and any directly attributable costs of the transaction;
- identifiable net assets are recorded initially at acquisition, at their fair values;
- any excess of the acquisition cost over the relevant share of identifiable net assets acquired is treated as goodwill, and any deficiency is recognised directly in the statement of comprehensive income;
- All intercompany transactions and balances are eliminated.

C. Investment in Associates and joint ventures

Investments in Associates

Associates are entities over which the Group has significant, but not controlling influence, generally accompanied by a shareholding of between 20% - 50% of voting rights.

In the consolidated financial statements, these investments are accounted for under the equity method, where:

- The investment is initially recognised at cost;
- The Group's share of profits or losses are recognised in the statement of comprehensive income.

Interests In Joint Ventures

A joint venture is a contractual arrangement whereby the bank together with other parties undertake an economic activity that is subject to joint control that is when the strategic financial and operating policy decisions relating to the activities require the unanimous consent of the parties sharing control. Joint venture arrangements that involve the establishment of a separate entity in which each venture has an interest are referred to as jointly controlled entities.

Where the Group undertakes its activities under joint venture arrangements directly, the Group's share of jointly controlled assets and any liabilities incurred jointly with other ventures are recognised in the financial statements of the jointly controlled entity. The Group reports its interests in jointly controlled entities at cost, except when the investment is classified as held for sale, in which case it is accounted for under IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

Notes to the Financial Statements

for the year ended 31 December 2013

D. Revenue

Interest income and expense

Interest income and expense are recognized in the statement of comprehensive income on an accrual basis using the effective yield method. The income arising from the various forms of installment credit has been determined using the effective interest method.

Interest income includes coupons earned on inscribed stock, accrued discount and premium on Treasury and Central Bank bills.

Short term insurance contracts

These contracts are the Term Life, Medical and Travel policies sold and underwritten by BSP Health Care (Fiji) Limited.

These contracts protect the Group's customers from the consequences of events such as death, medical emergency or loss on travel. Guaranteed benefits paid on occurrence of the specified insurance event are either fixed or linked to the extent of the economic loss suffered by the policyholder. There are no maturity or surrender benefits.

For all these contracts, premiums are recognised as revenue (earned premiums) proportionally over the period of coverage. The portion of premium received on in-force contracts that relates to unexpired risks at the Balance Sheet date is reported as the unearned premium liability. Premiums are shown before deduction of commission.

Claims and loss adjustment expenses are charged to income as incurred based on the estimated liability for compensation owed to contract holders or beneficiary. They include direct and indirect claims settlement costs and arise from events that have occurred up to the Balance Sheet date even if they have not yet been reported to the Group. The Group does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are estimated using the input of assessments for individual cases reported to the Group and statistical analyses for the claims incurred but not reported, and to estimate the expected ultimate cost of more complex claims that may be affected by external factors (such as court decisions).

Long term insurance contracts

These contracts insure human life events (for example death or survival) over a long duration. They protect the Group's customers from the consequences of events such as death, disability or critical illness. Guaranteed benefits paid on occurrence of the specified insurance event are fixed or linked to the level of bonus declared to the contract holder. Most of the policies have maturity and surrender benefits.

For all these contracts, premiums are recognised as revenue when they become payable by the contract holder. Premiums are shown before deduction of commission.

Approximately 90% of the above contracts in the Group's portfolio contain a Discretionary Participation Feature (DPF). This feature entitles the holder to receive, as a supplement to generated benefits, additional benefits or bonuses.

The liability for long term insurance contracts (principally Life Insurance) has been determined in accordance with LPS 1.04 Valuation of Policy Liabilities, issued by the Australian Prudential Regulation Authority.

The policy liability is calculated in a way that allows for the systematic release of planned profit margins as services are provided to policy owners and the revenues relating to those services are received (Margin on Services methodology). Services used to determine profit recognition include the cost of expected insurance claims and the allocation of future bonuses. The liability is generally determined as the present value of all future expected payments, expenses, taxes and profit margins reduced by the present value of all future expected premiums and take into consideration projected future bonuses. The liabilities are recalculated at each balance date using best estimate assumptions. These assumptions are revisited regularly and adjusted for actual experiences on claims, expense, mortality and investment returns.

Notes to the Financial Statements

for the year ended 31 December 2013

E. Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. All other risk related fees that constitute cost recovery are taken to income when levied. Non-refundable front-end loan fees are capitalized and deferred over the expected term of the financial instrument.

F. Borrowing expenses

Expenses associated with the borrowing of funds are charged to the statement of comprehensive income in the period in which they are incurred.

G. Loans and provisions for loan impairment

Loans are originated by providing funds directly to the borrower and are recognised when cash is advanced to borrowers.

All loans and advances receivable are subject to continuous management review. A specific provision for loan impairment is established if there is objective evidence that the Bank and the Group will not be able to collect all amounts due under the terms of loans. The amount of the provision approximates the difference between the carrying amount and the recoverable amount, which is the current best estimate of the present value of expected future cash flows arising from the asset. All bad debts are written off against the specific provision for loan impairment in the period in which they are classified as irrecoverable. Subsequent recoveries are credited to the provision for loan losses in the statement of comprehensive income.

General provisions for impairment are maintained to cover incurred losses unidentified at balance date in the overall portfolio of loans and advances. The provisions are determined having regard to the level of risk weighted assets, economic conditions, the general risk profile of the credit portfolio, past loss experience and a range of other criteria. The amount necessary to bring the provisions to their assessed levels, after write-offs, is charged to the statement of comprehensive income.

H. Goodwill

Goodwill represents the excess of the cost of any acquisition over the acquirer's interest in the fair value of the identifiable assets and liabilities acquired as at the exchange transaction. Goodwill is reported in the statement of financial position as an intangible asset.

In determining the estimated useful life of goodwill, management considers various factors including net selling price of the acquired business, existing market share, potential growth opportunities, and other factors inherent in the acquired business. This assessment is reviewed at each balance date, so that any indication of impairment with implications for the recoverability of goodwill can be tested, and adjustments to the carrying value of goodwill made if necessary.

I. Computer systems development costs

Costs incurred to develop and enhance the Bank and the Group's computer systems are capitalised to the extent that benefits do not relate solely to revenue that has already been brought to account and will contribute to the future earning capacity of the economic entity. These costs are amortised over the estimated economic life of four years using the straight-line method. Costs associated with maintaining computer software programs are recognised as an expense when incurred.

Notes to the Financial Statements

for the year ended 31 December 2013

J. Property, plant and equipment

Land and buildings are measured at fair value. Fair value is determined on the basis of regular independent valuation prepared by external valuation experts, based on discounted cash flows or capitalisation of net income (as appropriate). The fair values are recognised in the consolidated financial statements of the consolidated entity, and are reviewed at the end of each reporting period to ensure that the carrying value of land and buildings is not materially different from their fair values.

Any revaluation increase arising on the revaluation of land and buildings is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in profit or loss, in which case the increase is credited to the statement of comprehensive income to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of land and buildings is charged as an expense in statement of comprehensive income to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset.

Depreciation on revalued buildings is charged to statement of comprehensive income. On the subsequent sale or retirement of a revalued property, the attributable revaluation surplus remaining in the asset revaluation reserve, net of any related deferred taxes, is transferred directly to retained earnings.

Depreciation is provided on property, plant and equipment, including freehold buildings but excluding land. Depreciation is calculated on a straight line basis so as to write off the net cost or other revalued amount of each asset over its expected useful life to its estimated residual value. Leasehold improvements are depreciated over the period of the lease or estimated useful life, whichever is the shorter, using the straight line method. The estimated useful life, residual values and depreciation method is reviewed at the end of each annual reporting period.

The following basis and method of depreciation is used:

Class of asset	Method	Rate
Property (excluding land)	Straight-line basis	2 - 3% pa
Plant & equipment	Straight-line basis	10 - 25% pa
Equipment under operating lease	Straight-line basis	6 - 20% pa

Gains or losses on disposals (being the difference between the carrying value at the time of sale or disposal and the proceeds received) are taken into account in determining operating profit for the year. Where the carrying value of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Repairs and maintenance are taken into account in determining operating profit when the expenditure is incurred.

K. Leases

Bank is lessee

All leases entered into by the Bank and the Group are operating leases. Total payments made are charged to the statement of comprehensive income reflecting the pattern of benefits derived from the leased assets.

Bank is lessor

Finance leases are included in Loans and Advances to Customers and are accounted for under the finance method whereby income is taken to account over the life of the lease in proportion to the outstanding investment balance.

Assets subject to operating leases are separately disclosed in the statement of financial position, according to the nature of the asset. These assets are stated at cost less accumulated depreciation. The assets are depreciated on a straight line basis over the life of the operating lease. Lease income is recognised on a straight line basis over the term of the lease.

L. Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise notes and coins, and balances due to and from other banks.

Notes to the Financial Statements

for the year ended 31 December 2013

M. Provisions

Provisions are recognised when the Bank and the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Bank and the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

N. Employee benefits

A liability is required for benefits accruing to employees in respect of wages and salaries, annual leave, and long service leave when it is probable that settlement will be required and the liabilities are capable of being measured reliably.

Liabilities recognised in respect of 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.

Liabilities recognised in respect of employee benefits which are not expected to be settled within 12 months are measured as the present value of the estimated future cash outflows to be made by the consolidated entity in respect of services provided by employees up to reporting date.

Employment benefits - defined contribution plans

A defined contribution plan is a pension plan under which the Bank and the Group pays fixed contributions into a separate fund, and there is no recourse to the Bank and the Group for employees if the fund has insufficient assets to pay employee benefits relating to service up to the balance sheet date.

The Bank and the Group pays contributions to publicly or privately administered superannuation plans on a mandatory, contractual or voluntary basis in respect of services rendered up to balance sheet date by all citizen staff members. The contributions are at the current rate of employees' gross salary. Once the contributions have been paid, the Bank and the Group have no further payment obligations for post-employment benefits from the date an employee ceases employment with the Bank and the Group.

O. Income tax

Current Tax

Current tax is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or tax loss for the period. It is calculated using tax rates and tax laws that have been enacted or substantively enacted by reporting date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred tax

Deferred tax is accounted for using the balance sheet liability method. Temporary differences are differences between the tax base of an asset or liability and its carrying amount in the statement of financial position. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

In principle, deferred tax liabilities are recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that sufficient taxable amounts will be available against which deductible temporary differences or unused tax losses and tax offsets can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences giving rise to them arise from the initial recognition of assets and liabilities which affects neither taxable income nor accounting profit.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period(s) when the asset and liability giving rise to them are realised or settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Bank and the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities. Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Bank and the Group intends to settle its current tax assets and liabilities on a net basis

Notes to the Financial Statements

for the year ended 31 December 2013

O. Income tax (continued)

Current and deferred tax for the period

Current and deferred tax is recognised as an expense or income in the statement of comprehensive income, except when it relates to items credited or debited directly to equity, in which case the deferred tax is also recognised directly in equity.

P. Investments

Investments are classified into the following categories: held for trading, held-to-maturity and available-for-sale. Trading reflects active and frequent buying and selling, and financial instruments held for trading generally are used with the objective of generating a profit from short-term fluctuations in price or dealers margin. Investments with fixed maturity that the management has the intent and ability to hold to maturity are classified as held-to-maturity. Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; Management determines the appropriate classification of its investments at the time of the purchase.

All purchases and sales of investments are recognised on the trade date, which is the date that the Bank and the Group commits to purchase or sell the asset. Cost of purchase includes transaction costs. Trading and available-for-sale investments are subsequently carried at fair value, whilst held-to-maturity investments are carried at amortised cost using the effective yield method. Realised and unrealised gains and losses arising from changes in the fair value of trading investments are included in the statement of comprehensive income in the period in which they arise.

Q. Foreign currency

The consolidated financial statements of the Bank and the Group are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of these consolidated financial statements, the results and financial position of the Bank are expressed in Papua New Guinea kina, which is the Bank's functional and presentation currency.

In preparing the consolidated financial statements, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Foreign operations

On consolidation, the assets and liabilities of the consolidated entity's overseas operations are translated at exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly. Exchange differences arising, if any, are recognised in the foreign currency translation reserve, and recognised in profit or loss on disposal of the foreign operation.

R. Share capital

Share issue costs

External costs directly attributable to the issue of new shares are deducted from equity net of any related income taxes.

Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are declared.

Dividends for the year, declared after the balance sheet date, are dealt with in the subsequent events note.

Notes to the Financial Statements

for the year ended 31 December 2013

R. Share capital (continued)

Share options

The fair value of the employee services received in exchange for the grant of options is recognised as an expense. The total amount to be expected rateably over the vesting period is determined by reference to the fair value of the options determined at the grant date, excluding the impact of any non-market vesting conditions (for example profitability). Non-market conditions are included in assumptions about the number of options expected to become exercisable or the number of shares that the employee will ultimately receive.

The estimate is revised at each balance sheet date and the difference is charged or credited to the statement of comprehensive income, with a corresponding adjustment to equity. The proceeds received on exercise of the options net of any directly attributable transactions costs are credited to equity.

S. Asset impairment

At each reporting date, the Bank and the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Bank and the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Goodwill, intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually and whenever there is an indication that the asset may be impaired. An impairment of goodwill is not subsequently reversed.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the reversal of the impairment loss is treated as a revaluation increase.

T. Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured, with certain exceptions, at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the asset (or disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for such a sale and the sale is highly probable. The sale of the asset (or disposal group) must be expected to be completed within one year from the date of classification, except in the circumstances where sale is delayed by events or circumstances outside the Company's control and the Company remains committed to a sale.

Notes to the Financial Statements

for the year ended 31 December 2013

U. Convertible notes

Convertible notes issued by the company are regarded as compound instruments, consisting of a liability component equivalent to the 3 year fixed coupon amount and an equity component equivalent to the balance. At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for similar non-convertible debt. The difference between the proceeds of issue of the convertible loan notes and the fair value assigned to the liability component, representing the embedded option to convert the liability into equity of the company, is included in equity.

The interest expense on the liability component is calculated by applying the coupon rate of 7% to the liability component of the instrument. The difference between this amount and the interest paid is added to the carrying amount of the convertible notes.

V. Derivative financial instruments and acceptances

Forward foreign exchange contracts entered into for trading purposes are initially recognized at cost and subsequently re-measured at fair value based upon the forward rate. Gains and losses on such contracts are taken to the statement of comprehensive income.

Acceptances comprise undertakings by the Bank and the Group to pay bills of exchange drawn on customers. The Bank and the Group expects most acceptances to be settled simultaneously with the reimbursement from the customers. Customer acceptances are accounted for as off-balance sheet transactions and are disclosed as contingent liabilities and commitments.

The Bank and the Group does not actively enter into or trade in complex forms of derivative financial instruments such as currency and interest rate swaps and options.

The Bank and the Group does not have any financial instruments measured at level 1 and 3 and there were no transfers between 1, 2 and 3 during the financial year.

W. Comparatives

Comparative figures have been adjusted to conform to changes in presentation in the current year.

- Computer development costs has been moved to intangibles category from other assets category. Refer to note 7 (b).
- Elimination of the Fiji bank investment and the related assigned capital and capital adequacy reserve.

Investment in Subsidiary 2012	215,517
Elimination of Fiji Bank Branch investment entries	
- Assigned capital	(24,883)
- Capital adequacy reserve	(67,912)
- Colonial Bank assigned capital	(21,456)
	101,266
Transfer projects costs from other assets to investment	6,111
Adjusted balance for investment in subsidiary in 2012	107,377

Notes to the Financial Statements

for the year ended 31 December 2013

2. Net interest income

	Consolidated		Bank	
<i>All amounts are expressed in K'000</i>	2013	2012	2013	2012
Interest income				
Cash and short term funds	8,184	6,417	8,184	6,417
Treasury bills	47,176	53,759	47,176	53,759
Central Bank Bills	27,850	56,095	27,850	56,095
Inscribed stock	140,195	127,412	140,195	127,412
Loans and advances	569,262	496,988	568,332	497,047
Other	2,140	2,415	2,140	2,415
	794,807	743,086	793,877	743,145
Less:				
Interest expense				
Customer deposits	32,054	44,606	31,578	44,693
Other banks	13,589	8,547	13,589	8,547
Subordinated debt securities	8,307	8,330	8,307	8,330
Other borrowings	-	49	-	49
	53,950	61,532	53,474	61,619
	740,857	681,554	740,403	681,526

3. Banking fee and commission income

Fee and commission income				
Credit related	73,263	67,808	73,263	67,808
Trade and international related	13,467	11,894	13,467	11,894
Electronic banking related	46,770	34,505	46,770	34,505
Brokerage and fee income	3,789	2,407	-	-
Other	148,995	138,175	148,218	138,175
	286,284	254,789	281,718	252,382
Less:				
Fee and commission expenses				
Agencies	690	920	690	920
	690	920	690	920
	285,594	253,869	281,028	251,462

Notes to the Financial Statements

for the year ended 31 December 2013

4. Other banking income

	Consolidated		Bank	
<i>All amounts are expressed in K'000</i>	2013	2012	2013	2012
Foreign exchange related	353,463	223,708	353,463	223,708
Other	46,713	49,470	46,848	50,141
	400,176	273,178	400,311	273,849

Included in other income:

Profit/(loss) on sale of fixed assets	(906)	498	(906)	498
Change in fair value of assets held through profit and loss	-	5,922	-	-

Foreign Exchange related income includes gains and losses from spot and forward contracts and translated foreign currency assets.

5. Other operating expenses

Administration	194,455	186,099	129,474	128,217
Auditors remuneration (note 41)	2,707	2,496	2,110	1,423
Computing	39,521	34,983	39,521	34,983
Depreciation	90,817	57,968	86,723	54,806
Amortization of computer development	85,018	25,785	85,018	25,785
Non-executive Directors costs	1,434	1,424	1,224	1,244
Non-lending losses	16,942	15,386	16,942	15,386
Premises and equipment	79,150	55,742	70,730	55,742
	510,044	379,883	431,742	317,586
Staff costs				
Defined contribution plans	10,643	9,348	9,512	8,346
Statutory benefit contributions	10,908	9,334	10,908	9,334
Wages and salaries	227,150	211,490	210,461	197,227
Other	75,104	70,202	72,703	67,955
	323,805	300,374	303,584	282,862
	833,849	680,257	735,326	600,448

Notes to the Financial Statements

for the year ended 31 December 2013

6. Income tax

Income tax expense

All amounts are expressed in K'000

	Consolidated		Bank	
	2013	2012	2013	2012
Current tax	181,261	180,190	180,959	178,622
Deferred tax	(12,599)	(8,970)	(12,341)	(14,936)
Current year	168,662	171,220	168,618	163,686
Income tax under/(over) provided in previous years	1,465	(33,668)	(504)	(27,837)
	170,127	137,552	168,114	135,849
Tax calculated at 30% of profit before tax (2012: 30%)	178,406	160,631	177,863	160,631
Tax calculated at 20% of profit before tax - subsidiary	3,246	2,757	-	-
Expenses not deductible for tax	(13,520)	3,734	(9,245)	3,056
Net insurance income not subject to tax	-	4,098	-	-
Tax losses not recognised	530	-	-	-
Income tax under/(over) provided in previous years	1,465	(33,668)	(504)	(27,838)
	170,127	137,552	168,114	135,849

Provision for income tax

At 1 January	(13,112)	(77,961)	(13,022)	(73,684)
Income tax provision	(181,261)	(180,190)	(180,959)	(178,622)
Previous years over/(under) provided	4,125	6,364	4,125	5,564
Foreign tax paid	216	4,955	-	-
Tax payments made	156,637	233,720	156,634	233,720
At 31 December	(33,395)	(13,112)	(33,222)	(13,022)

Deferred taxes

Specific allowance for losses on loans and advances	11,704	44,912	11,704	44,912
General allowance for losses on loans and advances	71,033	19,504	71,033	19,504
Employee related provisions	18,708	21,573	18,453	15,783
Prepaid expenses	(1,285)	(1,112)	(1,285)	(1,112)
Other provisions	17,085	18,164	16,527	22,052
Depreciation and amortization	(29,234)	(29,952)	(27,033)	(22,588)
Unrealised foreign exchange gains	(10,444)	(4,658)	(10,381)	(4,658)
Deferred expenditure	9,435	8,150	9,435	8,150
	87,002	76,581	88,453	82,043

Notes to the Financial Statements

for the year ended 31 December 2013

6. Income tax (continued)

Represented by:

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Deferred tax asset	134,372	111,141	127,151	110,401
Deferred tax liability	(47,370)	(34,560)	(38,698)	(28,358)
At 31 December	87,002	76,581	88,453	82,043

Movement in deferred tax is reconciled as follows:

<i>All amounts are expressed in K'000</i>		Consolidation			
	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Closing balance
2013					
Gross deferred tax liabilities	(34,560)	(11,412)	(1,398)	-	(47,370)
Gross deferred tax assets	111,141	24,011	(780)	-	134,372
	76,581	12,599	(2,178)	-	87,002
2012					
Gross deferred tax liabilities	(19,028)	(13,046)	-	(2,486)	(34,560)
Gross deferred tax assets	87,625	22,016	1,500	-	111,141
	68,597	8,970	1,500	(2,486)	76,581
<i>All amounts are expressed in K'000</i>		Bank			
2013					
Gross deferred tax liabilities	(28,358)	(11,467)	1,127	-	(38,698)
Gross deferred tax assets	110,401	23,808	(7,058)	-	127,151
	82,043	12,341	(5,931)	-	88,453
2012					
Gross deferred tax liabilities	(18,627)	(7,245)	-	(2,486)	(28,358)
Gross deferred tax assets	87,336	22,181	884	-	110,401
	68,709	14,936	884	(2,486)	82,043

Notes to the Financial Statements

for the year ended 31 December 2013

7. (a) Intangible asset

	Consolidated		Bank	
<i>All amounts are expressed in K'000</i>	2013	2012	2013	2012
Gross carrying amount	201	2,243	-	-
Impairment adjustment	-	-	-	-
	201	2,243	-	-

The Directors have determined that the carrying value of the goodwill arising on consolidation as a result of elimination of BSP investment in its subsidiaries (except for BSP Capital Limited) is considered not materially impaired. These subsidiaries trade on a going concern basis and their normal business operations are not exceptionally impaired.

(b) Computer Development costs

At 1 January 2013	3,126	29,145	3,126	29,145
Additions	208,147	-	208,147	-
Adjustment	6,943	(234)	6,943	(234)
Amortisation expense	(85,018)	(25,785)	(85,018)	(25,785)
At 31 December 2013	133,198	3,126	133,198	3,126
Total Intangible assets	133,399	5,369	133,198	3,126

8. Investment in Subsidiaries

Name of Associates	Principal activity	Place of incorporation and operation, ownership %	2013	2012
BSP Capital Limited	Share brokerage/Fund Management/Capital Raising	PNG 100%	8,959	19,407
BSP Life Limited	Life Insurance	Fiji 100%	87,653	87,653
BSP Convertible Notes Limited	Capital Raising	Fiji 100%	317	317
			96,929	107,377

Provision for the impairment of the Investment in BSP Capital Limited

The directors have determined that the investment in the BSP Capital Limited has been materially impaired as the carrying amount of the investment is greater than the its net book value. As of the reporting date, the investment amount is written down to its net book value. The provision impairment impacts the bank's results but and not the consolidation as a result of elimination upon consolidation.

Opening balance	19,407	19,407
Net movement	4,519	-
Provision for impairment	(14,967)	-
Closing balance	8,959	19,407

Notes to the Financial Statements

for the year ended 31 December 2013

9. Investments in Associates and Joint Ventures

Name of Associates	Principal activity	Place of incorporation and operation	Proportion of ownership and voting power held	
			2013	2012
Suva Central Limited	Property rental	Fiji	50%*	50%*
Richmond Limited	Hotel operation	Fiji	61.3%** , 50%***	61.3%** , 50%***
Williams and Gosling	Freight forwarding	Fiji	27.7%*	27.7%*
Carpark Limited	Property	PNG	33.33%	33.33%
Malagan Limited	Property	PNG	33.33%	33.33%

*both ownership and voting power held, **ownership, ***voting power held.

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Associates				
Investment in associate – equity	53,166	42,394	-	-
Movement	7,464	(398)	-	-
Share of profit for year ended 31 December 2013	12,270	11,170	-	-
Net investment in associate	72,900	53,166	-	-
Summarised financial information of associate:				
Total assets	139,900	119,846	-	-
Total liabilities	(38,418)	(37,244)	-	-
Net assets	101,482	82,602	-	-
Net profit	22,316	18,932	-	-
Share of associate's profit	12,270	11,170	-	-
Joint Ventures				
Shares held in jointly owned entity – at costs	43,921	43,275	43,690	43,275
Total investments in associates and joint ventures	116,821	96,441	43,690	43,275

10. Cash and balances with Central Bank

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Notes, coins and cash at bank	391,639	423,238	353,809	380,916
Balances with Central Bank other than statutory deposit	572,581	510,161	572,581	510,161
Included in cash and cash equivalents	964,220	933,399	926,390	891,077
Statutory deposits with Central Bank	1,066,580	873,198	1,066,580	873,198
	2,030,800	1,806,597	1,992, 970	1,764,275

Notes to the Financial Statements

for the year ended 31 December 2013

11. Treasury and Central Bank bills

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Treasury and Central Bank bills – face value	3,309,115	3,225,565	3,309,115	3,225,565
Premium/(discount) for interest receivable	(25,683)	11,952	(25,683)	11,952
	3,283,432	3,237,517	3,283,432	3,237,517

12. Amounts due from other banks

Items in the course of collection	128,524	35,604	128,524	35,604
Placements with other banks	1,316,675	291,959	1,316,675	291,959
	1,445,199	327,563	1,445,199	327,563

13. Loans and advances to customers

Overdrafts	1,203,238	1,095,419	1,203,237	1,095,419
Lease financing	261,271	224,464	261,271	224,464
Term loans	2,951,144	2,638,291	2,931,168	2,617,631
Mortgages	1,124,777	1,028,791	1,124,300	1,028,000
Policy loans	43,013	38,194	-	-
Gross loans and advances net of reserved interest	5,583,443	5,025,159	5,519,976	4,965,514
Less allowance for losses on loans and advances	(277,081)	(220,533)	(275,788)	(214,721)
	5,306,362	4,804,626	5,244,188	4,750,793

The spread of the loans are detailed in the maturity analysis table on note 34. The loans are well-concentrated across various sectors and regions as analysed on note 33.

Lease financing

The Group and the bank provide finance leases to a broad range of clients to support financing needs in acquiring movable assets such as motor vehicles, aircraft and plant and equipment. Finance lease receivables are included within loans and advances to customers, analysed as follows:

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Gross investment in finance lease receivable				
Not later than 1 year	28,268	27,498	28,268	27,498
Later than 1 year and not later than 5 years	266,429	244,080	266,429	244,080
	294,697	271,578	294,697	271,578
Unearned future finance income				
Not later than 1 year	(11,895)	(719)	(11,895)	(719)
Later than 1 year and not later than 5 years	(21,531)	(46,395)	(21,531)	(46,395)
	(33,426)	(47,114)	(33,426)	(47,114)
Present value of minimum lease payment receivable	261,271	224,464	261,271	224,464

Notes to the Financial Statements

for the year ended 31 December 2013

13. Loans and advances to customers (continued)

Present value of minimum lease payment receivable is analysed as follows:

Not later than 1 year	16,373	26,779	16,373	26,779
Later than 1 year and not later than 5 years	244,898	197,685	244,898	197,685
	261,271	224,464	261,271	224,464

Provision for impairment

Movement in allowance for losses on loans and advances:

Balance at 1 January	220,553	168,072	214,721	162,174
Net new and increase provisioning	69,320	73,752	69,320	73,752
Loans written off against provisions / (Write back of provisions no longer required)	(12,792)	(21,291)	(8,253)	(21,205)
Balance at 31 December	277,081	220,533	275,788	214,721

Provision for impairment is represented by

Collective provision	237,400	174,220	236,776	173,635
Individually assessed or specific provision	39,681	46,313	39,012	41,086
Balance at 31 December	277,081	220,533	275,788	214,721

Loan impairment expense

Net collective provision funding	(57,449)	(65,013)	(57,449)	(65,013)
Net new and increase individually assessed provisioning	(11,871)	(8,739)	(11,871)	(8,739)
Total new and increase provisioning	(69,320)	(73,752)	(69,320)	(73,752)
Recoveries during the year	26,239	21,133	26,239	21,133
Net write back/(write off)	(35,492)	(18,333)	(35,492)	(18,333)
	(78,573)	(70,952)	(78,573)	(70,952)

In determining the potential loss in specific loans, groups of loans, or in the aggregate loan portfolio, all relevant factors have been considered including, but not limited to: current economic conditions, historical loss experience, delinquency trends, the effectiveness of the bank's lending policies and collection procedures, and the timeliness and accuracy of its loan review function in line with the Group Provisioning Policy.

Bank of South Pacific has met the minimum provisioning amounts are to be maintained under Prudential Standard 2/2003 - Asset Classification, provisioning and suspension of interest. At the end of each calendar quarter, or more frequently if warranted, the board of directors has caused management to evaluate the collectability of all loans, including any accrued and unpaid interest in line with Bank of South Pacific's loan policy.

Notes to the Financial Statements

for the year ended 31 December 2013

14. Property, plant and equipment

	Consolidated		Bank	
<i>All amounts are expressed in K'000</i>	2013	2012	2013	2012
Carrying value				
Capital Work in Progress	117,253	325,821	113,744	324,982
Premises	490,704	407,608	465,966	386,707
Accumulated depreciation	(105,509)	(76,888)	(97,875)	(70,004)
Net book value	385,195	330,720	368,091	316,703
Equipment	471,108	361,790	436,168	334,239
Accumulated depreciation	(350,196)	(274,039)	(328,380)	(257,645)
Net book value	120,912	87,751	107,788	76,594
Total net book value	623,360	744,292	589,623	718,279

Reconciliation of carry value of property, plant and equipment is set out below:

Capital WIP

At 1 January 2013	325,821	244,401	324,982	243,498
Additions	171,170	230,398	167,006	221,783
Transfers	(379,738)	(148,978)	(378,244)	(140,299)
At 31 December 2013	117,253	325,821	113,744	324,982

Premises

At 1 January 2013	330,720	296,539	316,703	281,258
Additions	90,489	51,841	86,745	52,634
Disposals	(7,877)	(422)	(7,877)	(422)
Depreciation expense	(28,137)	(17,238)	(27,480)	(16,767)
At 31 December 2013	385,195	330,720	368,091	316,703

Equipment

At 1 January 2013	87,751	81,963	76,594	72,766
Additions	88,909	44,140	83,360	39,177
Disposals	(789)	(5,617)	(644)	(5,305)
Depreciation expense	(54,959)	(32,735)	(51,522)	(30,044)
At 31 December 2013	120,912	87,751	107,788	76,594

Notes to the Financial Statements

for the year ended 31 December 2013

14. Property, plant and equipment (continued)

	Consolidated		Bank	
<i>All amounts are expressed in K'000</i>	2013	2012	2013	2012
Assets subject to operating lease				
Carrying value				
Aircraft	123,326	123,326	123,326	123,326
Accumulated depreciation	(61,821)	(54,100)	(61,821)	(54,100)
Net book value	61,505	69,226	61,505	69,226
Reconciliation of carry value of aircraft is set out below:				
Aircraft				
At 1 January	69,226	68,936	69,226	68,936
Revaluation net increase	-	8,285	-	8,285
Depreciation	(7,721)	(7,995)	(7,721)	(7,995)
At 31 December	61,505	69,226	61,505	69,226
Future minimum lease payments				
Not later than 1 year	10,104	8,373	10,104	8,373
Later than 1 year and not later than 5 years	25,427	28,609	25,427	28,609
	35,531	36,982	35,531	36,982
The carrying amount of land and buildings and aircraft had they been recognised under the cost model are as follows:				
Land	14,932	14,531	11,835	11,434
Buildings	100,867	102,444	86,240	86,192
Aircraft	61,505	60,392	61,505	60,392
At 31 December 2013	177,304	177,367	159,580	158,018

Freehold land and buildings carried at fair value

An independent valuation of the Bank's land and buildings was performed by GDA Pacific Valuers to determine the fair value of the land and buildings. The valuation, which conforms to International Valuation Standards, was determined by reference to capitalization of the notional income stream approach on the Market Value basis. The last valuation was dated 31 December 2011.

Assets subject to operating lease - aircraft

An independent valuation of the Bank's aircrafts was performed by Charles Taylor Aviation to determine the current realistic fair value for each of the aircraft. The valuation, which conforms to International Valuation Standards, takes into consideration the current global market variations for the specific types of aircrafts. The effective date of the recent valuation was done on 31 May 2012.

Notes to the Financial Statements

for the year ended 31 December 2013

15. Investment properties

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Opening net book value	56,755	60,308	-	-
Net movement	8,251	1,112	-	-
Transfer to asset held for sale	-	(3,706)	-	-
Gain / (loss) on revaluation	423	(959)	-	-
At 31 December 2013	65,429	56,755	-	-

16. Other financial assets

Securities – held to-maturity:

Inscribed stock – issued by Central Bank	2,121,654	1,505,589	1,924,536	1,354,659
Financial assets carried at fair value through profit and loss:				
Equity securities	49,144	52,361	-	-
At 31 December 2013	2,170,798	1,557,950	1,924,536	1,354,659

The fair value hierarchy of the financial assets carried at fair value through profit and loss:

2013	Level 1	Level 2	Level 3	Total
Equity securities	-	47,811	1,333	49,144
	-	47,811	1,333	49,144
2012				
Equity securities	-	51,278	1,083	52,361
	-	51,278	1,083	52,361

The fair value hierarchy disclosure is in accordance with International Financial Reporting Standards requirements.

17. Other assets

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Items in transit and other assets	305,184	398,018	290,995	357,349
Accrued income	75,882	76,079	75,882	76,079
Intercompany account	-	-	494	(11,454)
Outstanding premiums	26,050	20,865	-	-
Inventory	7,861	5,575	-	-
Prepayments	13,943	14,824	13,943	14,824
Accounts receivable	8,393	(3,442)	423	(2,691)
	437,313	511,919	381,737	434,107

Notes to the Financial Statements

for the year ended 31 December 2013

18. Amounts due to other banks

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Items in the course of collection	786,035	72,775	786,035	90,828

19. Amounts due to customers

On demand and short term deposits	10,232,667	9,012,413	10,326,962	9,016,405
Term deposits	1,968,332	1,848,109	1,969,264	1,904,286
	12,200,999	10,860,522	12,296,226	10,920,691

The majority of the amounts are due to be settled within twelve months of the balance sheet date as shown in the maturity analysis table on note 34. The deposits are spread across industries and region.

20. Subordinated debt securities

At 31 December, there are K75.525 million of debt securities outstanding, expected to be settled more than 12 months after the balance sheet date. The notes were issued during 2009, with a maturity date in 2019, and interest is payable semi-annually at 11% per annum. They are valued at amortised cost. There have been no defaults of interest or any other breaches of terms and conditions with respect to these debt securities in 2013.

21. Other liabilities

Creditors and accruals	76,584	79,054	63,812	66,330
Items in transit and all other liabilities	362,875	223,079	371,312	218,827
Policy liabilities	481,087	399,627	-	-
Premiums received in advance	3,985	5,387	-	-
Outstanding claims	10,398	6,420	-	-
Claims incurred but not reported (IBNR)	1,440	1,168	-	-
	936,369	714,735	435,124	285,157
Policy liability is reconciled as follows:				
Opening balance	399,627	376,743	-	-
Increase in policy liability	81,460	22,884	-	-
	481,087	399,627	-	-

Notes to the Financial Statements

for the year ended 31 December 2013

22. Other provisions

<i>All amounts are expressed in K'000</i>	Consolidated		Bank	
	2013	2012	2013	2012
Staff related	62,191	57,069	57,170	52,287
Provision for non-lending loss	30,947	25,394	30,947	25,394
Provision for others	16,899	13,517	16,899	13,517
	110,037	95,980	105,016	91,198
Staff related provisions:				
At 1 January 2013	57,069	46,478	52,287	42,609
Provisions charge	23,705	19,799	21,655	24,208
Payouts	(18,583)	(9,208)	(16,772)	(14,530)
At 31 December 2013	62,191	57,069	57,170	52,287

23. Ordinary shares – Bank

<i>Number of shares in '000s, Book value in K'000</i>	Number of shares	Book value
At 31 December 2011/1 January 2012	473,882	426,444
Share buyback	(4,681)	(41,630)
At 31 December 2012 / 1 January 2013	469,201	384,814
Share buyback	(777)	(3,316)
At 31 December 2013	468,424	381,498

At the company's annual general meeting held on 20 May 2011 in Port Moresby, the shareholders approved a reorganization of the company's capital through a share consolidation by which 10 existing BSP ordinary shares were consolidated into 1 BSP share.

In May 2011, the Directors agreed to introduce a share-buyback scheme of up to K40 million in conjunctions with the 1 for 10 share consideration. The share-buyback commenced in July 2011. At the expiry of the first buyback scheme the Directors approved a further buyback program of K40 million which commenced on Friday 9 March 2012 for a period of 12 months which ceased on 27 March 2013.

The issued capital of Bank of South Pacific Limited comprises ordinary shares. Following is a summary of principal shareholders as at 31 December 2013 and their respective percentage holdings.

Notes to the Financial Statements

for the year ended 31 December 2013

23. Ordinary shares – Bank (continued)

Major shareholders: % shareholding	2013	2012
Independent Public Business Corporation	18.00	17.97
National Superannuation Fund Limited	11.10	11.06
Nambawan Super Limited	10.03	10.04
Petroleum Resources Kutubu Limited	9.85	9.84
Credit Corporation (PNG) Limited	7.75	7.85
Motor Vehicle Insurance Limited	6.67	6.66
PNG Sustainable Development Program Limited	6.23	6.25
IFC Capitalization(Equity) Fund LP	4.87	4.86
International Finance Corporation	4.87	4.86
Teachers Savings & Loans Society Limited	3.70	3.69
Comrade Trustee Services Limited	3.09	3.13
Tropicana Limited	1.06	1.06
	87.22	87.27
All Others	12.78	12.73
	100.00	100.00

	Consolidated		Bank	
<i>All amounts are expressed in K'000</i>	2013	2012	2013	2012
Earnings per ordinary share				
Net Profit attributable to shareholders (K'000)	436,828	407,744	424,762	399,588
Weighted average number of ordinary shares in use ('000)	469,136	469,201	469,136	469,201
Basic and diluted earnings /(loss) per share (expressed in toea)	93.1	86.9	90.5	85.2

Basic earnings per ordinary share are calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year. Bank of South Pacific Limited has no dilutive potential ordinary shares. Consequently, basic earnings per ordinary share equals diluted earnings per share.

Dividend paid on ordinary shares

Interim ordinary dividend (2013: 20 toea; 2012: 20 toea)	93,685	93,970	93,685	93,970
Final ordinary dividend (2012: 38 toea; 2011: 35 toea)	178,001	165,024	178,001	165,024
	271,686	258,994	271,686	258,994

Applicable dividend withholding tax of 17% has been deducted for payment to the relevant authority.

Notes to the Financial Statements

for the year ended 31 December 2013

24. Reserves and retained earnings	Consolidated		Bank	
	2013	2012	2013	2012
<i>All amounts are expressed in K'000</i>				
Retained earnings				
At 1 January	870,148	721,398	838,292	697,698
Net profit for the year	436,828	407,744	424,762	399,588
Dividend paid	(271,686)	(258,994)	(271,686)	(258,994)
At 31 December	1,035,290	870,148	991,368	838,292
Reserves comprise				
Revaluation reserve	170,103	170,103	170,103	170,103
Capital reserve	635	635	635	635
Equity component of convertible notes	18,218	18,218	-	-
Options reserve	-	4,526	-	4,526
General reserve	2,875	2,875	2,875	2,875
Exchange reserve	10,441	14,574	7,833	14,574
	202,272	210,931	181,446	192,713
Movement in reserves for the year:				
Revaluation reserve				
At 1 January	170,103	160,293	170,103	160,293
Asset revaluation increment	-	12,296	-	12,296
Deferred tax on asset revaluation	-	(2,486)	-	(2,486)
At 31 December	170,103	170,103	170,103	170,103
Capital reserve				
At 1 January	635	635	635	635
At 31 December	635	635	635	635
Options reserve				
At 1 January	4,526	3,238	4,526	3,238
Movement during the year	(4,526)	1,288	(4,526)	1,288
At 31 December	-	4,526	-	4,526
General reserve				
At 1 January	2,875	2,875	2,875	2,875
At 31 December	2,875	2,875	2,875	2,875

Notes to the Financial Statements

for the year ended 31 December 2013

24. Reserves and retained earnings (continued)

	Consolidated		Bank	
	2013	2012	2013	2012
<i>All amounts are expressed in K'000</i>				
Exchange reserve				
At 1 January	14,574	11,087	14,574	15,627
Movement during the year	(4,133)	3,487	(6,741)	(1,053)
At 31 December	10,441	14,574	7,833	14,574

Exchange reserve

The movement in exchange reserve is a result of taking on alignment entries and month end entries of BSP's foreign branches in Solomon Islands and Fiji. These treatments are in accordance with applicable accounting standards.

Equity component of convertible notes

On 20 April 2010, the Group issued 3,064,967 Fiji Dollars (FJD) denominated mandatory convertible notes through its wholly owned subsidiary BSP Convertible Notes Limited (BSP CN) at an issue price of FJD5.25 (K7.30) per note. Each note entitles the holder to convert to ten (10) Fiji Class shares. On conversion all notes are redeemed for their face value and the proceeds of that redemption are applied as the subscription price for Fiji Class shares. Notes can only be redeemed in cash at the election of BSP CN Fiji with regulatory approval. The amount payable at redemption will be greater of the market value or face value of the note plus accrued interest. The notes have mandatorily converted to Fiji Class Shares on 20 April 2013.

The net proceeds received from the issue of the convertible notes have been split between the financial liability element and the equity component, representing the residual attributable to the option to convert the financial liability into equity of BSP CN.

The equity component of K18.218 million has been credited to equity (option premium on convertible notes).

Note holders have no right to vote at meetings of BSP Convertible Notes Limited.

Statutory capital requirements in Fiji

As a requirement of the Reserve Bank of Fiji, BSP Fiji operations is required to maintain assigned capital of K24.833m (2012: K24.833m) and capital adequacy reserve of K68.547m (2012: K68.547m).

Notes to the Financial Statements

for the year ended 31 December 2013

25. Contingent liabilities and commitments

Off balance sheet financial instruments

	Consolidated		Bank	
	2013	2012	2013	2012
<i>All amounts are expressed in K'000</i>				
Standby letters of credit	47,692	18,051	47,692	18,051
Guarantees and indemnities issued	181,232	64,490	170,124	121,782
Foreign exchange contract	374,934	57,291	374,934	57,291
Trade letters of credit	47,691	86,963	25,619	86,963
Commitments to extend credit	860,453	1,290,923	695,233	1,178,340
	1,512,002	1,517,718	1,313,602	1,462,427

Legal Proceedings

A number of legal proceedings against the Bank and the Group were outstanding as at 31 December 2013. Suitable provisions has been made based on existing management information and professional advice, on likelihood of any success of claim against the Bank. Based on information available at 31 December 2013, the Bank and the Group estimates a contingent liability of K77.9 million (2012: K74.780 million) in respect of these proceedings.

Statutory deposits with the Central Bank

Cash reserve requirement - 9% of all amounts due to customers (2012: 8%)

1,066,580	873,198	1,066,580	742,495
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Commitments for capital expenditure

Amounts with firm commitments, and not reflected in the accounts

154,344	24,646	154,344	24,646
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Operating lease commitments

Not later than 1 year	40,079	23,048	40,079	23,048
Later than 1 year and not later than 5 years	37,556	80,914	37,556	80,914
	77,635	103,962	77,635	103,962

26. Fiduciary activities

The Group especially through BSP Capital Limited conducts investment fund management, stock broking and other fiduciary activities as responsible entity, trustee, custodian or manager for investment funds and trusts, including superannuation. These funds are not consolidated as the Group does not have direct or indirect control. Where the funds incurs liabilities in respect of these activities, and the primary obligation is incurred in an agency capacity, for the fund or clients rather than its own account, a right of indemnity exists against the assets of the applicable fund or trust. As these assets are sufficient to cover the liabilities and it is therefore not probable that the Group will be required to settle the liabilities, the investments in the assets and liabilities of these activities are not included in the consolidated financial statements.

Notes to the Financial Statements

for the year ended 31 December 2013

27. Directors and executive remuneration

Directors remuneration

Directors of the company received remuneration including benefits during 2013 as detailed below:

All amounts are in K

Name of Director	Meetings attended / total held	Appointed/ (Resigned)	Base emolument	Bonus shares	Other compensation	Total remuneration	
						2013	2012
K. Constantinou, OBE	7/7	-	222,539	-	-	222,539	195,090
T. E. Fox, OBE	7/7	-	213,542	-	-	213,542	210,037
Dr. I. Temu	7/7	-	112,014	-	-	112,014	113,910
C. C. Procter	6/7	-	217,388	-	-	217,388	211,969
Sir N. Bogan	6/7	-	104,967	-	-	104,967	101,224
R. Fleming*	4/4	1 June 13	-	-	-	-	-
I. B. Clyne*	3/3	(31 May 13)	-	-	-	-	-
J. G. Jeffery, CBE	2/2	(23 May 13)	62,385	-	-	62,385	160,244
G. Aopi, CBE	7/7	-	115,456	-	-	115,456	116,043
G. Robb, OAM	7/7	-	280,613	-	-	280,613	207,104
F. Talao	6/7	-	104,875	-	-	104,875	108,869
E. B Gangloff	0/1	28 Nov 13	-	-	-	-	-

Directors Thomas Fox and Ila Temu retired by rotation in accordance with Clause 15.3 of the Company's Constitution and being eligible, offered themselves for re-election by the shareholders at 24th May 2013 Annual General Meeting. John Jeffery resigned as a Director of the BSP Board on 23rd May 2013. Ernest Gangloff joined the Board as a Director on 28 November 2013 and will offer himself for election by the Shareholders at the Annual Meeting in May 2014.

Non-executive Directors – Constantinou, Fox and Procter received an allowance of K60,000 as Board of Directors of BSP Capital Ltd which forms part of the Group. Director Geoff Robb was appointed as a Director to the Board of BSP Capital Ltd and receives this Directors fee of K60,000 per annum for this.

Ian B. Clyne ceased to be Group CEO and Managing Director on 31st May 2013. Robin Fleming was appointed Group CEO and Managing Director as of 1st June 2013.

* Managing Director / Chief Executive Officer receives no fees for his services as Director during the year. Other members of BSP executive management who serve as directors of subsidiaries of BSP Group, receive no fees for their services as Director.

Notes to the Financial Statements

for the year ended 31 December 2013

27. Directors and executive remuneration (continued)

Executive remuneration

The number of employees or former employees whose income from the Bank was equal to or greater than K100,000 during the year, are classified in income bands of K10,000 as follows:

Remuneration K'000	2013 No.	2012 No.	Remuneration K'000	2013 No.	2012 No.	Remuneration K'000	2013 No.	2012 No.
100 – 110	34	28	420 – 430	2	1	740 – 750	1	-
110 – 120	16	29	430 – 440	2	1	750 – 760	2	2
120 – 130	21	21	440 – 450	-	2	760 – 770	2	1
130 – 140	21	25	450 – 460	2	-	770 – 780	1	-
140 – 150	24	14	460 – 470	-	1	780 – 790	1	-
150 – 160	11	9	470 – 480	-	-	790 – 800	-	-
160 – 170	10	8	480 – 490	-	2	800 – 810	1	1
170 – 180	13	8	490 – 500	1	3	810 – 820	-	3
180 – 190	8	6	500 – 510	1	3	820 – 830	1	1
190 – 200	9	6	510 – 520	3	5	830 – 840	1	-
200 – 210	1	5	520 – 530	2	-	840 – 850	-	-
210 – 220	7	3	530 – 540	2	3	850 – 860	1	-
220 – 230	4	4	540 – 550	3	2	880 – 890	1	-
230 – 240	4	3	550 – 560	-	2	890 – 900	1	-
240 – 250	9	5	560 – 570	2	-	910 – 920	1	-
250 – 260	7	5	570 – 580	4	5	950 – 960	-	1
260 – 270	6	5	580 – 590	-	2	960 – 970	1	-
270 – 280	4	2	590 – 600	3	2	980 – 990	2	-
280 – 290	3	5	600 – 610	5	-	1050 – 1060	-	1
290 – 300	-	2	610 – 620	2	4	1060 – 1070	-	1
300 – 310	3	7	620 – 630	1	-	1090 – 1100	1	-
310 – 320	4	3	630 – 640	2	1	1100 – 1110	1	0
320 – 330	1	1	640 – 650	-	3	1260 – 1270	1	-
330 – 340	2	1	650 – 660	3	3	1350 – 1360	-	3
340 – 350	2	2	670 – 680	-	2	1440 – 1450	-	1
350 – 360	2	3	680 – 690	1	2	1660 – 1670	1	-
360 – 370	3	2	690 – 700	3	1	1730 – 1740	1	-
370 – 380	2	3	700 – 710	1	4	1790 – 1800	1	-
380 – 390	2	1	710 – 720	1	1	2430 – 2440	1	-
390 – 400	3	2	720 – 730	-	1	4500 – 4510	-	1
400 – 410	4	1	730 – 740	1	-	6800 – 6810	1	-
Total							312	291

Executives' remuneration stated includes phantom share options.

Notes to the Financial Statements

for the year ended 31 December 2013

27. Directors and executive remuneration (continued)

The specified executives during the year were:

Ian B Clyne	Robin Fleming	Robert Loggia	Richard Borysiewicz	Frans Koote
Johnson Kalo	Peter Beswick	Paul Thornton	Edward Ruha	Haroon Ali
Aho Baliki	Giau Duruba	Mark Railston		

Specified executives' remuneration in aggregate (K'000)

	Salary	Primary Bonus	Non-monetary	Super	Post-employment Prescribed benefits	Other	S/T incentive	Other benefits	Total
2013	13,143	4,251	201	191	-	-	1,339	755	19,880
2012	8,213	1,954	220	200	-	-	1,200	378	12,165

28. Reconciliation of operating cash flow

	Consolidated		Bank	
	2013	2012	2013	2012

All amounts are expressed in K'000

Reconciliation of operating profit/(loss) after tax to operating cash flow before changes in operating assets

Operating profit/(loss) after tax	436,828	407,744	424,762	399,588
Add: Tax Expense	170,127	137,552	168,114	135,849
Operating profit before income tax	606,955	545,296	592,876	535,437

Major non cash amounts

Depreciation	90,817	57,968	86,723	54,806
Amortisation of computer development costs	85,018	25,785	85,018	25,785
Net (profit)/loss on sale of fixed assets	906	(498)	906	(498)
Movement in forex income accrual	10,746	(710)	10,746	(710)
Movement in provision for doubtful debts	104,812	92,085	104,812	92,085
Movement in payroll provisions	5,778	9,587	5,778	9,587
Net effect of other accruals	(4,909)	12,304	32,703	24,722
Operating cash flow before changes in operating assets	900,123	741,817	919,562	741,214

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with less than 90 days maturity.

Cash and balances with Central Bank (note 10)	2,030,800	1,806,597	1,992,970	1,764,275
Due from other banks (note 12)	1,445,199	327,563	1,445,199	327,563
Due to other banks (note 18)	(786,035)	(72,775)	(786,035)	(90,828)
	2,689,964	2,061,385	2,652,134	2,001,010

Notes to the Financial Statements

for the year ended 31 December 2013

29. Segment information

For management purposes, segment information determination is based on the risks involved with the provision of core banking services and products and the Group's related financial services businesses and the Bank and Group's management reporting system. The main business lines for management purposes are core banking segments of retail bank, wholesale bank which includes corporate and paramount strategic business units, insurance operations in Fiji, and BSP Capital's stock broking and fund management activities. The Bank of South Pacific Limited and Group's business segments operates in Papua New Guinea, Niue, Fiji and Solomon Islands. Inter segment adjustments reflects elimination entries in respect of inter segment income and expense allocations including funds transfer pricing.

All amounts are expressed in K'000

Analysis by business segments:

Year ended 31 December 2013

	Retail	Wholesale	Fiji Bank	Insurance	BSP Capital	Others	Adjust Inter Segments	Total
Revenue	510,606	669,906	111,716	188,370	3,687	32,356	99,101	1,615,742
Costs	(363,856)	(255,319)	(96,827)	(172,475)	(6,921)	(31,901)	(81,488)	(1,008,787)
Operating results	146,750	414,587	14,889	15,895	(3,234)	455	17,613	606,955
Income tax expense								(170,127)
Profit after tax								436,828

Year ended 31 December 2012

	Retail	Wholesale	Fiji Bank	Insurance	BSP Capital	Others	Adjust Inter Segments	Total
Revenue	395,269	636,433	83,105	155,994	2,407	56,158	268,301	1,597,667
Costs	(258,909)	(326,565)	(78,522)	(142,209)	(6,315)	(33,878)	(205,973)	(1,052,371)
Operating results	136,360	309,868	4,583	13,785	(3,908)	22,280	62,328	545,296
Income tax expense								(137,552)
Profit after tax								407,744

Notes to the Financial Statements

for the year ended 31 December 2013

30. Related party transactions

Related parties are considered to be enterprises or individuals with whom the Bank and the Group is especially related because either they or the Bank are in a position to significantly influence the outcome of transactions entered into with the Bank and the Group, by virtue of being able to control, dominate or participate in a fiduciary capacity, in decision-making functions or processes. The Bank and the Group conducted transactions with the following classes of related parties during the year:

- Directors and/or parties in which the director has significant influence
- Key management personnel and other staff and/or parties in which the individual officer has significant influence

A number of banking transactions are entered into with these related parties in the normal course of business, and include loans, deposits, property rentals, share transfers and foreign currency transactions. These transactions are carried out on commercial terms and market rates. For the year ended 31 December 2013, balances and transactions of accounts for Directors were as follows:

<i>All amounts are expressed in K'000</i>	2013	2012
Deposits		
Opening balances	139,557	208,359
Net movement	52,889	(68,802)
Closing balance	<u>192,446</u>	<u>139,557</u>
Interest paid	4,022	7,261
Loans and advances		
Opening balances	172,725	157,039
Loans issued	339,602	219,795
Interest	40,128	58,296
Charges	11,590	6,113
Loan repayments	(179,725)	(268,518)
Closing balance	<u>384,320</u>	<u>172,725</u>

Employment-based transactions are provided for staff. Such transactions include marginal discounts on rates, and specific fee concessions. These incentives are mainly percentage-based on market rates and fees, and as such, staff accounts are always subject to underlying market trends in interest rates and fees. As at 31 December 2013, staff account balances were as follows:

<i>All amounts are expressed in K'000</i>	2013	2012
Housing loans	18,111	17,296
Other loans	16,442	16,674
	<u>34,553</u>	<u>33,970</u>
Cheque accounts	8,083	23,736
Foreign currency accounts	237	320
Savings accounts	10	11
	<u>8,330</u>	<u>24,067</u>

Notes to the Financial Statements

for the year ended 31 December 2013

30. Related party transactions (continued)

Interests Register

The following are transactions recorded in the interests register:

Name	Nature of Interest	
K. Constantinou, OBE Chairman	Director	Bank of South Pacific Ltd ¹ , BSP Capital Ltd ¹ , Airways Hotel & Apartment Ltd, Lamana Hotel Ltd, Lamana Development Ltd, Hebou Constructions Ltd, Heritage Park Hotel Ltd, Gazelle International Hotel Ltd, Airlines PNG Ltd, Oil Search Ltd, Alotau International Hotel Ltd, Kimbe Bay Hotel Ltd, Grand Pacific Hotel Ltd, City Centre Development Ltd, Coastwatchers Court Ltd, Waigani Assets Ltd, Southern Seas Investments Ltd, Texas Chicken South Pacific Ltd.
	Shareholder	Airways Hotel & Apartment Ltd, Lamana Hotel Ltd, Lamana Development Ltd, Texas Chicken South Pacific Ltd..
	Member	Australian Institute of Company Directors, PNG Institute of Directors, Pacific Games Authority ^{1,6} , Anglicare Foundation.
T. E. Fox, OBE, BEc Deputy Chairman	Director	Bank of South Pacific Ltd ² , BSP Capital Ltd, Teyo No. 1 Ltd ⁵ , BSP Life Ltd, Akura Ltd
	Shareholder	Bank of South Pacific Ltd, Teyo No. 1 Ltd, Akura Ltd.
	Trustee/Member	Institute of National Affairs ⁸ , PNG Institute of Directors.
Robin Fleming	Director	Bank of South Pacific Ltd ⁹ , BSP Capital Ltd, BSP Convertible Notes Ltd, BSP Rural Ltd, BSP Life Ltd, BSP Capital Securities Ltd, BSP Services Ltd, Capital Nominees Ltd, BSP Nominees Ltd, Malagan Ltd, Carpark Ltd, NGIP Agmark Ltd, BSP Services (Fiji) Ltd, BSP Health Care (Fiji) Ltd, BSP Investments (Fiji) Ltd
	Shareholder	Bank South Pacific Ltd.
	Member	Australian Institute of Company Directors, PNG Institute of Directors, Anglicare Foundation.
G. Aopi, CBE, MBA	Director	Bank of South Pacific Ltd, Oil Search Ltd ⁷ , Steamships Trading Co Ltd, POMSoX Ltd, Marsh Ltd, Wahinemo Ltd, CDI Foundation.
	Shareholder	Bank of South Pacific Ltd, Oil Search Ltd ⁷ , Hirad Ltd, Wahinemo Ltd, Newcrest Ltd, Highlands Pacific Ltd, Melanesian Trustees (ICPNG), Kumul Asset Management.
	Member/Trustee	Institute of National Affairs, Business Council of PNG, PNG Chamber of Mines & Petroleum, Oil Search Health Foundation.
Dr I. Temu, PhD, MEc	Director	Bank of South Pacific Ltd, Tipi Enterprise Ltd, Telemu Ltd ¹ , Kina Petroleum Ltd, National Petroleum Company Ltd, Savi-Tec Ltd.
	Shareholder	Telstra Ltd, Nautilus Minerals Niugini Ltd.
	Employee	Barrick Gold Ltd.
	Member	Divine Word University.
C. C. Procter, MEc, FFin	Director	Bank of South Pacific Ltd, BSP Capital Ltd, Sun Hung Kai & Co. Ltd, Allied Overseas Ltd, Eurogold Ltd, Tanami Gold NL.
	Member	Australian Institute of Company Directors.
E. B. Gangloff	Director	Bank of South Pacific Ltd, Gangloff Consulting Ltd, Laurabada Investments Ltd, New Britain Palm Oil Ltd.
	Shareholder	Gangloff Consulting, Laurabada Investments Ltd.
	Member	CPA PNG, PNG Institute of Directors, Vice-President PNG Business Council, Institute of National Affairs, Business & Officials Committee PNG/Australia Bilateral Ministerial Committee, CIMC Trade Services Commissions Chairman.

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for the year ended 31 December 2013

30. Related party transactions (continued)

Interest Register (continued)

Name	Nature of Interest	
Sir N. Bogan, KBE, LLB	Director	Bank of South Pacific Ltd, Nambawan Super Ltd ^{1,5} , In Touch Media Ltd ¹ , Coprez Communications Ltd ¹ , Coprez Holdings Ltd, Mapai Transport Ltd, Ahi Holdings Ltd.
	Shareholder	In Touch Media Ltd, Coprez Holdings Ltd.
	Member	Chancellor Unitech, Chairman PNG Taxation Review.
G. Robb, OAM	Director	Bank of South Pacific Ltd, BSP Capital Ltd
	Member	Australian Institute of Company Directors,
F Talao, LLB	Director	Bank of South Pacific Ltd.
	Member	External Stakeholders Advisory Panel to Morobe Mining Joint Venture, Australian Institute of Company Directors.

¹Chairman, ²Deputy Chairman, ³Managing Director, ⁴Executive Director, ⁵General Manager, ⁶Councillor

⁵Company is shareholder of Bank of South Pacific Limited, or shareholder of company that is shareholder

⁶Company has commercial banking facilities with Bank of South Pacific Limited, ⁹Chief Executive Officer

31. Bank operations, risks and strategies in using financial instruments

All business operations must deal with a variety of operational and financial risks. The business activities of a bank expose it to very critical and specific risks, which are principally related to the Bank and the Group's primary financial intermediary role in the financial markets, including the use of financial instruments including derivatives. These market risks (risk of an advance event in the financial markets that may result in loss of earnings) include liquidity risk, foreign exchange risk, interest rate risk and credit risk.

The Bank and the Group accepts deposits from customers at both fixed and floating rates and for various periods and seeks to earn above average interest margins by investing these funds in high quality assets. These margins are achieved and increased by consolidating short-term funds and lending for longer periods at higher rates whilst maintaining sufficient liquidity to meet all claims that might fall due.

The Bank and the Group also seeks to optimise its interest margins by obtaining above average returns, net of provisions, through lending to commercial and retail borrowers with a range of credit standing. In addition to directly advancing funds to borrowers, the Bank and the Group also enters into guarantees and other commitments such as letters of credit, performance bonds, and other bonds.

The Bank and the Group also enters into transactions denominated in foreign currencies. This activity generally requires the Bank and the Group to take foreign currency positions in order to exploit short term movements in the foreign currency market. The Board places limits on the size of these positions. The Bank and the Group also has a policy of using offsetting commitments for foreign exchange contracts, effectively minimising the risk of loss due to adverse movements in foreign currencies.

Risk in the Bank and the Group is managed through a system of delegated limits. These limits set the maximum level of risk that can be assumed by each operational unit and the Bank and the Group as a whole. The limits are delegated from the Board of Directors to executive management and hence to the respective operational managers.

The risk management framework establishes roles, responsibilities and accountabilities of the Asset and Liability Committee, the Credit Committee, the Operational Risk Committee and the Executive Committee, the specific management committees charged with the responsibility for ensuring the Bank and the Group has appropriate systems, policies and procedures to measure, monitor and report on risk management. The framework also includes policies and procedures which detail formal feedback processes to these management committees, to the Audit, Risk and Compliance Committee of the Board, and ultimately to the Board of Directors.

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for the year ended 31 December 2013

32. Capital adequacy

The Bank and the Group is required to comply with various prudential standards issued by the Bank of Papua New Guinea (BPNG), Reserve Bank of Fiji & Central Bank of Solomon Islands, the official authorities for the prudential supervision of banks and similar financial institutions in Papua New Guinea, Fiji and Solomon Islands. One of the most critical prudential standards is the capital adequacy requirement. All banks are required to maintain at least the minimum acceptable measure of capital to risk-weighted assets to absorb potential losses. The BPNG follows the prudential guidelines set by the Bank of International Settlements under the terms of the Basel Accord. The BPNG revised prudential standard 1/2003, Capital Adequacy, prescribes ranges of overall capital ratios to measure whether a bank is under, adequately, or well capitalised, and also applies the leverage capital ratio. The Bank and the Group complies with the prevailing prudential requirements for total capital and leverage capital. As at 31 December 2013, the Bank and the Group's total capital adequacy ratio and leverage capital ratio satisfied the capital adequacy criteria for well-capitalised. The minimum capital adequacy requirements set out under the standard are: Tier 1 8%, total risk base capital ratio 12% and the leverage ratio 6%.

The measure of capital used for the purposes of prudential supervision is referred to as base capital. Total base capital varies from the balance of capital shown on the statement of financial position and is made up of tier 1 capital (core) and tier 2 capital (supplementary). Tier 1 capital is obtained by deducting from equity capital and audited retained earnings (or losses), intangible assets including deferred tax assets. Tier 2 capital cannot exceed the amount of tier 1 capital, and can include subordinated loan capital, specified asset revaluation reserves, unaudited profits (or losses) and a small percentage of general loan loss provisions. The leverage capital ratio is calculated as Tier 1 capital divided by total assets on the balance sheet.

Risk weighted assets are derived from on-balance sheet and off-balance sheet assets. On balance sheet assets are weighted for credit risk by applying weightings (0, 20, 50 and 100 per cent) according to risk classification criteria set by the BPNG. Off-balance sheet exposures are risk weighted in the same way after converting them to on-balance sheet credit equivalents using BPNG specified credit conversion factors.

The Bank and the Group's capital adequacy level is as follows:

	Balance sheet / notional amount		Risk-weighted amount	
	2013	2012	2013	2012
<i>All amounts are expressed in K'000</i>				
Balance sheet assets (net of provisions)				
Currency	2,030,800	1,806,597	-	-
Loans and advances	5,306,362	4,804,626	5,009,265	4,594,014
Investments and short term securities	5,454,230	4,795,467	-	-
All other assets	3,017,398	1,926,412	2,778,531	1,847,900
Off balance sheet items	1,512,002	1,517,718	714,414	316,934
Total	17,320,792	14,850,820	8,502,210	6,758,848

Audited Capital Ratios	Capital (K'000)		Capital Adequacy Ratio (%)	
	2013	2012	2013	2012
a) Tier 1 capital	1,181,187	1,185,382	13.9%	17.4%
Tier 1 + Tier 2 capital	1,533,093	1,516,086	18.0%	22.3%
b) Leverage Capital Ratio			7.6%	9.0%

The capital adequacy ratio has been affected by the capitalisation of the software development costs, categorized under intangibles per note 7, which is deducted from tier 1 capital.

33. Credit risk and asset quality

The Bank incurs risk with regards to loans and advances made to customers and other monies or investments held with financial institutions. Credit risk is the likelihood of future financial loss resulting from the failure of clients or counter-parties to meet contractual obligations to the Bank and the Group as they fall due.

Notes to the Financial Statements

for the year ended 31 December 2013

33. Credit risk and asset quality (continued)

Credit risk is managed by analysing the risk spread across various sectors of the economy and by ensuring risk is diversely spread by personal and commercial customer. Individual exposures are measured using repayment performance, reviews and statistical techniques. Comprehensive credit standards and approval limits have been formulated and approved by the Credit Committee. The Credit Committee (which reports to the Board through the Executive and Chief Executive Officer) is responsible for the development and implementation of credit policy and loan portfolio review methodology. The Credit Committee is the final arbiter of risk management and loan risk concentration.

As indicated in Accounting Policy G – Loans and provision for loan impairment, the Bank and the Group has in place processes that identify, assess and control credit risk in relation to the loan portfolio, to assist in determining the appropriateness of provisions for loan impairment. These processes also enable assessments to be made of other classes of assets that may carry an element of credit risk. The Bank and the Group assigns quality indicators to its credit exposures to determine the asset quality profile.

Large credit exposures are also monitored as part of credit risk management. These are classified as the largest 25 individual accounts or groups of related counter-parties. As at 31 December 2013, the 25 largest exposures totaled K3.2 billion, accounting for over 60% of the Bank and 60% of the Group's total loan portfolio (2012: K2.815 billion, accounting for over 56% and 56% respectively).

The Bank of Papua New Guinea has maintained a revised prudential standard for asset quality since October 2003. The revised standard specifies more detailed criteria for the classification of loans into various grades of default risk and corresponding loss provision levels as a consequence of those gradings. Since its introduction, the Bank and the Group has complied with the requirement at all times.

Credit related commitments

These instruments are used to ensure that funds are available to a customer as required. The Bank and the Group deals principally in the credit related commitments set out below.

Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank and the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same risk as loans.

Documentary and trade letters of credit are written undertakings by the Bank and the Group on behalf of a customer, authorising a third party to draw drafts on the Bank and the Group for specified amounts under specified terms and conditions. They are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a conventional loan.

Commitments to extend credit represent undrawn portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. Whilst the potential exposure to loss equates to the total undrawn commitments, the likely amount of loss is less than the total commitment since the commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank and the Group monitors the term to maturity of these commitments because longer term commitments generally carry a greater degree of credit risk than shorter term commitments.

Economic sector risk concentrations

Economic sector risk concentrations within the customer loan portfolio are as follows:

All amounts are expressed in K'000

As at 31 December	2013	%	2012	%
Commerce, finance and other business	2,391,072	45	1,937,732	40
Private households	695,782	13	946,132	20
Government and public authorities	444,670	9	101,621	2
Agriculture	267,367	5	116,451	2
Transport & communication	583,853	11	723,624	15
Manufacturing	394,268	7	520,588	11
Construction	529,350	10	458,478	10
Net loan portfolio balance	5,306,362	100	4,804,626	100

Notes to the Financial Statements

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34. Liquidity risk

Liquidity risk is the risk of being unable to meet financial obligations as they fall due. The Board, through the Asset and Liability Committee, sets liquidity policy to ensure that the Bank and the Group has sufficient funds available to meet all its known and potential obligations.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of banking activities. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

Short-term mismatch of asset and liability maturity at 31 December 2013

The maturity profile of material Assets and Liabilities as at 31 December 2013 is shown in the following schedule. The mismatching of maturity of assets and liabilities indicates an apparent negative net "current" asset position. However, as stated in the preceding paragraph, mismatched positions are established and managed to achieve profit opportunities that arise from them, particularly in a normal yield curve environment. Accordingly, this mismatched maturity position is considered manageable by the Bank and the Group, and does not impair the ability of the Bank and the Group to meet its financial obligations as they fall due. The Directors are also of the view that the Bank and the Group is able to meet its financial obligations as they fall due for the following additional reasons:

- The Bank and the Group complies with the Minimum Liquid Asset Ratio ("MLAR") and Cash Reserve Requirement ("CRR") set by the regulatory authority, the Bank of Papua New Guinea ("BPNG"). The MLAR is the minimum ratio of liquid assets to total customer deposits considered by the regulator as sufficient to support exceptional liquidation by depositors, of their funds. The requirement to hold a minimum of 25% of the value of total customer deposits in the form of prescribed liquid assets was reduced to zero by the BPNG in September 2010. As at 31 December 2013, the Bank and the Group's Liquid Asset Ratio was approximately 41.78% (2012: 38.92%).
- The CRR specifies that a bank must hold an amount equal to 9% of its total customer deposits in the form of cash in an account maintained at the BPNG. The Bank and the Group complies with this daily requirement on an ongoing basis. The balance of the CRR account is shown in note 10, Cash and Balances with Central Bank, and note 28, Cash & Cash Equivalents.

Maturity of assets and liabilities

All amounts are expressed in K'000

As at 31 December 2013	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Assets						
Cash and balances with Central Bank	2,030,800	-	-	-	-	2,030,800
Treasury & Central Bank bills	548,769	1,284,959	1,442,069	7,635	-	3,283,432
Due from other banks	1,110,091	86,764	248,344	-	-	1,445,199
Loans and advances	1,275,469	106,587	662,365	1,408,141	1,853,800	5,306,362
Investments	152,673	30,185	83,642	937,033	967,265	2,170,798
Total assets	5,117,802	1,508,495	2,436,420	2,352,809	2,821,065	14,236,591

Notes to the Financial Statements

for the year ended 31 December 2013

34. Liquidity risk (continued)

All amounts are expressed in K'000

As at 31 December 2013	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Liabilities						
Due to other banks	786,035	-	-	-	-	786,035
Due to customers	10,516,602	400,548	364,169	81,441	838,239	12,200,999
Other liabilities	936,369	-	-	-	75,525	1,011,894
Other provisions	133,632	57,170	-	-	-	190,802
Total liabilities	12,372,638	457,718	364,169	81,441	913,764	14,189,730
Net liquidity gap	(7,254,835)	1,050,777	2,072,251	2,271,368	1,907,301	46,861
As at 31 December 2012	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Total assets	4,749,543	1,306,911	1,923,849	1,325,159	2,428,791	11,734,253
Total liabilities	10,915,010	506,315	315,394	48,723	81,767	11,867,209
Net liquidity gap	(6,165,467)	800,596	1,608,455	1,276,436	2,347,024	(132,956)

35. Operational risk

Operational risk is the potential exposure to unexpected financial or non-financial losses arising from the way in which the Bank and the Group conducts its business. Examples of operational risks include employee errors, systems failures, fire, floods, or similar losses to physical assets, fraud, or criminal activity. Operational risk is managed through formal policies, documented procedures, business practices and compliance monitoring.

An operational risk management function is responsible for the maintenance of these policies, procedures practices and monitoring the organization's compliance with them. The Operational Risk Committee coordinates the management process across the organization.

An independent internal audit function also conducts regular reviews to monitor compliance with policy and regulatory environment and examines the general standard of control.

The Operational Risk Committee and the internal audit function mandatorily report to the Board Audit, Risk and Compliance Committee.

36. Foreign exchange risk

Foreign exchange risk is the risk to earnings caused by a change in foreign exchange rates on open currency positions. The objective of foreign exchange risk management within the Bank and the Group is to minimise the impact on earnings of any such movement.

The Bank and the Group accepts foreign currency denominated transactions and therefore has exposure to movements in foreign currency. The Bank and the Group has a policy to offset these transactions by minimising daily exposure. This is done through hedging material exposures as they arise. As foreign exchange contracts generally consist of offsetting commitments, they involve only limited foreign exchange risk to the Bank and the Group and material loss is not envisaged.

Notes to the Financial Statements

for the year ended 31 December 2013

36. Foreign exchange risk (continued)

Currency concentration of assets, liabilities, and off-balance sheet items

All amounts are expressed in K'000

As at 31 December 2013	USD	AUD	EURO	PGK	Other	Total
Assets						
Cash and balances with Central Bank	2,856	2,340	47	1,395,220	630,337	2,030,800
Treasury & Central Bank bills	-	-	-	3,153,436	129,996	3,283,432
Due from other banks	684,184	345,435	20,417	23,745	371,418	1,445,199
Loans and advances	228,719	3,431	152	3,699,064	1,374,996	5,306,362
Other financial assets	-	-	-	1,904,598	266,200	2,170,798
Other assets	-	-	-	1,361,940	210,259	1,572,199
Total assets	915,759	351,206	20,616	11,538,003	2,983,206	15,808,790
Liabilities						
Due to other banks	(339,396)	(36,883)	-	(13,702)	(396,054)	(786,035)
Due to customers	(396,834)	(252,396)	(13)	(9,805,477)	(1,746,279)	(12,200,999)
Other liabilities	-	-	-	(601,844)	(600,852)	(1,202,696)
Total liabilities	(736,230)	(289,279)	(13)	(10,421,023)	(2,743,185)	(14,189,730)
Net on-balance sheet position	179,529	61,927	20,603	1,116,980	240,021	1,619,060
Off-balance sheet net notional position	(283,238)	(59,576)	(20,535)	938,667	187,067	762,385
Credit commitments	-	-	-	1,512,002	-	-

31 December 2012

Total Assets	414,670	193,415	22,696	10,626,406	2,075,915	13,333,102
Total Liabilities	(343,027)	(364,966)	(3)	(9,149,052)	(2,010,161)	(11,867,209)
Net on-balance sheet position	71,643	(171,551)	22,693	1,477,354	65,754	1,465,893
Off-balance sheet net notional position	26,463	2,355	27,018	-	1,034,611	1,090,447
Credit commitments	-	-	-	1,517,718	-	-

Notes to the Financial Statements

for the year ended 31 December 2013

37. Interest rate risk

Interest rate risk in the balance sheet arises from the potential for a change in interest rate to have an adverse effect on the revenue earnings in the current reporting period and future years. As interest rates and yield curves change over time the Bank and the Group may be exposed to a loss in earnings due to the effects of interest rates on the structure of the balance sheet. Sensitivity to interest rates arises from mismatches in the re-pricing dates, cash flows and other characteristics of the assets and their corresponding liability funding. These mismatches are actively managed as part of the overall interest rate risk management process governed by the Assets and Liabilities Committee (ALCO), which meets regularly to review the effects of fluctuations in the prevailing levels of market interest rates on the financial position and cash flows of the Bank and the Group. The objective of interest rate risk control is to minimise these fluctuations in value and net interest income over time, providing secure and stable sustainable net interest earnings in the long term. The table below illustrates the interest sensitivity of assets and liabilities at the balance date.

Given the profile of assets and liabilities as at 31 December 2013 and prevailing rates of interest, a 1% increase in rates will result in a K15.3 million increase in net interest income, whilst a 1% decrease in rates will result in a K45.2 million decrease in net interest income.

Interest sensitivity of assets, liabilities and off balance sheet items – re-pricing analysis

All amounts are expressed in K'000

As at 31 December 2013	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing
Assets						
Cash & Balances with Central Bank	-	-	-	-	-	2,030,800
Treasury & Central Bank bills	2,453,175	822,622	7,635	-	-	-
Due from other banks	1,350,589	94,609	-	-	-	-
Loans and advances	4,595,301	248,375	376,046	81,548	301	4,792
Investments	41,713	61,648	450,145	518,833	1,184,568	-
Other assets	5,894	5,052	20,207	5,363	-	1,458,333
Total assets	8,446,672	1,232,306	854,033	605,744	1,184,869	3,493,925
Liabilities						
Due to other banks	786,035	-	-	-	-	-
Due to customers	6,674,541	294,855	158,042	16,396	26	5,057,140
Other liabilities	-	-	-	-	75,525	983,739
Other provisions	-	-	-	-	-	143,432
Total liabilities	7,460,576	294,855	158,042	16,396	75,551	6,184,311
Interest sensitivity gap	986,096	937,451	695,991	589,348	1,109,318	(2,690,386)

Notes to the Financial Statements

for the year ended 31 December 2013

37. Interest rate risk (continued)

Interest sensitivity of assets, liabilities and off balance sheet items – re-pricing analysis

As at 31 December 2012	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing
Assets						
Cash and balances with Central Bank	-	-	-	-	-	1,806,597
Treasury and Central Bank bills	962,220	1,154,447	1,120,850	-	-	-
Due from other banks	327,563	-	-	-	-	-
Loans and advances	4,308,480	59,811	219,660	216,675	-	-
Investments	-	34,250	296,750	523,060	703,890	-
Other assets	-	-	-	-	-	1,598,849
Total assets	5,598,263	1,248,508	1,637,260	739,735	703,890	3,405,446
Liabilities						
Due to other banks	72,775	-	-	-	-	-
Due to customers	5,823,901	410,159	292,971	48,723	5	4,284,763
Other liabilities	-	-	-	-	75,525	714,735
Other provisions	-	-	-	-	-	143,652
Total liabilities	5,896,676	410,159	292,971	48,723	75,530	5,143,150
Interest sensitivity gap	(298,413)	838,349	1,344,289	691,012	628,360	(1,737,704)

Notes to the Financial Statements

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38. Fair values of financial assets and liabilities

There is no material difference between the fair value and carrying value of the financial assets and liabilities of Bank of South Pacific Limited and the Group.

In the normal course of trading, the Bank and the Group enters into forward exchange contracts. The Bank and the Group does not actively enter into or trade in, complex forms of derivative financial instruments such as currency and interest rate swaps and options.

Exposures in foreign currencies arise where the Bank and the Group transacts in foreign currencies. This price risk is minimised by entering into counterbalancing positions for material exposures as they arise. Forward and spot foreign exchange contracts are used.

Forward exchange contracts outstanding at 31 December 2013 stated at the face value of the respective contracts are:

All amounts are expressed in respective FCY'000 and K'000

As at 31 December 2013		USD	AUD	EURO	GBP	Other	Total
Selling	FCY	(121,041)	(30,538)	(44)	(1,550)	(262,287)	-
	Kina	318,482	71,112	160	2,636	9,853	402,243
Buying	FCY	10,100	-	-	-	926	-
	Kina	(23,246)	-	-	-	(4,063)	(27,309)

As at 31 December 2012		USD	AUD	EURO	GBP	Other	Total
Selling	FCY	(35,634)	(4,709)	(3,966)	-	(7,489)	-
	Kina	75,347	10,443	10,551	-	1,413	97,754
Buying	FCY	16,068	-	-	4,116	-	-
	Kina	(33,285)	-	-	(14,085)	-	(47,370)

39. Policy liabilities for BSP Life Limited

Key assumptions used in determining this liability are as follows:

Discount Rates

For contracts which have a Discretionary Participating Feature, the discount rate used is linked to the assets which back those contracts. For 31 December 2013 this was 4.69% per annum (31 December 2012: 4.69% per annum), based on 5 year government bond rate and expected earnings from the investment portfolio. For contracts without DPF, a rate of 3.2% per annum was used at 31 December 2013 (31 December 2012: 3.2% per annum). For Accident business a rate of 3.2% per annum was used at 31 December 2013 (31 December 2012: 3.2% per annum). These rates were based on the 5 year government bond.

Investment and Maintenance Expenses

Future maintenance and investment expenses are based on budgeted expenses. Future inflation has been assumed to be 3.5% per annum (31 December 2012: 3.5% per annum) for determining future expenses.

Taxation

The rates of taxation enacted or substantially enacted at the date of the valuation (i.e. 20%) are assumed to continue into the future.

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39. Policy liabilities (continued)

Mortality and Morbidity

Projected future rates of mortality for insured lives are based on the Fiji Mortality Statistics tabled FJ90-94 Male. These are then adjusted by comparing with the Group's own experience. The mortality rates used was 70% of the FJ90-94 Male table.

Rates of Discontinuance

Best estimate assumptions for the incidence of withdrawal and discontinuance are based on the Group's experience and are reviewed regularly. Rates used for the long term insurance contracts are as follows:

	2013	2012
Whole of Life and Endowment Insurance	15%	15%
Term Insurance	18%	18%
Accident Insurance	14%	14%

Basis of Calculation of Surrender Values

Surrender values are based on the provisions specified in the policy contracts. There have been no changes to surrender bases during the period (or the prior periods) which have materially affected the valuation result.

Discretionary Participating Business

For most participating business, bonus rates are set such that, over long periods, the returns to contract holders are commensurate with the investment returns achieved on the pool of assets which provide security for the contract, together with other sources of profit arising from this business. Distributions are split between contract holders and shareholders with the valuation allowing for shareholders to share in distributions at a maximum allowable rate of 20% (31 December 2012: 20%). For business written between 1995 and 1998 the shareholder receives 11% of distributions.

In applying the contract holders' share of profits to provide bonuses, consideration is given to equity between generations of policyholders and equity between the various classes and sizes of contracts in force. Assumed future bonus rates included in the liability for the long term insurance contracts were set such that the present value of the liabilities equates to the present value of assets supporting the business together with assumed future investment returns, allowing for the shareholder's right to participate in distributions.

Reinsurance

Contracts entered into by the Company with Reinsurers under which the Company is compensated for losses on one or more contracts issued by the Company, are classified as reinsurance contracts.

As the reinsurance agreements provide for indemnification by the Reinsurers against loss or liability, reinsurance income and expenses are recognised separately in the statements of comprehensive income when they become due and payable in accordance with the reinsurance agreements.

Reinsurance recoveries are recognised as claims recoveries under the statements of comprehensive income. This is netted off against the claim expenses. Reinsurance premiums are recognized as Reinsurance Expenses.

Notes to the Financial Statements

for the year ended 31 December 2013

40. Events occurring after balance sheet date

No matters or circumstances have arisen since the end of the financial year which significantly affected or may significantly affect the operations of the Bank and the Group, the results of these operations, or the state of affairs of the Bank and the Group in future financial years.

41. Remuneration of auditors

	Consolidated		Bank	
	2013	2012	2013	2012
<i>All amounts are expressed in K'000</i>				
Financial statement audits	2,707	2,496	2,110	1,423
Other services	4,413	8,731	4,413	8,731
	7,120	11,227	6,523	10,154

The external auditor Deloitte Touche Tohmatsu is also engaged in providing other services to the Bank and Group as required. The provision of other services included secondment of staff to BSP Capital Limited, due diligence and board strategy planning.

Independent Audit Opinion to the members of Bank of South Pacific Limited and subsidiaries

We have audited the accompanying consolidated financial report of Bank of South Pacific Limited and subsidiaries which comprise the consolidated statement of financial position as at 31 December 2013, the consolidated statement of comprehensive income, consolidated statement of changes in equity and the consolidated statement of cash flow for the year then ended, and a summary of significant accounting policies, other explanatory information and the directors' declaration.

Director's Responsibility for the Consolidated Financial Statements

Directors are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with the Companies Act 1997 and International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Audit Opinion

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Bank of South Pacific Limited and subsidiaries as at 31 December 2013, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on Other Legal and Regulatory Requirements

The financial report of the Bank of South Pacific Limited and subsidiaries is in accordance with the Companies Act 1997 and proper accounting records have been kept. Bank of South Pacific Limited and subsidiaries are in compliance with the Banking and Financial Institutions Act 2000 and other applicable acts and regulations.

During the year ended 31 December 2013 we also provided Bank of South Pacific Limited with tax and consulting services.


DELOITTE TOUCHE TOHMATSU


Suzaan Theron

Registered under the Accountants Act 1996
Partner, Chartered Accountants

Port Moresby, 26th day of March 2014

