



ANNUAL REPORT  
**2009**



Bank of South Pacific Limited

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## THE VISION

***"To be the  
leading bank in  
the South Pacific"***

The key features of BSP's **strategy**:

- *A focus on sales and services*
- *Operational excellence*
- *High performing teams*
- *Profitable growth*



...your bank's locations



**BSP - Fiji**



**BSP - Solomon Islands**



**BSP - Niue**





**NN Beangke** Chairman

Once more BSP has achieved a record result in 2009, a year which commenced with a significant level of uncertainty as to the extent and impact of the global financial crisis in PNG.

Some of the Bank's achievements over the year were:

- After tax net profit of K257.1 million, an increase of 12.6% on the after tax net profit of K228.3 million reported in 2008;
- Shareholders rewarded with a dividend payment of K100.31 million in July 2009, representing 2.2 toea per share and 44% of the 2008 net after tax profit;
- Tier 1 capital ratio of 18% and regulatory total capital ratio of 22.1% and maintaining its "well capitalised" status;
- Return on equity remained in excess of 30%;
- Cost to income ratio of 46% as the bank embarked on its re-investment program;
- Continued organic growth in customer deposits of K973 million to K6,759 million with market share of 53.27% in Papua New Guinea;
- Loans and advances organic growth of K517 million to K2,860 million with market share of 51.81% in Papua New Guinea.

The balance sheet growth reflects not just continuing stable organic business growth of BSP in PNG and its Pacific Island branches; BSP added a further K1,430 million of assets (along with 20 bank branches) through the acquisition of the National Bank of Fiji (trading as Colonial National Bank) and Colonial Fiji Life Limited

in Fiji from the Commonwealth Bank of Australia in November 2009, to unambiguously underline the Bank's expansion strategy in the Pacific region.

As mentioned in the highlights section, BSP's capital base remains in the "well capitalised" status as defined by the regulator, the Bank of Papua New Guinea. Group Capital adequacy is 22.1%, a reduction from the 28.8% level as at year-end 2008, reflecting the strong growth in BSP total balance sheet assets.

The maintenance of capital at sufficient levels to accommodate growth as well as to provide a cushion against real business risks in the Pacific is central to the long term strategy and planning of the BSP Group. As part of this strategy, in 2009 the bank raised K75.5 million in capital through an inaugural issue of term subordinated notes in PNG, and in March this year, embarked on a convertible note Issue in Fiji.

BSP continues at the forefront of the development of electronic banking facilities in the Pacific region. In 2009, BSP introduced SMS banking to the PNG market and over 45,000 users had subscribed to this product by the end of 2009. During the year 54 new ATMs were installed in PNG, of which 11 were additions to the ATM network, along with GPRS eftpos machines in selected locations. There were 11 ATMs commissioned for deployment in the Solomon Islands, and soon after the acquisition of the National Bank of Fiji, 40 ATMs were purchased for installation in Fiji.

The PNG economy showed resilience despite the depressed economic conditions experienced by many of its major trading partners in the aftermath of the global financial crisis. Key economic data in 2009 included:-

- GDP growth estimate of 4.5%;
- Inflation of 5.3%;
- Easing of monetary policy by Bank of PNG with the Kina Facility Rate reduced by 1% to 7% in December 2009;
- Foreign reserves increased to US\$2,452m (K6,556m) at the end of 2009 representing approximately 10 months import cover and 14 months non-mineral import cover;
- Total employment increased by 3.8%

The Solomon Islands and Fiji economies remained more subdued during the year. In the Solomon Islands the economy remains heavily reliant on timber and fish exports and the RAMSI assistance programme continues to be beneficial to the economy. Fiji experienced flooding and cyclones in 2009 which affected tourist numbers and the associated inflows from this sector. Nevertheless business confidence remains positive and BSP growth expectations are sound.

The acquisition of the Fiji Colonial Group business from

Commonwealth Bank of Australia was a significant achievement for BSP. This investment is the largest since the purchase of and amalgamation with PNGBC in 2002, and continues BSP's strategy of expansion across the Pacific. I extend a special welcome to all our new staff and customers in Fiji.

I thank all staff and the executive for their commitment and dedication throughout 2009, that has seen the bank continue to achieve strong results under challenging circumstances. With their continued support the bank will be well placed to meet exceptional challenges and opportunities in the future.

To all shareholders and my fellow Board members – I acknowledge with thanks your ongoing support and look forward to reporting

another year of achievement by BSP in 2010.

**N N BEANGKE**  
Chairman





**BSP Head Office** Port Moresby

- 1957** — The Bank commenced operations on 1 May 1957 in Port Moresby as a branch of the National Bank of Australasia Limited.
- 1974** — Operations were later expanded to several centres and on 17 May 1974 the Company was incorporated as Bank of South Pacific Limited, a wholly owned subsidiary of the Australian parent, with a paid-up capital of K2.00 million.
- 1980** — In April 1980 and August 1981, a total of 300,000 ordinary fully paid shares of K1.00 were issued to the public in Papua New Guinea, thus increasing the paid-up capital to 2,300,000 fully paid K1.00 shares.
- 1993** — On 24 August 1993, the nationally owned company, National Investment Holdings Limited (NIHL) acquired the 87% shareholding held by National Australia Bank. On 25 October 1993, 100% ownership of the Bank was achieved by NIHL, which later changed its name to BSP Holdings Limited.
- 1995** — In December 1995, BSP Holdings Limited completed a successful capital raising of K2.70 million by way of a Convertible Note Issue. The holding company took up an additional 2,700,000 fully paid shares of K1.00 in Bank of South Pacific Limited, increasing the issued capital to K5,000,000.
- 1998** — In October 1998, BSP Holdings Limited raised K12.90 million through a Rights Issue of shares at K3.00. During December 1998 BSP Holdings Limited went into voluntary liquidation and its shareholders now hold shares in Bank of South Pacific Limited.
- 2001** — In 2001 the Privatisation Commission, on behalf of the Government of Papua New Guinea, offered for sale a 51% interest in the Papua New Guinea Banking Corporation (PNGBC) through

a competitive trade sale process. The Company participated in this process by lodging a bid whereby it proposed to effect the acquisition of PNGBC by way of an amalgamation under the Companies Act rather than through a sale and purchase.

- 2002** — Following an appraisal of all bids lodged in relation to the acquisition of PNGBC, the Commission agreed to accept the Company's bid. The Company, the Commission and the PNGBC executed the amalgamation deed in December 2001 which provided for the implementation of the amalgamation. The amalgamation was completed on 9 April 2002.
- 2003** — The Company's shares were listed on the Port Moresby Stock Exchange on 27 August 2003.
- 2004** — In 2004, the Company returned a profit after tax of K86.65 million up from the K39.98 million result in 2003. As at 31 December 2004, shareholders' equity reached K255.63 million. During 2004, the Bank acquired the Niue Branch operations of Westpac Banking Corporation.
- 2005** — In November 2005, Standard & Poors (S&P) issued an inaugural credit rating for Bank of South Pacific Limited. The rating was B+ Stable, consistent with the S&P sovereign rating for Papua New Guinea.
- 2005** — 2005 saw continued strong financial performance and balance sheet growth. Profit after tax increased to K99.22 million. Total assets increased to K2.95 billion and shareholders equity grew to K308.30 million. Market capitalisation reached K1.40 billion. During this year, Capital Stockbrokers Limited was acquired and renamed BSP Capital Limited.
- 2006** — Strong balance sheet growth with total assets reaching K4.33 billion and a 12.50% increase in after tax profit to K111.62 million continued the strong growth and financial performance during 2006.
- 2006** — On 18 December 2006 a BSP branch was established in Suva, Fiji following the acquisition of the Habib Bank Ltd interests in Fiji.
- 2007** — The acquisition of the National Bank of Solomon Islands Ltd was completed during April 2007. Now rebadged as a branch of BSP, it has the largest branch network in the Solomon Islands.
- 2007** — Outstanding performance continued during 2007. Total assets increased to K5.80 billion, after tax profit increased by 71% to K191.07 million and market capitalisation to K3.28 billion. Expense to income ratio reduced to 39.40%.
- 2008** — Performance was strong for the year despite the broader effects of downturn in the global economy beginning to impact the PNG economy in the last half of the year. After tax profit continued to grow, with an increase of 19% over the prior year, despite the BSP Capital CDO provisioning of K50 million. Strong balance sheet growth continued despite these effects with total assets increasing by 17% to K6.8 billion and capitalisation increasing by 33% to K4.3 billion.
- 2009** — BSP posted sound results as the global economic downturn continued, increasing after tax results by 13%; BSP acquired the National Bank of Fiji and Colonial Fiji Life Insurance Limited from Commonwealth Bank of Australia, contributing K1.2 billion to assets growth of K2.6 billion.





**Noreo Beangke, BA (Ec)**

*Chairman*

Director since August 1993.

Appointed Chairman May 1994.

Noreo Beangke holds a Bachelor of Economics degree from the University of Papua New Guinea. Mr Beangke is also Chairman of PNG Coffee Exports Ltd, and a Director of New Guinea Islands Produce Ltd and Credit Corporation (Fiji) Limited.



**Ian B Clyne**

*Chief Executive Officer*

Director since December 2008.

Ian Clyne was appointed as Chief Executive Officer by the Board of Bank South Pacific Limited on 17 October 2008. He has had a distinguished career in banking and finance, his most recent appointment was Executive Vice President and Managing Director, ING Bank Śląski Group, Poland. During his career Mr Clyne, a Bachelor of Business graduate from the Curtin University, Perth, Western Australia, has held senior banking appointments in Australia, PNG, Pakistan, Hong Kong/China, France, UK, Singapore, Indonesia, Italy, and Poland, during a career with the Indosuez Bank, ING Barings and Lippo Bank. Prior to embarking on an international banking career, Mr Clyne worked in Papua New Guinea with Nambawan Finance Limited and Indoniu Finance during 1980-1986.



**Tom Fox, OBE, BEc**

*Non-Executive Director*

Director since June 1993.

Thomas Fox is currently an Executive Director of Kramer Group Limited. He holds a Bachelor of Economics degree from the University of Papua New Guinea. He commenced his career with the Reserve Bank of Australia, and gained wide experience in senior management roles within semi-government institutions, and private sector companies, which included serving as the Managing Director of the Investment Corporation of Papua New Guinea for 8 years. His other current directorships include, PNG Sustainable Infrastructure Ltd, Capital Life Insurance Company Ltd. Mr Fox is also a trustee for the Institute of National Affairs, and a foundation member and fellow of the PNG Institute of Directors.



**John Jeffery**

*Non-Executive Director*

Director since June 2001.

John Jeffery had a long and successful career in Australia before moving to Papua New Guinea in 1986 to take up a position at Madang based James Barnes PNG Limited. Mr Jeffery's directorships include Chairman NASFUND and The Tower Ltd. He also continues to serve as President of the Employers' Federation of PNG and is a founding member of the PNG Institute of Directors Inc.



**Gereia Aopi, CBE, MBA**

*Non-Executive Director*

Director since April 2002.

Gereia Aopi has achieved several tertiary degrees in Papua New Guinea, and a Masters of Business Administration from the University of Queensland. His career began with the PNG Development Bank and progressed through a variety of positions to Managing Director. He currently holds the position of General Manager, PNG with Oil Search Limited. Mr Aopi is also currently a director of Steamships Trading Company Limited, POMSox Ltd, Niu Marsh Ltd, Kumul Hotels and Endeavour Properties Ltd and is the Chairman of Telikom (PNG) Ltd and Chairman for Independent Public Business Corporation.



**Dr Ila Temu, PhD, MEd**

*Non-Executive Director*

Director since 2003.

Dr Temu achieved a distinguished academic career with the University of Papua New Guinea, the National Research Institute, the Australian National University and the University of California, Davis USA where he was awarded his Ph D. Dr Temu entered the private sector during 1996 when he was appointed Managing Director, Mineral Resources Development Company and during 2000 he accepted the appointment as General Manager, Government Relations, Placer Niugini Ltd. He is a member of the Management Group for the PNG Incentive Fund and an executive member of the Employers' Federation of Papua New Guinea.



**Sir Nagora Bogan, KBE, LLb**

*Non-Executive Director*

Appointed a director in 2003.

Sir Nagora Bogan graduated with a Bachelor of Law from the University of Papua New Guinea in 1978. In 1992 Sir Nagora was appointed Commissioner General of the PNG Internal Revenue Commission. In 1996, he was appointed as PNG's Ambassador to the United States with accreditation as Ambassador to Mexico and High Commissioner to Canada. In 2002 Sir Nagora became a private business entrepreneur. He is Chairman and CEO of In Touch Media Ltd, a multimedia/record label company, Chairman of the Board of POSF Limited and Director on several private company boards. Sir Nagora received his knighthood during 1997 in recognition of his distinguished public service.



**Lyle Procter, MEd, FFin**

*Non-Executive Director*

Director since July 2004.

Lyle Procter has been a career central banker, having spent 36 years with the Reserve Bank of Australia. He also spent several years with the Australian Department of Foreign Affairs. Since retiring from the Reserve Bank Mr Procter has worked as a consultant to the International Monetary Fund, Washington, and the Asian Development Bank, Manila. He has also worked privately as a consultant to the Australian banking industry, and in several South-East Asian countries. Other current directorships include Sun Hung Kai and Co. Ltd and Quality HealthCare Asia Ltd.



**John Kapi Natto, BA, B Ed Hons**

*Non-Executive Director*

Appointed a Director in 2006

John Kapi Natto graduated from Hobe Sound Bible College, Florida USA in 1989 with a Bachelors Degree in Education and also graduated from University of Papua New Guinea with a Bachelor of Education (Honours) Degree in 1991. He is currently the Managing Director of Kutubu Security Services Ltd which provides total security services to the Oil Search operations in Kutubu, SHP. Mr Natto is the Chairman of Namoporo Landowners Association Inc and Petroleum Resources Kutubu Ltd.



**Kostas Constantinou,**

*Non-Executive Director*

Appointed a Director in 2009

Kostas Constantinou joined the Bank South Pacific Board in April 2009. He is a prominent businessman and is a Director of several private companies including Airways Hotel & Apartments Limited, Lamana Hotel Limited, Lamana Development Limited, Hebou Constructions Limited, Heritage Park Hotel Limited and Gazelle International Hotel Limited. As well as Bank of South Pacific, Mr Constantinou holds two other public company Directorships - Airlines of Papua New Guinea Limited, which is a POMSoX listed company and Oil Search Limited which is dual listed entity on POMSoX and the ASX. He serves on the Remunerations & Nominations Committee for both organizations and is a member of the PNG and Australia Institute of Company Directors. Mr Constantinou also holds a number of high level public sector appointments and serves as Chairman of the National Physical Planning Board of Papua New Guinea and Deputy President of the Employers Federation of Papua New Guinea. He is the Honorary Consul for Greece in Papua New Guinea and Trade Commissioner of Solomon Islands to Papua New Guinea.



**Ian B. Clyne** Chief Executive Officer

### INTRODUCTION

I take great pleasure & pride in reporting to shareholders that BSP has achieved another record result. Our net profit increased by K28.74m to K257.12m, a 12.6% improvement on BSP's 2008 results. As our Chairman's Report indicated, this performance was characterized by continued sound growth in terms of Total Deposits -16.8% to K6,759m, and Total Loans - 22.1% to K2,860m. BSP Group's Total Balance Sheet now exceeds K9 billion.

This has been a remarkable achievement when one considers the many uncertainties faced by the banking & business sectors as a result of the Global Financial Crisis (GFC) which has had a very severe impact on many international economies.

A significant amount of time and effort was devoted by BSP to Capital & Liquidity Management to mitigate as much as possible any additional risks associated with these uncertain times. Fortunately for PNG, mineral, oil & gas, and general commodity prices recovered much earlier than economic forecasts, and PNG remained relatively unaffected by the global financial crisis.

As part of our capital planning strategy BSP launched a "Subordinated Notes" issue in the first half of 2009. This was the first ever note issue of this type in PNG and raised K75.5 million. These notes are now listed and traded on POMSIX. BSP is currently undertaking a "Convertible Note" issue in Fiji to raise Fiji dollar liquidity to support our expanding Fiji operations, and to encourage Fiji equity participation in BSP inline with our Pacific expansion strategy.

From an investor's perspective, all BSP's key performance indicators remain sound. These include a return on equity of 30.7%, earnings per share of 5.6 toea, and a cost income ratio of 46%.

### THE BANK

BSP is now very much a "forward looking" institution. In early 2009 we commissioned an "independent" review of all BSP business units to simply understand our strengths, weaknesses & challenges. Financial Access an International consultancy that specialises in advising emerging market banks was contracted to undertake the study. Based on their review a comprehensive "modernisation" strategy was approved by BSP's Board of Directors. The aim of this initiative is to firstly, position BSP to be able to fully participate in

the increased economic activity that will accompany the PNG LNG Project, secondly significantly improve BSP's general banking service levels in terms of products, processes, systems and improve overall staff training levels and ultimately improve "customer service" levels. Finally to ensure that BSP has the structure and ability to support the continuation of our Pacific expansion strategy.

As a direct outcome of this review BSP introduced a new organisational management structure, and has initiated a major capital "renewal" program of all our IT hardware & software. PricewaterhouseCoopers have also been contracted to review & map all BSP branch processes to identify & assist BSP to implement streamlined workflow processes throughout our branch network. Ultimately many current manual processes will be automated. This is a major project which kicked off towards year end & will continue throughout 2010 & 2011. We believe major customer service level improvements should be achieved, as well as significant cost benefits from the elimination of inefficient, time consuming manual processes.

KPMG have also provided extremely valuable assistance by managing BSP's new 3 year Medium Term Strategic Planning Review which covered every business unit. This review was undertaken in September 2009 and formed the base for our 2010-12 budget plan which was submitted to the Board of Directors & subsequently approved. This review process will be conducted on an annual basis as part of our normal budgeting & strategy process. The 2010-12 outcomes of this review very much supported the need to continue to implement the "modernisation" program highlighted by the Financial Access Report.

The re-branding of Bank South Pacific to BSP was very much part of our modernisation & change program. We want to make BSP a more energetic, young, modern community orientated Pacific Bank. The re-branding has had an extremely positive effect both from our customers perspective, and from our staff's perspective. BSP is now clearly the Number "One" bank in PNG, and ultimately the Pacific. The re-branding has also been rolled out to the Solomon Islands & Fiji and received a very positive reception.

BSP is now one of the leading companies in PNG in terms of supporting community and sporting projects. We are committed as a responsible corporate citizen to give back to the people & communities in which we operate. Our focus is very much children & youth programs in education, health & sport. Our young people are the future of our nation and deserve our support. The BSP School Tennis program was attended by 18,000 children in the 10 towns where it was conducted in 2009. BSP branches were also each given K20,000 to support a local community project, our only requirement was that staff actively participated & gave their time – this has been an outstanding success.

BSP's "love your bank" program is focused on our communities programs around PNG & the Pacific.

### NEW PRODUCTS AND SERVICES

BSP launched SMS banking early in the year and now has over 45,000 users. We also successfully launched operating & novated lease products for our corporate clients. A major service improvement initiative has been the expansion of BSP's ATM Network, BSP currently has 160 ATM's in PNG, with plans to exceed 200 ATM's in 2010. Over 2 million ATM transactions are now conducted each month by our customers in PNG using BSP's ATM network. We strongly believe we can significantly reduce branch over crowding by the continued expansion of our ATM network. GPRS EFTPOS terminals have also been launched to further support retailers around PNG. BSP is committed to being the leader in electronic banking services in PNG & the Pacific.

Fraud continues to be a serious operational risk for BSP. A major fraud spanning 5 years was uncovered in mid 2009. BSP prior to this date had already initiated a number of improvements in our operational risk management having established a new operational risk team whose objective is to constantly review the key risk components of BSP's operations in terms of Processes, Systems and People. BSP has also purchased a major Anti Money Laundering Software that can identify unusual transactions. A major focus of BSP in our 'modernisation' strategy is to significantly reduce operational risks. BSP has a "Zero" tolerance policy regarding staff frauds and has ensured that all fraud cases are reported to the police & those involved are charged & dismissed. Corruption is not just a BSP problem, but a general business & community problem, it is seriously impacting all levels of PNG society & restricts economic development, especially in terms of expanding services to the less developed communities.

**EXPANSION**

BSP is now truly a Pacific bank. The successful acquisition of the Colonial Group in Fiji from the CBA was a major achievement for BSP in 2009. This was a major project for BSP, the due diligence process was conducted on an extremely professional basis and I would like to personally congratulate everyone involved throughout the acquisition process.

BSP Fiji has the largest branch network in Fiji, BSP is now the largest Retail Bank in Fiji.

The acquisition has given BSP an important presence in the Pacific and enormous opportunities for future expansion.

**THE YEAR(S) AHEAD**

2010-12 are years of enormous challenges and opportunities. BSP is committed to "Transforming" ourselves into a 21st Century bank. Every product, process, system is being upgraded or replaced. New customer service initiatives have already been identified and are in the process of implementation. BSP's "Core" Banking system is being upgraded, as is our communication infrastructure. Along with PwC's lead branch process redesign project, these are all 'major' project undertakings and are our Number one focus and priority. These projects are multi year projects, however customers will start to see "real" service improvement towards year end 2010, with "significant"

service level improvements in 2011/12 and beyond.

BSP is committed to opening new branches in Porgera, Harbour City & Vision City in Port Moresby in 2010, and potentially Tari in 2010/11. Our ATM Network will continue to expand to more than 200 in PNG, Fiji 90, and Solomon Islands 8 by year end 2010.

BSP will also launch a "Rural" banking initiative based on technology solutions to try to take cost effective banking services to many un-banked rural communities. Electronic banking & SMS Banking will continue to be further expanded in Fiji & Solomon Islands.

BSP will continue to look for interesting expansion opportunities in the Pacific.

**CONCLUSION**

BSP has a bright & positive future. Our "Transformation" & "Modernization" programs are the largest projects BSP has ever undertaken. The benefit to our customers will be better product offers, better service and more ways to access your money. For BSP staff it will mean more efficient, less laborious processes, improved training leading to greater job satisfaction & greater career opportunities and rewards. For our shareholders we aim to achieve greater profitability, leading to greater shareholder value.

BSP is committed to this "Transformation" and "Modernization" path.

I sincerely thank all BSP Executives, Management and Staff for their efforts in 2009, and their acceptance of and enthusiasm for the new BSP which we are now building for the future.



**IAN B. CLYNE**  
Chief Executive Officer



Ian B. Clyne BSP Love your bank launch





**Executive Management team** Back row (L-R) Robin Fleming, Ian B Clyne, Peter Dixon, Frans Koote. Front row (L-R) Aho Baliki, Ian Mason, Johnson Kalo and Giau Duruba (**absent**) Hans Abma

The daily execution of the Bank's business operations is the responsibility of the seven strategic business units (SBUs), Retail Bank, Corporate and International, Paramount Banking, Credit and Risk, Human Resources, Operations and Finance & Planning.

Highlights of each SBU performance in 2009 include:

### RETAIL BANK

The SBU Retail Bank looks after the personal and small business customers of Bank South Pacific across its combined network of 63 branches in Papua New Guinea, Solomon Islands, Fiji and Niue and almost 200 ATM's and over 2000 EFTPOS machines. It looks after their loan requirements, deposit requirements and transactional banking needs.

### 2009 Highlights

The most dramatic change in Retail Bank which took place in 2009 was the introduction of a new organization structure. This restructure of the organization is part of the bank's modernization process which started this year. The objective of this change is the creation of a pro-active and sales-driven organization with the focus on delivering an excellent service and products developed based on clients needs.

An important part of this strategy is to keep on improving our delivery channels. The most important initiative in this area

was the introduction of SMS banking. SMS banking allows BSP customers to use their mobile phone to check their balances, obtain information about their 3 last transactions and transfer money to BSP accounts.

Another important channel to support our customers is our ATM network. We continued to increase our ATM penetration in the Pacific. In PNG the number increased to 155 machines, in the Solomon Islands installation started with 11 machines and 42 machines were deployed to Fiji late in the year.

The number of EFTPOS machines is growing rapidly especially since the introduction of the fast wireless Mobile (GPRS) and IP devices which have been well received by our business clients.

Finally we started with the upgrade of our main delivery channel which is our branch network. This improvement process of refurbishment and moving counter lines to make more room for clients and rebranding will continue in 2010.

In 2009 we started a project to improve all our products, procedures and processes. The reduction of bureaucracy, an optimal automation of the different processes and more attractive product packages must lead to further growth of our active client base and an increase in the sale of our products.

As part of its corporate responsibility in PNG, BSP initiated a community projects program throughout the branch network. BSP

has the strong belief that the bank has a responsibility to help each of the communities in which it operates. Branches were required to identify potential community projects which would benefit the community in the areas of Education, Health, Sports and Social, which allowed for the hands on participation of our bank staff in the delivery of the project. Over 30 projects were delivered in 2009 such as the refurbishing of local hospital wards and health clinics, renovating, rebuilding and repainting classrooms in local schools, bringing the opportunity for health checks to the people and supplying and installing with professional guidance, water tanks to schools where children previously did not have access to clean water supplies.

### 2010 Challenges

Like 2009, 2010 will see a focus on a further improvement in our customer service standards and an expansion of our outreach. Besides investing in the refurbishment of the current branches and the projects to improve the processes and reducing the queues in the branches, BSP will set up special branches to service high net value customers.

In 2010 BSP will open up the access to financial services and improve financial literacy in the rural parts of PNG by setting up a large network of agents. This will include customer education programs and programs to build a better savings culture in all areas of PNG.

We will continue with surveys to measure customer satisfaction, using the feedback together with continued automation of the processes to drive customer service to a higher level.

We will increase the size of our electronic banking network in Papua New Guinea significantly with additional ATM's and we will expand the functionalities of the ATM's and SMS banking.

Enhancements will be made to our internet banking suite to provide an easier customer interface and the ability to make payments to other BSP account holders and accounts at other banks.

### CORPORATE AND INTERNATIONAL

Corporate & International forms a major part of BSP's Wholesale banking operations. The Corporate & International SBU comprises four functional business units being Corporate Lending, Commercial Lending, Business Lending and Treasury.

As a result of an organisational restructure in the second half of 2009, the International Operations business unit, which was previously controlled by Corporate & International, now falls under the control of the Operations SBU of the bank.

### LENDING

Lending growth in 2009 remained strong despite concerns with possible flow-on impacts of the global financial crisis on the PNG economy and domestic interest rate rises in the first quarter of

2009. The total BSP wholesale lending portfolio grew by 24.8% over 2009.

Significant lending growth was achieved in both the Corporate and Commercial lending units, with a slowdown in Business lending growth in 2009 after very strong growth in this area over the previous 3 years.

BSP maintained its dominant market position in terms of PNG lending, with the bank increasing its share of the Kina lending market to 53.5% at the end of 2009 from 50.7% as at the end of 2008. Despite continued solid lending growth in 2009, credit policy remained prudent to ensure the maintenance of a quality Wholesale lending portfolio.

BSP's team of professional and experienced Relationship Managers continued to provide BSP with a competitive advantage in the market, with 2009 seeing further consolidation of relationships with our valued Wholesale clients and a proactive approach adopted in identification of quality credit opportunities.

A major strategic planning exercise was conducted across all SBUs in the second half of 2009, with 3 year strategic plans developed as a blue print for the improvement and growth of the BSP business. Strategic initiatives developed for the Corporate & International SBU will be progressively rolled out across 2010, with more efficient processes and enhanced product offerings to result in improved standards of customer service and satisfaction.

BSP takes pride in the role it plays in terms of development of PNG's business entrepreneurs and a further series of successful small business workshops were conducted in major centres across PNG during the year.

In terms of future prospects, the PNG LNG project will of course provide significant opportunities for BSP to grow its Wholesale business. Whilst growth targets are difficult to quantify at this stage, the project impact will see the emergence of many new business opportunities across a number of economic sectors.

The Wholesale team capacity will be strengthened to ensure sufficient resources are available to cope with the demands of the LNG project and product and service offerings reviewed and enhanced to ensure the suite of Wholesale products and services on offer is in keeping with customer demand and expectations.

Going forward, the Corporate & International business of BSP's international branches will be controlled on a Group basis from PNG in a move to more functional reporting lines and to improve on service delivery. Despite challenging political and economic conditions in Fiji, good potential exists in that market to grow BSP's Corporate & International business in the years ahead.

### TREASURY

The Treasury Business Unit within the Wholesale SBU manages the Bank's foreign exchange and domestic money market activities.

Treasury' foreign exchange earnings fell during the year despite a 24% increase in year-on-year turnover. Competitive pressures were the main driver of compressed spreads especially within the mining sector in conjunction with an extremely illiquid market during the first half of the year. Reliance of earnings from the mining sector was mitigated to an extent with increased activities in cocoa, coconut oil & palm oil sectors. Foreign exchange earnings are expected to increase strongly in 2010 on the back of LNG activities.

Interest earnings on liquid assets in 2009 significantly surpassed budget expectations due to opportunities gained by investing higher volumes of depositor funds in short-term government securities. Domestic liquidity tightening due to withdrawal of depositor's funds for LNG activities combined with lower interest rate yields may reduce interest earnings on liquid assets in 2010.

Five Treasury officers completed the Australian Financial Markets Association Core Accreditation course in 2009 and are expected to complete the Foreign Exchange Markets Module this year. From a risk perspective, the Bank and in particular Treasury will benefit from the time being invested in Financial Risk modeling tools in line with world best practice.

### PARAMOUNT BANKING

Paramount Banking continued its success story by providing high quality of service to the Bank South Pacific's high value client base through relationship management of the Bank's large liability customers.

Highlights for the year included: -

- Depositors' funds, remained to a consolidation level of over K3.25 billion during 2009, considering it was a year of financial uncertainty.
- Continued enhancement of our strategic partnership with the National Government and Donor Aid Groups with target expansion of the Bank's electronic banking network.
- Continued support of the National Government's District Services Improvement Program and Treasury rollout.

In 2010, Paramount Banking will continue to refine its service delivery strategies through:-

- Working closely to support our major clients in their endeavours to achieve their business and strategic goals.
- Improving the delivery and quality of service via our Paramount Banking Service Centres.
- Commencing the upgrade and refurbishment of Paramount Banking Service Centres, which includes Lae, Madang, Kokopo and three locations in Port Moresby (Boroko, Port Moresby and Waigani).

Paramount Banking aims is to be different to its competitors by being the Banker of choice for its high value net worth and liability clients.

### CREDIT AND RISK

As with all strategic business units within the bank, the structure and functional responsibilities were reviewed in conjunction with international consultants Financial Access. An outcome of the review was a more focused approach to audit and risk management within the bank with the separation of Audit and Risk functions by way of the creation of a new Operational Risk business unit and the establishment of a new Credit Inspection business unit.

The realignment also resulted in a further strengthening of the bank's corporate governance framework with Audit business unit and Legal business unit reporting directly to the Chief Executive Officer under the revised structure. Lending Support, which attends to loan document preparation, loan document custody and settlements, came under the control of the Chief Operating Officer's strategic business unit during the year.

During 2010 all business units will be involved in the integration of the Colonial Fiji business into BSP. There will also be significant project activity associated with process and system transformation.

### Credit

During 2009 the bank continued to experience significant lending growth largely driven by the Corporate lending sector on the back of major capital expenditure programs particular in the Mining & Resource, Property and Infrastructure Sectors. There was a slow down in lending to the small to medium enterprise customers as a result of slower economic growth of PNG in 2009. The Bank of PNG maintained stable interest rates through 2009 after various rate rises in 2008 that slowed inflation and economic growth.

Economic activity is expected to return to a higher growth rate through 2010 with the final approval of the LNG project in PNG having been given in December 2009. Construction and development work will progress this year which is expected to drive economic activity in all customer segments.

All asset quality indicators remain sound, a reflection of the Bank's very proactive approach to identification of early warning signs and ongoing management of problem loans.

Lending Policies and Procedures continue to be reviewed on an ongoing basis with numerous changes implemented in 2009 as a result of the changing economic conditions in PNG and globally. There will be significant activity in 2010 associated with the continuing improvement of the banks approach to, and management of credit risk.

Integration of the credit function in the Fiji operations acquired in December 2010 has commenced to ensure no interruption to our customers' lending needs are experienced and BSP policies and procedures are maintained in all parts of our operations.



### Asset Management

The buoyant property market continued through 2009 and this again reflected in the many number of customers with non-performing loans voluntarily disposing of assets alleviating time consuming and costly mortgagee sales.

Fiscal performance exceeded that of 2008 and there was an increase in recoveries associated with asset sales, which in part was a reflection of higher values in the property market. As would be expected in periods of substantial asset growth there were some larger loans that have migrated to non accrual status. Overall non performing loan to total advance ratios remained consistent with past years however.

Court litigations continued to be adversely affected by delays from time to time but the bank continues to progress these legal actions, as shareholders would expect.

### Audit

The Audit and Risk Business Unit was restructured during the latter half of 2009 and three separate business units created – Audit Business Unit; Operational Risk Business Unit and Credit Inspection Business Unit.

This was carried out to accommodate and strengthen the Bank's on going corporate governance principles in providing specialised and enhanced risk management and audit functions across all of the jurisdictions that it operates within.

The Bank has its main Audit team based in Port Moresby and a smaller team located in Honiara, Solomon Islands. Besides these teams, three Regional Audit Officer positions were created and filled in late 2009. These Regional Audit Officers are based in Mt Hagen, Lae & Kokopo and are responsible for closely monitoring branches within their regions each day, providing a more comprehensive coverage to ensure that the branches are complying with the bank's internal controls, policies & procedures.

### Credit Inspection

Credit Inspection is a new business unit, which commenced in November 2009. Key activities will be scheduled on site visitation/inspection of all wholesale business units across PNG, Solomon Islands and Fiji, with off-site/centralised inspection of selected retail business units. Credit Inspection may also undertake ad-hoc inspections based on specific factors, such as industry concentration or local economic factors. Reports will be tabled at the completion of each review, which will detail not only asset quality, procedural accuracy & remedial actions required, but also provide some credit analysis/writing guidelines to portfolio managers. Historically, a limited credit inspection function has been undertaken by external consultants and with the creation of this new business unit, it is envisaged that such future engagement may well be limited to key focus or specialised areas, working in conjunction with the new business unit.

### Legal Services

Legal Services department maintained effective service standards in respect of compliance with POMSOX reporting requirements, BPNG regulatory requirements, corporate compliance requirements, and also board secretarial functions within the bank. The department continued with its carriage of in house legal matters and internal legal advice to departments within the bank. Work was commenced on the creation of a compliance section within Legal Services to more effectively manage and monitor compliance functions across the bank.

### Operational Risk

The Operational Risk function was separated from Audit and Risk in late September 2009 to further strengthen the overall risk management capability of BSP.

As part of establishment of this new business unit, an Operational Risk Management Framework based on the Basel II Standardised Approach model was developed and is now in the process of being implemented across the bank.

A dedicated Operational Risk Manager has been assigned to each Strategic Business Unit to expedite the embedding of Operational Risk into their day-to-day operational activities, as well as enabling both Operational Risk and the Strategic Business Unit gain a better understanding of the risks that it is exposed to.

The Operational Risk Manager is also tasked with driving the various risk initiatives documented in the operational risk management framework such as mapping of the internal processes, identifying the key risks and mitigating controls, developing monitoring tools (key risk indicators), assisting Executives and Senior Management with regular risk reporting and providing risk awareness to all key staff within the bank.

## HUMAN RESOURCES

The Human Resources Strategic Business Unit provides support services to all the strategic business units in these core People Capital Management service functions namely; Recruitment & Selection, Training & Development, Performance & Benefits Management. The following HR activities were undertaken in FY 2009;

- developed a 3 year Strategic Plan for the HR SBU, with key focus on improving internal communication, staff training, key staff retention and improving HR operations;
- introduced a new HR Organisation structure, with four (4) key business units namely; Training and Central Administration, Talent Management & Development, Organisation Design and HR Strategic & Planning;
- introduced the revised core competencies dictionary with both the positive and negative behavioural standards for each

competencies, and are linked to the revised Performance Management System;

- revamped the Assessment Centre Recruitment Model with new sets of tests designed for specific job clusters to support Business Unit Managers in selecting the right staff for the right job;
- introduced new salary line policies for senior national managers, competitively pegged to the private sector salary line to retain our key management staff;
- developed and lodged the BSP three (3) year (2010 - 2012) Training and Localisation Plan, and subsequently obtained approved work permits/entry visas for all our expatriate staff well before the expiry date - 31/01/10.

In 2009, we experienced some marginal improvements in the HR metrics we normally benchmark our performance against. The staff turnover remained at 10% for the second time, which is an excellent outcome by PNG standards and the LNG impact. Total headcount increased to 2717 persons including overseas branches due to a combination of domestic volume growth, the commencement of the "Transformation" program, and the acquisition of the Colonial Group of Fiji from Commonwealth Bank of Australia.

Total training mandays increased marginally to 7568 from 7299 mandays in 2008, still maintaining the 3 mandays per person despite total headcount increase.

A number of key HR initiatives we planned to implement in 2009 like, Bank Intranet, 1 day Management workshops and CHRIS KIOSK System were actually developed, and/or sourced, but were put on hold due to the "Transformation" program in the Bank.

In line with the Transformation Program, and the business needs of the various Strategic Business Units of the Bank, the key focus for the HR SBU in 2010 are; staff training - "back to basics", staff recruitment and retention, and improving internal communications.

Therefore, we plan to implement these HR strategies to support the other Strategic Business Units;

- introduce staff selection policies and procedures manual and train key business unit managers to use these procedures in recruiting staff to fill their vacancies;
- develop and conduct product knowledge training targeting all employees in the Bank;
- support the business units to prepare job profiles for all generic roles in the respective business units under the new job profile format and align key information on the job profiles to recruitment, performance appraisal and training need analysis;
- introduce a new HR Management System to automate more HR Management processes in the Bank;
- re-hay all our positions and where needed introduce new

salary practice lines and benefits to key job grades in line with market trends;

- introduce a monthly HR newsletter featuring key information on the "Transformation" program and other HR policies/procedures changes in the Bank.

## OPERATIONS

The Operation SBU underwent a major re-organization, in terms of bringing all operational banking departments under a single organizational unit. This was done in line with international best practices in Banking. Units were transferred from Wholesale, Retail and Credit/Risk SBU's. The SBU now contains the following Business Units:

- Information Technology
- Project Management Office
- Branch Operations
- International Operations
- Channel Operations
- Lending Support
- Support Services
- Security Services
- Intranet/Documentation

Efforts are being undertaken to arrange all operational activities in a single location, though due to physical constraints this will not be entirely feasible in the short term. Plans have been raised to establish by 2012 a "Pacific Operations Centre" in Port Moresby, intended to hold ultimately all units, responsible for BSP's banking operations in the Pacific.

Apart from the above reorganization, the following notable projects were achieved. The first mobile EFTPOS terminals based on GPRS technology were introduced in the country. The public release of SMS Banking, unique to PNG, was completed, which now has over 45,000 users. The new optical document Archival Solution – BizeDocs was implemented, which will very significantly reduce printing costs and paper consumption by the bank. The sophisticated document management system will especially support lending/credit operations as well as boost efficiencies. In BSP Solomon Islands the core banking system was replaced and the system brought inline with BSP standards, that will ultimately apply for all BSP's organizational units in the Pacific.

In 2010, Operations will be focused on projects relating to the bank-wide Transformation Program to improve delivery of services and enhancement of efficiency. In parallel, Operations will work on following projects:

- Use state of the art MS SharePoint technology in order to complete an extended internal communication system, handling most documents and form flows.
- Restructure and re-design all operational processing within the Bank, in order to boost efficiency and straight-through-processing.
- Replace present Payment and Treasury solutions with more modern efficient systems.
- Continue ATM Rollout of over 100 new machines, while

- implementing a sophisticated monitoring environment.
- Further enhancements to BSP's network infrastructure, which is already the most extensive in the country.
- Mid 2010 the BSP's Internet Banking will be completely revamped and brought up to state of the art standards.
- Integrate all added operational units in various geographical locations (e.g. BSP/Colonial Fiji).
- IT is investing heavily in improving our staff skills levels through a number of in-house and external training courses leading to professional certifications.
- The data-centres and IT Infrastructure of the Bank will be further improved and enhanced.

### FINANCE AND PLANNING

Finance & Planning Strategic Business Unit (SBU) exists to deliver both financial and non-financial information that is accurate and complete for the purpose for which it is required, in a timely and efficient manner. Finance & Planning Strategic Business Unit continues to meet its compliance reporting and statutory responsibilities.

Internally, improvement in the overall quality, accuracy, timeliness and relevance of management information continued despite challenges in filling human resource needs in 2009.

Hiring people with accounting and finance skills remains a real challenge as there is increasing competition for these skills in the local market. Training of accounting & finance staff is ongoing and fully supported by management. Finance ensure that all employees are informed, well-trained, engaged and committed with an emphasis on staff to complete professional examinations with professional bodies like CPA PNG.

As part of BSP's organizational transformation, BSP Finance & Planning is focused on positioning itself as a true partner to all internal and external stakeholders.

In 2009, during formulation of the Transformation Program, Finance & Planning developed a strategy map defining and aligning key 'Finance Objectives' to the needs of Finance Stakeholders to achieve overall corporate strategy. These key strategic objectives included:

- Continued development of our technical capabilities and our understanding of the Bank and Group's business, as a basis for improved professional standards of service to the rest of the Bank and Group;
- Re-implementation of an integrated planning, budgeting and forecasting process, enhanced by simplified, automated processes;
- Updating and consolidation of Finance & Planning policies and procedures in line with BSP corporate governance framework;
- Improved business reporting practices and outputs, with emphasis on automation to achieve more responsive internal reporting for businesses;
- Modernise data ownership practices to help standardise information definitions and reporting routines;

- Ensure capital management planning is continuously adapted to support BSP's transformation and growth strategies.

Finance and Planning Strategic Business Unit has undergone a re-structure, to align itself to the new Finance strategy and meet the above objectives.

Ahead of us, BSP Finance & Planning has a set of strategic actionable plans based on the above objectives for delivery in the next three years. Work has already commenced, aiming to deliver initiatives within the transformation timeframe.







## The Core Values

These core values are shared by all at BSP. They serve to underpin, guide and shape everything we do as we work toward realising the vision of being the leading Bank in the South Pacific.

### **Integrity:**

Integrity defines our obligation as bank employees to embrace the highest level of ethical principles, meet the demands of compliance and care deeply about the preservation and promotion of standards of behaviour in our work place and in our community.

### **Leadership:**

We are leaders at Bank South Pacific, because we all understand that what we do and how we do it acts to influence and inspire others around us.

### **People:**

Our concept of people includes all who work in BSP, our customers, suppliers and shareholders and we are committed to considering their special needs and to treating each and every person with dignity and respect.

### **Professionalism:**

Being professional means that we are committed to continual self-development and achieving the highest possible standards in accord with the principles and practices that shape outcomes in the financial services industry.

### **Quality:**

Quality is a special value for BSP. It represents our pledge to being highly efficient in our use of resources, doing things as simply as possible, getting it right first time and consistently delivering superior customer service.

### **Teamwork:**

Our commitment to teamwork is based on the understanding that there is wisdom in all, that cohesive teamwork creates greater job satisfaction and that achieving our vision is only possible if we work enthusiastically as a team.

## CORPORATE GOVERNANCE

Bank South Pacific Ltd (BSP) has adopted an approach to Corporate Governance that is underpinned by its core values of Integrity, Leadership, People, Professionalism, Quality and Teamwork. This approach is supported by a comprehensive framework of Corporate Governance principles and policies. The BSP Board ("the Board") has demonstrated its commitment to developing and maintaining a standard of corporate governance that seeks to match global practice.

The Board ensures that it complies with the requirements of BSP home exchange, Port Moresby Stock Exchange ("POMSOX"). It also closely monitors developments in corporate governance principles and practice within Australia and has benchmarked itself against:-

1. ASX Corporate Governance Council "Corporate Governance and Best Practice Recommendations"
2. Australian Prudential Regulatory Authority Prudential Standard APS 510
3. Standard Australia AS 8000-2003 Good Governance Principles

BSP is mindful of the advantages of demonstrating to investors that its corporate governance standards meet the requirements expected of companies listed in countries such as Australia. This Corporate Governance Statement therefore compares BSP's corporate governance practices to the ASX Corporate Governance Council and Best Practice Recommendations.

BSP manages in excess of half the banking market in Papua New Guinea, and is predominantly owned by institutions and individuals in Papua New Guinea. The Board, Management and staff of BSP are very much aware of their responsibilities to the people of Papua New Guinea. The set of Corporate Governance principles developed by BSP is intended to provide a framework that will help to ensure that BSP deals fairly and openly with all its stakeholders – shareholders, customers and staff alike.

BSP publishes its corporate governance practices on its website. This is available at [www.bsp.com.pg](http://www.bsp.com.pg) in the shareholders section.

### 1 THE BOARD OF DIRECTORS

#### a) Role and Responsibility of the Board

The roles and responsibilities of the Board are defined in the Board Charter. This document also details the matters reserved for the Board and matters that have been delegated to management. The Board, with the support of its Committees, is responsible to the shareholders for the overall performance of the Company including its strategic direction; establishing goals for management; and monitoring the achievement of those goals with a view to optimising Company performance and increasing shareholder value.

Key functions of the Board include:

- overall strategy of the Company, including operating, financing, dividend, and risk management;

- appointing the Chief Executive Officer and setting an appropriate remuneration package;
- appointing General Managers and setting appropriate remuneration packages;
- appointing the Company Secretary and setting an appropriate remuneration package;
- endorsing appropriate policy settings for management;
- reviewing Board composition and performance;
- reviewing the performance of management;
- approving an annual strategic plan and an annual budget for the Company and monitoring results on a regular basis;
- ensuring that appropriate risk management systems are in place, and are operating to protect the Company's financial position and assets;
- ensuring that the Company complies with the law and relevant regulations, and conforms with the highest standards of financial and ethical behaviour;
- acquisitions and disposals material to the business;
- establishing authority levels;
- Directors' remuneration via the Remuneration & Nomination Committee;
- selecting, with the assistance of the Audit, Risk and Compliance Committee, and recommending to shareholders, the appointment of external auditors;
- approving financial statements.

A number of these responsibilities have been delegated by the Board to various Committees. The Committees and their responsibilities are detailed below under Board Committees.

The Board has delegated to management responsibility for:

- developing the annual operating and capital expenditure budgets for Board approval, and monitoring performance against these budgets;
- developing and implementing strategies within the framework approved by the Board, and providing the Board with recommendations on key strategic issues;
- appointing management below the level of General Manager and preparing and maintaining succession plans for these senior roles;
- developing and maintaining effective risk management policies and procedures;
- keeping the Board and the market fully informed of material developments.

#### b) Membership, expertise, size and composition of the Board

The Corporate Governance Principles affirm that the majority of the Board should be independent. As is typical of small financial markets generally there are, in Papua New Guinea, very considerable demands on the relatively small numbers of

people with the skills and experience to fill the demanding role of Non-Executive Director on the Boards of the Nation's larger corporate institutions. In these circumstances it is inevitable that a number of the Non-Executive Directors of BSP will also have roles on the Boards, or in Senior Management, of institutions that may be significant shareholders in, or substantial customers of, the Bank. Directors of BSP are meticulous in handling situations where there could potentially be conflicts of interest, by declaring their interests in advance, and absenting themselves from any consideration of matters where a conflict might arise. The Bank's Corporate Governance Principles require Directors to disclose any new Directorships and equity interests at each Board meeting.

The maximum number of Directors, as prescribed by the Constitution approved by shareholders, is 10. At the date of this Report there are 10 Directors, with 9 Non Executives designated as independent, plus the Chief Executive Officer. Under the Constitution, at each annual general meeting one-third of the company's Directors, in addition to any Director appointed during the year, excluding the Chief Executive Officer, must offer themselves for re-election by the shareholders. Normally, Non-Executive Directors are expected to serve a maximum of four three-year terms, dating from the AGM at which the newly elected Director is first confirmed by shareholders. This provision has effect from the date the Bank took its present form, following the merger of BSP with the Papua New Guinea Banking Corporation in April 2002. The Board will apply this provision with a degree of flexibility should it be necessary to ensure appropriate continuity, bearing in mind the particular circumstances of the Papua New Guinea market.<sup>1</sup>

The Board has a broad range of skills, experience and expertise that enables it to meet its objectives. Details of the Directors' business backgrounds and experience are provided on pages 10 and 11.

The Board accepts that it has a responsibility to shareholders to ensure that it maintains an appropriate mix of skills and experience (without gender bias) within its membership, and consequently gives careful consideration to setting criteria for new appointments it may recommend to shareholders in accordance with the Company's Constitution. It has delegated the initial screening process involved to its Remuneration and Nomination Committee which, in accordance with its Charter, may seek independent advice on possible new candidates for Directorships. All Directors must be satisfied that the best candidate has been selected.

Nominees of the Board and/or shareholders must meet the "fit and proper person" criteria established by the Bank of Papua New Guinea before they can take their place on the Board. The Board does not accept that any office bearer and/or employee of an institutional shareholder, by virtue only of his/her position within that organisation, have an automatic right to be appointed to the Board.

<sup>1</sup>For example, to avoid a situation where a number of Directors would otherwise be approaching retirement date at around the same time, or to recognise circumstances when suitably qualified candidates may not be immediately available.

On joining the Board, new Directors will be provided with a comprehensive orientation program.

### c) Role and selection of the Chairman

The Chairman is elected by the Directors and his role includes:

- ensuring all new Board members are fully aware of their duties and responsibilities;
- providing effective leadership on the company's strategy;
- presenting the views of the Board to the public
- ensuring the Board meets regularly throughout the year, and that Minutes are taken and recorded accurately;
- setting the agenda of meetings and maintaining proper conduct during meetings;
- reviewing the performance of non-executive Directors.

The Chairman is not permitted to occupy the role of Chief Executive Officer.

Noreo Beangke, who sits on the Board as an independent Non-Executive Director, is the current Chairman. He has been Chairman of Bank South Pacific since the Bank took its present form following the merger with the Papua New Guinea Banking Corporation.

### d) Director independence and Conflict of Interest

Directors are determined to be independent if they are judged to be free from any material or other business relationship with the Bank that would compromise their independence. Prior to appointment Directors designate are required to provide information to the Board for it to assess their independence.

In assessing the independence of Directors the Board will consider a number of criteria including:

- the Director is not an executive of the Bank;
- the Director is not a substantial shareholder of the Bank or otherwise associated directly with a substantial shareholder of the Bank;
- the Director has not within the last 3 years been a material consultant or a principal of a material professional adviser to the Bank or a group member, or an employee materially associated with the service provided;
- the Director is not a material supplier to or customer of the Bank or other group member, or a material consultant to the Bank or other group member, or an employee materially associated with the material supplier or customer;
- the Director has no material contractual relationship with the Bank or other group member other than as a Director of the Bank;

- the Director is free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the Director's ability to act in the best interests of the Bank.

This information is assessed by the Board to determine whether on balance the relationship could, or could reasonably be perceived to, materially interfere with the exercise of the Director's responsibilities. Materiality is assessed on a case-by-case basis.

As noted earlier, the Board is cognisant of the need to avoid conflicts of interest and it has in place policies and procedures for the reporting of any matter, which may give rise to a conflict between the interests of a Director and those of the Company. These arrangements are designed to ensure that the independence and integrity of the Board are maintained.

The Bank of Papua New Guinea sets prudential limits on loans to "associated persons": Bank South Pacific fully conforms with these requirements.

Financial Note 27, Related party transactions, on pages 79 - 81, provides details of Directors' interests.

#### e) Meetings of the Board and attendance

Scheduled meetings of the Board are held at least every two months, and the Board meets on other occasions as necessary to deal with matters requiring attention. Meetings of Board Committees are scheduled regularly during the year. The Board has a policy of rotating its meetings between locations where the Company has a significant presence. On these occasions the Board also visits Company operations and meets with local management and key customers.

The Chairman, in consultation with the Chief Executive Officer, determines meeting agendas. Meetings provide regular opportunities for the Board to assess BSP management of financial, strategic and major risk areas. To help ensure that all Directors are able to contribute meaningfully, papers are provided to Board members one week in advance of the meeting. Broad ranging discussion on all agenda items is encouraged, with healthy debate seen as vital to the decision making process.

Financial Note 28, Directors' and Executive remuneration, on pages 81 - 83, provides attendance details of Directors at Board meetings during 2009.

#### f) Review of Board Performance

The Remuneration and Nomination Committee reviews the processes by which the Board regularly assesses its own performance in meeting its responsibilities. It is intended to extend the assessment of the Board as a whole to include an assessment of the contribution of each individual Director. The Board is cognisant of the need to continually identify areas for improvement; to ensure that it meets the highest standards of corporate governance; and for the Board and each Director to make an appropriate contribution to the Company's objective of providing value to all its stakeholders. The performance review is conducted annually, and may involve assistance from external consultants.

#### g) Board Access to Information and Advice

All Directors have unrestricted access to company records and information and receive regular detailed financial and operational reports to enable them to carry out their duties. The General Managers make regular presentations to the Board on their areas of responsibility. The Chairman and the other Non-Executive Directors have the opportunity to meet with the Chief Executive Officer and the General Managers for further consultation, and to discuss issues associated with the fulfilment of their roles as Directors.

The Board recognises that in certain circumstances individual Directors may need to seek independent professional advice, at the expense of the Company, on matters arising in the course of their duties. Any advice so received is made available to other Directors. Any Director seeking such advice is required to give prior notice to the Chairman of his or her intention to seek independent professional advice.

## 2 BOARD COMMITTEES

#### a) Board Committees and Membership

The Board has established two Committees whose functions and powers are governed by their respective Charters. These committees are the Audit Risk and Compliance Committee, and the Remuneration and Nomination Committee.

Membership of the Committees and a record of attendance at committee meetings during the year is detailed in table below. Remuneration details are provided in Financial Note 28 on page 81.

#### Membership of Board Committees as at 31 December 2009

Board Audit Risk and Compliance Committee		Remuneration and Nomination Committee	
John Jeffery - Chairman	5/5	Tom Fox - Chairman	2/2
Vai Reva (Resigned)	2/2	Noreo Beangke	1/2
Gerea Aopi	1/5	Ila Temu	2/2
Tom Fox (Appointed)	3/3		

#### b) Committee Charters

The Committee Charters are available in the shareholders information section of the BSP website [www.bsp.com.pg](http://www.bsp.com.pg)

#### c) Committee Structure

Committee members are chosen for the skills, experience and other qualities they bring to the Committee. At the next Board meeting following each Committee meeting, the Board is given a report by the Chairman of the respective Committee and Minutes of the meeting are tabled.



The Audit Risk and Compliance Committee is comprised of three Non-Executive Directors, a majority of whom should be independent, and who are duly appointed by the Board. The Chairman of the Audit Risk and Compliance Committee must be one of the independent Directors, other than the Chairman of the Board. Each member should be capable of making a valuable contribution to the Committee and membership is reviewed annually by the BSP Board.

The Remuneration and Nomination Committee comprises three Non-Executive Directors, the majority of whom should be independent, and who are duly appointed by the Board. The Chairman of the Remuneration and Nomination Committee must be one of the independent Directors, other than the Chairman of the Board. Each member should be capable of making a valuable contribution to the Committee, and membership is reviewed annually by the BSP Board.

A review of the performance of Committee members will form part of the Board's performance review.

### **d) Board Audit Risk and Compliance Committee**

The Audit Risk and Compliance Committee is delegated by the Board with responsibility for reviewing and monitoring the:

- integrity of the financial statements and the financial reporting and audit process;
- external auditor's qualifications, performance and independence;
- performance of the internal audit function of the Bank;
- systems of internal control and management of all risks;
- systems for ensuring operational efficiency and cost control;
- systems for approval and monitoring of expenditure including capital expenditure;
- processes for monitoring compliance with laws and regulations (both in Papua New Guinea and overseas);
- implementation of Board decisions by management and making recommendations to the Board for the appointment of the external auditor;
- annual internal audit plan and its ongoing review.

In the course of fulfilling its mandate, the Committee meets with both the internal and external auditors without management present.

#### **i. Annual Financial Statements**

The Audit Risk and Compliance Committee reviews the annual financial statements to determine whether they are complete and consistent with the information known to Committee members and to assess whether the financial statements reflect appropriate accounting principles. In particular it:

- pays attention to complex and/or unusual transactions;
- focuses on judgmental areas, for example those involving valuation of assets and liabilities; provisions; litigation reserves; and other commitments and contingencies;

- meets with management and the external auditors to review the financial statements and the results of the audit;
- reviews the other sections of the Annual Report before its release and considers whether the information is understandable and consistent with members' knowledge about the Bank and its operations;
- satisfies itself as to the accuracy of the financial accounts, reconciles them with management accounts presented to the Committee, and signs off on the financial accounts of the Bank before they are submitted to the Board.

#### **ii. External Audit**

The Audit Risk and Compliance Committee is responsible for making recommendations to the Board on appointment and terms of engagement of BSP external auditors. The selection is made from appropriately qualified companies in accordance with Board policy. The Board submits the name of the recommended appointee to shareholders for ratification. In line with the policy of the Bank of Papua New Guinea, the signing partner in the external audit firm must be rotated at least every three years.

The Committee reviews annually the performance of the external auditors and makes recommendations to the Board regarding the continuation or otherwise of their appointment, consistent with the Bank of Papua New Guinea's Prudential Standard No. 7/2005 – External Auditors, while ensuring their independence is in line with Board policy (see below).

There is a review of the external auditor's proposed audit scope and approach, to ensure there are no unjustified restrictions. Meetings are held separately with the external auditors to discuss any matters that the Committee or the external auditors believe should be discussed privately. The external auditor attends meetings of the Audit Risk and Compliance Committee at which the external audit and half yearly review are agenda items.

The Committee ensures that significant findings and recommendations made by the external auditors are received and discussed promptly, and that management responds to recommendations by the external auditors in a timely manner.

The duly appointed external audit firm may not be engaged by the company to provide specialist consultancy services relating to financial, strategic and or taxation matters.

The external auditor is invited to the Annual General Meeting of shareholders and is available to answer relevant questions from shareholders.

The Bank of Papua New Guinea Prudential Standards provide for a tri-partite meeting between BPNG, the external auditors, and the Bank, if required.

#### **iii. Internal Audit**

The Audit Risk and Compliance Committee approves, on the recommendation of management, the appointment of Manager Audit and Risk. The Committee meets regularly with Manager Audit and Risk.

Reviews are undertaken of the scope of the work of the internal

audit function to ensure no unjustified restrictions or limitations have been placed upon Audit and Risk Department. The Audit Risk and Compliance Committee also reviews the qualifications of internal audit personnel and endorses the appointment, replacement, reassignment or dismissal of the internal auditors.

An independent review by an expert consultant is made annually as to the effectiveness of the internal audit and risk function. These reports are presented to the Board Audit Risk and Compliance Committee, and the Board.

The Audit Risk and Compliance Committee meets separately with the internal auditors to discuss any matters that the Committee, or the internal auditors, believe should be discussed privately. The Internal Auditor has direct access to the Audit Risk and Compliance Committee and to the full Board. The Committee ensures that significant findings and recommendations made by the internal auditors are received and discussed promptly, and that management responds to recommendations by the internal auditors on a timely basis.

Internal Audit meets with the external auditors half yearly, to review the scope and findings of internal audit's annual audit plan, and the extent of the external audit plan, having regard to internal audit's findings.

#### iv. Compliance

The Audit Risk and Compliance Committee reviews the effectiveness of the systems for monitoring compliance with all legal and regulatory obligations and the Constitution of the Bank. It also reviews the results of management's investigation and follow-up (including disciplinary action) of any fraudulent acts, or non-compliance.

The Committee obtains regular updates from management and the Bank's legal officers regarding compliance matters, and satisfies itself that all regulatory compliance matters have been considered in the preparation of the financial statements.

Reviews of the findings of any examinations by regulatory agencies are undertaken and the Chairman of the Board Audit Risk and Compliance Committee has the right to approach a regulator directly in the event of a prudential issue arising.

#### v. Risk Management

The Committee's role in the Bank's risk management processes are detailed in 3(b) below.

#### e) Board Remuneration and Nomination Committee

The Remuneration and Nomination Committee has been established to assist the Board in fulfilling its oversight responsibilities in respect of Board and Senior Executive Management selection, appointment, review and remuneration.

The responsibilities of the Remuneration and Nomination Committee are:

- oversee the selection and appointment of a Chief Executive Officer and recommend an appropriate remuneration and benefits package to the full Board;

- determine and review appropriate remuneration and benefits of Directors for recommendation to the full Board, and subsequently to the shareholders;
- identify and maintain a clear succession plan for the Executive Management Team, ensuring an appropriate mix of skills and experience as well as appropriate remuneration and benefits packages are in place and reviewed regularly;
- ensure that the Board itself maintains an appropriate mix of skills and experience necessary to fulfil its responsibilities to shareholders while maintaining a world class Corporate Governance regime;
- receive and endorse positions/titles recommended by the Managing Director from time to time as applying to designated Senior Executive Management positions;
- review the procedures in place to ensure that all new Senior Executive appointees are adequately qualified and experienced, and that proper recruitment procedures are followed;
- review and make recommendations to the Board on the appointment and terms and conditions of employment to all Senior Executive Management positions;
- review and approve all termination arrangements for such Senior Executives;
- review transactions between the Company and any of the Directors or relevant Senior Executives;
- review and make recommendations to the Board on employee remuneration and benefits policies and practices generally;
- engage external consultants as and when deemed appropriate to benchmark remuneration packages for Executives and Senior Management;
- review Board performance, tenure, and succession planning.

The Board has in place a review process, led by the Chairman, that involves a peer review of performance based on a broad range of criteria.

### 3 RISK MANAGEMENT

#### a) Approach to Risk Management

The Bank's Risk Management activities are aligned to the achievement of the Bank's Objectives, Goals and Strategic Focus Plans. The Board, in consultation with the Executive Committee, determines the Bank's risk appetite and risk tolerance. These benchmarks are used in the risk identification, analysis and risk evaluation processes.

BSP distinguishes the following major risks:

**Credit Risk** - The potential for financial loss where a customer or counterparty fails to meet their financial obligation to the Bank.

**Market Risk** - The potential financial loss arising from the Bank's activities in financial, including foreign exchange, markets. More detailed commentary on financial risk management is provided in

the Notes to the financial accounts.

**Liquidity Risk** – The risk of failure to adequately meet cash demand in the short term without incurring financial losses.

**Interest Risk** - Risk to earnings from movement in interest rates.

**Operational Risk** - The risk of loss resulting from inadequate or failed internal processes, people, or from external events, including legal and compliance risk.

The Bank's Asset & Liability Committee monitors market risk, interest risk, and liquidity risk, and the Credit Committee monitors credit risk. Operational risk is managed at Business Unit level and a risk register system has been implemented across the Bank. The Executive Committee and the Board overview the highest tier of risks within these risk registers.

The Bank's risk management policy ensures that the Bank has in place acceptable limits for the risks identified by the Bank's employees. The risk management approach encompasses the following:

- defining the types of risks that will be addressed by each functional or policy area (i.e., credit risk, interest rate risk, liquidity risk, operational risk, etc.);
- ensuring that mechanisms for managing (identifying, measuring, and controlling) risk are implemented and maintained to provide for organisation wide risk management;
- developing information systems to provide early warning, or immediate alert, of events or situations that may occur, or already exist, that could create one or more types of risk for the Bank;
- creating and maintaining risk management tools, including those requested by the Board, such as policies, procedures, risk registers, controls and independent testing, personnel management and training, and planning;
- instituting and reviewing risk measurement techniques that Directors and management may use to establish the Bank's risk tolerance, risk identification approaches, risk supervision or controls, and risk monitoring processes;
- developing processes for those areas that represent potential risks;
- establishing appropriate management reporting systems regarding these risks so individual managers are provided with a sufficient level of detail to adequately manage and control the Bank's risk exposures.

### **b) Risk Management Roles and Responsibilities**

The Board accepts responsibility for ensuring it has a clear understanding of the types of risks inherent in the Bank's activities. Therefore responsibility for overall risk management in BSP is vested with the Board. However every employee from Executive Management to the newest recruit has a responsibility and a part to play in the process.

There is a formal system of financial and operational delegations

from the Board to the Managing Director, and from the Chief Executive Officer to the General Managers. These delegations reflect the Bank's risk appetite, and are cascaded down to managers who have skills and experience to exercise them judiciously.

The Board defines the accountabilities (including delegated approval/control authorities/ limits) and reporting/ monitoring requirements for the risk management process. The severity of risks identified in the risk identification, analysis and evaluation processes, and noted in the Strategic Business Unit Risk Registers, is used to determine the approval/ control authorities/ limits. The Board will review these risk limits annually along with an annual review of the Bank's significant risks.

The Board has adopted guidelines, with the help of management analysis, covering the maximum loss exposure the Bank is able and willing to assume. These guidelines are detailed in the Bank's Risk Policy and Procedures Manual which has been externally reviewed and approved by the Board.

The Board has also delegated to the Audit Risk and Compliance Committee responsibility for overview of loss control and for overseeing the risk management function.

The Board Audit Risk and Compliance Committee is responsible for providing regular reports and recommendations to the Board on the risk management activities of the Bank, especially relating to risk issues that are outside of the authority of the Bank's Executive Committee to approve.

The Bank's Executive Committee is responsible for deliberating on risk management issues which are outside of the delegated authorities/ limits of the Credit Committee, Asset and Liability Committee (ALCO) and General Managers, with escalation of these issues to the Audit Risk and Compliance Committee, and the Board itself, in case of need.

### **c) Management Assurance**

The Board is provided with regular reports about BSP financial condition and its operating performance. Annually the Chief Executive Officer and the Chief Financial Officer certify to the Board that:

- the financial records of the Bank have been properly maintained and that they accurately record the true financial position of the Company;
- the financial statements and notes meet all appropriate accounting standards;
- there are sound systems of risk management and control that are operating effectively.

Additionally all General Managers provide bi-annual statements attesting that:

- they have assessed and documented the risks and internal control procedures in their Strategic Business Unit;
- they have identified any changes in business, operations and computer systems and the risks that may arise from those changes;

- the risk management and internal compliance and control systems are appropriate and operating efficiently and effectively;
- any weaknesses in the risk management and internal compliance and control systems have been identified and remedial action taken.

#### 4 ETHICAL BEHAVIOUR

BSP acknowledges the need for Directors and employees at all levels to observe the highest standards of ethical behaviour when undertaking Company business. To this end, the Board has adopted

- a Code of Conduct for both Directors and members of the Executive Management team of the Company and stipulated that each Director, and relevant employees, acknowledge in writing having read, understood and agreed to abide by the Code; and
- a Corporate Mission, Objectives, and Core Values Statement which establishes principles to guide all employees in the day to day performance of their individual functions within the Company.

To ensure the maintenance of high standards of corporate behaviour on an ongoing basis, the Board further stipulates that senior management periodically undertake an appropriate communication program to reinforce both the Code and Core Values Statements. All Directors are encouraged to maintain membership of an appropriate Directors Association to keep abreast of current trends in Director's duties, responsibilities and corporate governance issues.

BSP is committed to a culture in which it is safe and acceptable for employees, customers and suppliers to raise concerns about poor or unacceptable practices, irregularities, corruption, fraud and misconduct.

The Bank has adopted a whistle blowing policy that is designed to support and encourage staff to report in good faith matters such as:

- unacceptable practices;
- irregularities or conduct which is an offence or a breach of laws of Papua New Guinea (actions and decisions against the laws of Papua New Guinea including non-compliance);
- corruption;
- fraud;
- misrepresentation of facts;
- decisions made and actions taken outside established BSP policies & procedures;
- sexual harassment;
- abuse of Delegated Authorities;
- misuse of company assets;
- disclosures related to miscarriages of justice;

- health and safety risks, including risks to the public as well as other employees;
- damage to the environment;
- other unethical conduct;
- failure to comply with appropriate professional standards;
- abuse of power, or use of the Bank's powers and authority for any unauthorised purpose or personal gain;
- breach of statutory codes of practice.

Directors and Management of the Company are subject to Securities Act 1997 restrictions for buying, selling or subscribing for securities in the Company if they are in possession of inside information, i.e. information which is not generally available and, if it were generally available, a reasonable person would expect to have a material effect on the price or value of the securities of the Company.

Further Directors and management may only trade in the securities of the Company, subject to the foregoing insider trading restrictions, during each of the eight weeks following the announcements of half yearly profit and yearly profit or the date of issue of a prospectus. Management should discuss proposed share trades with the Chief Executive Officer in advance, who in turn will keep the Chairman of the Board apprised of management activities. Directors should discuss proposed share trades with the Chairman in advance.

In addition Directors and management must not trade in any other entity if inside information on such entity comes to the attention of the Director or management by virtue of holding office as an Officer of the Bank.

#### 5 MARKET DISCLOSURE

The Bank's continuous disclosure regime is fundamental to the rights of shareholders to receive information concerning their securities. The most important aspect of the Bank's shareholder communication policy is to comply with the continuous disclosure regime and to implement best practice disclosure policy.

Market announcements are posted to BSP website immediately after release to the market. All market announcements made by the Bank since its listing in August 2003 are currently available on the website.

Where BSP provides financial results briefings to analysts or media, these briefings are published on the website as soon as possible after the event. In any event no material information which has not been previously released to the market is covered in such briefings. The material upon which the briefing is based (such as slides or presentations) is released to the market prior to the briefing.

The Bank's insider trading rules are important adjuncts to the continuous disclosure regime in ensuring that shareholders are given fair access to material information regarding securities. BSP seeks to limit the opportunity for insider trading in its own securities through its continuous disclosure policies and the dealing rules applying to its employees and Directors.

### 6 SHAREHOLDER COMMUNICATIONS

BSP Code of Conduct requires its employees to act with high standards of honesty, integrity, fairness and equity in all aspects of their employment with the Bank.

With this in mind, BSP commits to dealing fairly, transparently and openly with both current and prospective shareholders using available channels and technologies to communicate widely and promptly. The Bank commits to facilitating participation in shareholder meetings, and dealing promptly with shareholder enquiries.

Our shareholder communication policy is built around compliance with disclosure obligations and aspiring to be at the forefront of best practice in disclosure. Our framework for communicating with shareholders is to concisely and accurately communicate:

- our strategy;
- how we implement that strategy; and
- the financial results consequent upon our strategy and its implementation.

The Bank uses shareholder forums such as the Annual General Meeting, and group meetings with larger shareholders, within disclosure policies, to communicate financial performance and strategies.

### 7 REMUNERATION

BSP remuneration policy for senior management is comprised of a fixed component and an at risk component that is directly related to long term incentives. The remuneration packages of General Managers and the Chief Executive Officer are approved

by the Remuneration and Nomination Committee, and details are provided by the Committee to the Board.

Fixed remuneration of senior management is reviewed at the time of contract renewal taking into account the nature of the role, the pay position relative to comparable market pay levels, and individual and business performance.

The “at risk” component of the remuneration package is a performance based Executive Management Share Option Plan (EMSOP). This plan is structured to provide senior management with the incentive to deliver sustained growth in value for shareholders. Performance hurdles are incorporated in the EMSOP and senior staff are selected to participate based on their annual performance, potential, and the business need to retain critical skills.

Further information about the EMSOP is provided in Note 23 to the Annual Accounts on pages 75-77. Under PNG tax law individuals who participate in the EMSOP are responsible for any related taxation liabilities.

Non-executive Directors are remunerated on a fixed basis within an aggregate Directors’ fee pool approved periodically by shareholders. An external review of non-executive Directors’ remuneration was undertaken by First Commercial Limited in 2006. The shareholders last approved a pool of K1.00 million in May 2006. During 2009 K0.75 million of the pool was utilised (2008: K0.73 million).

A table of fees paid to Directors during 2009 is produced on page 81. Non-executive Directors are not paid any retirement or superannuation benefits, nor do they participate in any share option programs.



**Deputy General Managers** L-R: Robert DeBrouwere, Paul Russell, Daryl Balchin, Lew Kenah and Robert Mantel

<b>Profit and Loss (K'000)</b>	<b>2004</b>	<b>2005<sup>2</sup></b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
Net interest income	159,602	161,804	209,581	276,872	377,100	<b>473,969</b>
Non interest income	110,919	144,174	134,531	202,510	243,828	<b>251,743</b>
Bad and doubtful debt (expense)/recovery	(601)	3,968	1,311	4,345	(11,353)	<b>(15,020)</b>
Other operating expenses	(166,283)	(167,265)	(178,573)	(188,871)	(229,599)	<b>(335,146)</b>
Operating Profit	103,637	142,230	166,850	294,856	379,976	<b>375,546</b>
Impairment of non-current asset	-	-	(1,775) <sup>3</sup>	(10,373) <sup>4</sup>	(50,000)	<b>2,372</b>
Profit before tax	103,637	142,230	164,518	283,571	328,798	<b>378,143</b>
Income tax (expense)	(16,986)	(43,006)	(52,902)	(92,499)	(100,464)	<b>(121,025)</b>
Profit/(loss) after tax	86,651	99,224	111,616	191,072	228,334	<b>257,118</b>
<b>Dividends (toea)</b>						
Dividends paid per share <sup>5</sup>	0.47	1.0	1.4	1.6	2.2	<b>2.2</b>
<b>Balance Sheet (K'000)</b>						
Net loans and advances	680,174	873,538	1,163,252	1,550,271	2,343,844	<b>3,638,562</b>
Total assets	2,196,639	2,952,458	4,333,666	5,819,549	6,807,868	<b>9,397,821</b>
Deposits	1,836,729	2,542,935	3,773,805	5,055,917	5,782,020	<b>7,493,779</b>
Capital	255,632	308,300	396,295	571,700	744,254	<b>934,097</b>
<b>Performance Ratios</b>						
Return on Assets	4.2%	3.4%	3.1%	3.8%	3.6%	<b>3.2%</b>
Return on Equity	39.7%	32.2%	31.7%	39.5%	34.7%	<b>30.6%</b>
Expense/Income	61.5%	54.6%	51.9%	39.4%	45.0%	<b>46.0%</b>
<b>Key prudential ratios</b>						
Capital adequacy	31.9%	29.4%	25.9%	29.0%	22.8%	<b>22.1%</b>
Liquid Asset Ratio	56.0%	56.2%	51.4%	50.3%	47.5%	<b>50.1%</b>
Leverage ratio	10.7%	9.6%	7.5%	9.2%	10.4%	<b>9.1%</b>
<b>Exchange rates (One (1) PNG Kina buys):</b>						
US Dollar	0.3101	0.3230	0.3300	0.3525	0.3735	<b>0.3700</b>
AUS Dollar	0.4222	0.4400	0.4171	0.3999	0.5396	<b>0.4127</b>

(Source – Bank of Papua New Guinea Quarterly Economic Bulletin)

<sup>2</sup> From 2005 onwards, statistics are consolidated for Bank of South Pacific and its subsidiaries

<sup>3</sup> Impairment of goodwill on acquisition of net assets of Habib Bank Ltd, Fiji Operation, Dec 2006

<sup>4</sup> Impairment of remaining goodwill in respect of acquisitions of Capital Stockbrokers Ltd (2005), Habib Bank Ltd - Fiji Branch (2006) and National Bank of Solomon Islands (2007)

<sup>5</sup> Dividends were declared, are paid in July of each year; Dividend per share has been adjusted for 1/10 share split 2008.

# REBRANDING

## BSP REBRAND LAUNCHING



OVERSEAS BRANCHES AND SUBSIDIARIES

Summary Financial Information

All amounts are expressed in K'000

	Total assets	Total Liabilities	Turnover	Net Profit After Tax
Solomon Islands	249,095	230,560	14,654	10,082
Fiji branches	164,897	138,948	3,299	(3,338)
Niue	3,912	4,349	291	(369)
Colonial Fiji Entity *	1,472,800	1,298,578	3,600	2,222
BSP Capital	16,901	11,693	264	(2,842)

\* Results from December 2009

RETAIL BANK – OVERSEAS BRANCHES

2009 Highlights

Our two BSP branches in Fiji showed a continuing growth in 2009 in spite of the subdued economic conditions in this country. In 2009 BSP started the process to acquire Colonial National Bank. The purchase was completed in December 2009 and this will give BSP access to more products and services that could be used in PNG. The acquisition adds 20 branches to BSP's Pacific network.

In the Solomon Islands, the profits achieved were again above budget.

The performance in 2009 of the BSP branch in Niue was positive although the pressure on the result is increasing because of the outflow of deposits to New Zealand where banks can offer higher interest rates.

2010 Challenges

We will continue to explore the opportunities to further expand our operations in the Pacific.

BSP CAPITAL LIMITED

BSP Capital has had a year of transformation. It has divided its operating divisions to better reflect how its business is derived. The respective divisions are Equities, Corporate, Funds Management,

Compliance and Risk Management and lastly Information Technology. One of the major tasks undertaken during the year was a review of the business units by KPMG, where a number of recommendations were made for changes. As investors are aware, technology is an integral part of any stockbroking business and many of the recommendations were made in that area. We will implement new processes in the Equities division that will assist greatly in eradicating errors and better inform management of the daily trades and attendant issues pertinent to the area. The system will compliment what happens between the Front Office (where orders are placed) and the Back Office (where orders are booked). Our manual systems are antiquated and the flow of information is hindered by the processes. We expect that the new computerized system will be in place for the second half of the year.

The Equities and Corporate Division was successful in raising K75, 525,000 for BSP through an Unsecured Subordinated Notes issue in 2009. The Notes were listed on POMSoX and have proven popular with investors, especially those looking for long term, high yield investments. The Global Economic Crisis had only a marginal effect upon the share market in PNG. Takeover activity was brisk and real GDP growth continued at around 6.2%. The major projects throughout the country and the building construction sector were responsible for the majority of the growth experienced in 2009.

BSP Capital has had a Funds Management business for some years. New senior management have stepped in, and a number of additional staff has been employed with extensive Funds Management experience to compliment the department. A state of the art Funds Management IT system will be in place by July 2010, and combined with a major internal structure, we will be a formidable force to contend with in 2010 and onwards. We are cognizant of the fact that large revenues will soon be handed to Landowner Groups from various projects in PNG. It is our aim to assist in the timely investment of those funds so that wealth can be generated across a larger part of the country than previously. We look to the Funds Management division to be the largest contributor to revenues in BSP Capital.

It has been another year of challenges which has also involved many internal structural changes at BSP Capital. We believe that the new Dealing System will change the face of the way stockbroking has been done in PNG. The major review of BSP Capital by KPMG and the subsequent recommendations made by them, have been implemented and the positive benefits are already being felt. We have made 2010 the year of consolidation where BSP Capital transforms itself in to a profitable and solid contributor to the BSP stable.



# Community



"I love being a part of BSP a bank that's 100% committed to the people of PNG."  
Ian Clyne, CEO BSP with Jason, Cheshing Home resident.



New classroom at St Francis Primary School, Koki



BSP has supported many Health Checks at Clinics across PNG.

## Did you know...

At BSP we're much more than just a bank... we are a real part of your community.

**Giving back.** In 2009, BSP's new CEO, Ian Clyne, addressed a need for the bank to be more involved in each of the communities in which it operates. As BSP is PNG owned, Ian Clyne has a strong belief that the bank has a responsibility to help each of those communities. Not only financially by funding local projects, but in a real community spirited way by fully involving the local branch team, encouraging them to join in and help make those projects a reality.

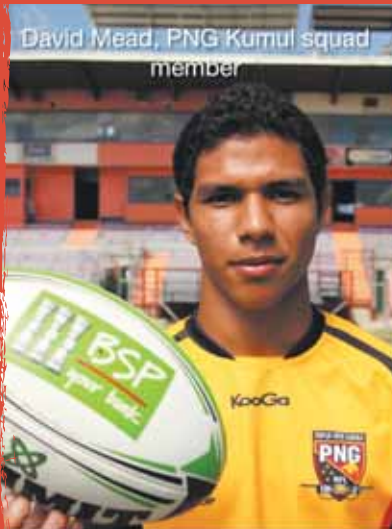
Our Branch Managers went out and talked to the people. They listened and learnt what was important to their community.

Our staff became increasingly more aware of the needs of the local people. In a way not seen before, our Branch Managers and staff reached out with much more personal commitment, devoting their own time on weekends in an effort to ensure their local communities benefited in the best way possible.

Projects like refurbishing local hospital wards and health clinics, renovating, rebuilding and repainting classrooms in local schools, bringing the opportunity for health checks to the people, providing new medical equipment and supplies to various hospitals around the country. Supplying and installing with professional guidance, water tanks to schools where children previously did not have access to clean water supplies.

These projects are on-going and are being driven by the enthusiasm of our BSP teams at every branch nationwide, fully supported financially by BSP with funding of K700,000 already provided, and led by an untiring effort to make a real difference... and to be very much a part of your community.

# Sports



BSP is committed to children throughout PNG to have the opportunity to play more sport and to encourage a healthier lifestyle. The Malasang Primary School participated in the BSP Tennis Programme, as did thousands and thousands of children nationwide.

## At BSP we're bringing healthy sporting activities to our children across the nation

In May 2009, BSP, as a strong supporter of sports throughout PNG, undertook a new direction to bring the healthy, active sport of tennis to school children and their teachers in a large number of schools around the nation.

With BSP's funding of K150,000 to the PNG Tennis Association, and encouraging local area support and involvement from our Branches throughout the country, the BSP Regional Community Tennis Programme became a reality. The programme was launched in Daru. Too often, sponsorships take place only in the main centres, but at BSP we were determined to make this a sponsorship with a difference.

The programme has rolled out around the country with tennis training and activities so far taking place in Kiunga, Wewak, Maprik, Aitape, Vanimo, Tabubil, Madang and Buka. The second phase of the programme was recently launched in Kimbe and will see it travel through schools in both West and East New Britain, Oro, New Ireland and Manus provinces before year end. The

programme is scheduled to continue in 2010 starting off in the Highlands region.

In 2009 over 17,000 school children and their teachers have participated in a most enthusiastic way in the BSP Tennis Programme.

We have found that wherever the programme has reached, it has made an incredible difference to both the school children and their teachers. Much of the success is due to the dedication of the two highly talented PNG Tennis Association Development Officers, Michael Foo and Lavu Ivuyo, who travel and provide coaching at the various schools, ably assisted by our BSP Branch Managers and staff in each location.

BSP is proud to support the development of rugby league footballers from grassroots to the elite level. In fact, BSP supports a wide range of sports and activities with a focus on children's health and wellbeing.

BSP... Your Sport. Your Bank

## Your bank's community principles

### BSP Beliefs

BSP believes in people and communities and in supporting your ideas and dreams. This drives us to help you, our customer, and your community to fulfil your goals. It leads us to seek and understand your needs and to build a real connection to grow healthy and sustainable communities.

### BSP

At BSP we seek to be a partner in all the communities across PNG, with a real sense of purpose to focus on activities that improve social and economic wellbeing for the present and for the future. We understand that we are successful if we can make a contribution that:

- delivers real value for a community
- gives opportunities to everyone in a community, because we believe everyone deserve a chance
- involves all of our resources, not just financial
- involves our people
- gives us the opportunity to talk to our customers about what's important to them and their community
- may be local to a province or region, but national in their significance

## DIRECTORS' REPORT for the Year Ended 31 December 2009

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The Directors take pleasure in presenting the Financial Statements of the Company and the Group for the year ended 31 December 2009. 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) and the Group is the provision of commercial banking and finance services throughout Papua New Guinea and the Pacific region. BSP is a company 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 the Solomon Islands, Fiji Islands and Niue. The registered office is at Douglas Street, Port Moresby.

**Review of operation**

For the year ended 31 December 2009, the Company's profit after tax was K257.738 million (2008: K226.779 million profit). The Group's profit after tax was K257.118 million (2008: K228.334 million).

**Dividends**

No dividends have been declared by the Company in respect of the year ended 31 December 2009 (2008: K100.305 million dividend was paid on 16<sup>th</sup> July 2009 in respect of the year ended 31 December 2008).

**Directors and officers**

The following were Directors of the Bank of South Pacific Limited during the year ended 31 December 2009:

Mr N N Beangke	Mr J G Jeffery	Mr K Constantinou (Appointed)
Mr T E Fox	Mr Ian B Clyne	
Mr G Aopi	Mr V Reva (Resigned)	
Sir N Bogan	Mr C C Procter	
Dr I Temu	Mr J K Natto	

Details of Directors' tenure and Directors and executives' remuneration during the year are provided in Note 28 of the Notes to the Financial Statements.

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 85. Details of amounts paid to the auditors for audit and other services are shown in Note 5 of the Notes to the Financial Statements.

**Donations**

Donations made by the Company during the year amounted to K282,976 (2008: K165,583).

**Interests Register**

Transactions recorded in the Interests Register are disclosed in Note 27 of the Notes to the Financial Statements.

For, and on behalf of, the Directors.

Dated and signed in accordance with a resolution of the Directors in Port Moresby this 5th day of March 2010.



**N.N. Beangke**  
Chairman



**Kostas Constantinou**  
Director

## STATEMENT BY THE DIRECTORS

### STATEMENT BY THE DIRECTORS for the Year Ended 31 December 2009

The Directors declare that:

- a) in the Directors' opinion, there are reasonable grounds to believe that the Company & 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 giving a true and fair view of the financial position and performance of the consolidated entity.

#### Additional Statutory Information

The results of the Company 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 Company and the Group misleading or inappropriate.

No contingent liability has arisen since the end of the financial year, which continues to exist at the date of this report, other than those disclosed in the financial statements.

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 Company 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 5th day of March 2010.



**N.N. Beangke**  
Chairman



**Kostas Constantinou**  
Director

YOUR COMMUNITY, YOUR BANK



## STATEMENT OF COMPREHENSIVE INCOME

### STATEMENT OF COMPREHENSIVE INCOME for the Year Ended 31 December 2009

	Note	Group		Bank	
		2009	2008	2009	2008
<i>All amounts are expressed in K'000</i>					
Interest income	1	582,862	435,974	576,954	435,656
Interest expense	1	(108,893)	(58,874)	(106,746)	(58,874)
<b>Net interest income</b>		<b>473,969</b>	377,100	470,208	376,782
Fee and commission income	2	108,809	87,309	106,030	82,914
Other income	3	142,934	156,519	125,623	153,713
<b>Net Operating income</b>		<b>725,712</b>	620,928	<b>701,861</b>	613,409
Bad and doubtful debts (expense)/recovery	4	(15,020)	(11,353)	(16,376)	(11,353)
Other operating expenses	5	(335,146)	(229,599)	(308,684)	(224,054)
<b>Operating profit</b>		<b>375,546</b>	379,976	<b>376,801</b>	378,002
Property revaluation adjustment		2,372	-	2,372	-
CDO buy-back provision	8	-	(50,000)	-	(50,000)
Share of loss from Associates accounted for using the equity method	10	225	(1,178)	(1,209)	(1,178)
<b>Profit before tax</b>		<b>378,143</b>	328,798	377,964	326,824
Income tax expense	6(a)	(121,025)	(100,464)	(120,226)	(100,045)
<b>Operating profit/(loss) after tax from ordinary activities</b>		<b>257,118</b>	<b>228,334</b>	<b>257,738</b>	<b>226,779</b>
<b>Other comprehensive income</b>					
Exchange difference on translation of foreign operations/subsidiaries	24	(7,076)	(3,361)	(6,862)	(298)
Net value gain on revaluation of share options	24	( 249)	944	(249)	944
Net movement in asset revaluation	24	37,623	(1,019)	37,628	(1,019)
<b>Other comprehensive income for the year, net of tax</b>		<b>30,298</b>	<b>(3,436)</b>	<b>30,517</b>	<b>(373)</b>
<b>Total comprehensive income for the year</b>		<b>287,416</b>	<b>224,898</b>	<b>288,255</b>	<b>226,406</b>
Earnings per share - basic and diluted (toea per share)	30	5.6	5.0	5.7	4.9

The attached notes form an integral part of these financial statements

**STATEMENT OF FINANCIAL POSITION  
for the year ended 31 December 2009**
*All amounts are expressed in K'000*

	Note	Group		Bank	
		2009	2008	2009	2008
<b>ASSETS</b>					
Cash and balances with Central Bank	11	996,393	434,627	796,197	433,900
Treasury & Central Bank bills	12	2,325,713	1,833,910	2,305,708	1,833,910
Amounts due from other banks	13	191,888	283,978	186,655	283,978
Loans and advances to customers	14	3,638,562	2,343,844	2,860,022	2,343,844
Properties held for sale	15(a)	9,011	-	-	-
Property, plant and equipment	15(b)	282,246	175,443	243,302	175,048
Assets subject to operating lease	15(c)	86,024	94,568	86,024	94,568
Other financial assets	16	1,512,569	1,529,146	1,331,311	1,529,146
Investment in associates	10	47,733	1,826	1,417	1,826
Investment in subsidiaries		-	-	226,201	30,540
Intangibles	9	21,333	-	-	-
Investment properties	15(d)	70,990	-	-	-
Deferred tax asset	17	52,603	27,146	41,210	26,881
Other assets	18	162,756	83,380	88,680	63,984
<b>Total assets</b>		<b>9,397,821</b>	<b>6,807,868</b>	<b>8,166,727</b>	<b>6,817,625</b>
<b>LIABILITIES</b>					
Amounts due to other banks	19	26,594	11,416	12,202	11,416
Amounts due to customers	20	7,493,779	5,782,020	6,759,626	5,786,145
Subordinated debt securities	21(b)	75,525	-	75,525	-
Other liabilities	21(a)	670,955	105,544	202,260	107,993
Provision for income tax	6(b)	109,691	68,416	103,377	68,355
Deferred tax liabilities	17	31,881	17,094	31,881	17,081
Other provisions	22	55,299	79,124	45,778	78,238
<b>Total liabilities</b>		<b>8,463,724</b>	<b>6,063,614</b>	<b>7,230,649</b>	<b>6,069,228</b>
<b>SHAREHOLDERS' EQUITY</b>					
Ordinary shares	23	318,014	318,014	318,014	318,014
Retained earnings	24	553,912	394,367	551,625	394,461
Other reserves	24	62,171	31,873	66,439	35,922
<b>Total shareholders' equity</b>		<b>934,097</b>	<b>744,254</b>	<b>936,078</b>	<b>748,397</b>
<b>Total equity and liabilities</b>		<b>9,397,821</b>	<b>6,807,868</b>	<b>8,166,727</b>	<b>6,817,625</b>

The attached notes form an integral part of these financial statements



## STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

### STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY for the Year Ended 31 December 2009

<b>Bank</b>				<b>Retained Earnings / (Accumulated losses)</b>	
	<b>Note</b>	<b>Share capital</b>	<b>Reserves</b>		<b>Total</b>
<i>All amounts are expressed in K'000</i>					
<b>Balance at 1 January 2008</b>	23&24	271,536	36,295	264,434	572,265
Net profit		-	-	226,779	226,779
Final dividend paid for 2007		-	-	(99,509)	(99,509)
Deferred income 2008		-	-	2,757	2,757
Other comprehensive income		-	(373)	-	(373)
Net share buy back/Issue of ordinary shares	23	46,478	-	-	46,478
<b>Balance at 31 December 2008</b>	23&24	<b>318,014</b>	<b>35,922</b>	<b>394,461</b>	<b>748,397</b>
Net profit		-	-	257,738	257,738
Final dividend paid for 2008		-	-	(100,305)	(100,305)
Deferred income 2009		-	-	(269)	(269)
Other comprehensive income	24	-	30,517	-	30,517
<b>Balance at 31 December 2009</b>	23&24	<b>318,014</b>	<b>66,439</b>	<b>551,625</b>	<b>936,078</b>
<b>Group</b>					
<b>Balance at 31 December 2008</b>	23&24	318,014	31,873	394,367	744,254
Net profit		-	-	257,118	257,118
Final dividend paid for 2008		-	-	(100,305)	(100,305)
Deferred income 2009		-	-	2,732	2,732
Other comprehensive income		-	30,298	-	30,298
<b>Balance at 31 December 2009</b>	23&24	<b>318,014</b>	<b>62,171</b>	<b>553,912</b>	<b>934,097</b>

The attached notes form an integral part of these financial statements



**Ian B. Clyne** BSP SMS Banking

**STATEMENT OF CASH FLOW**  
**for the Year Ended 31 December 2009**
*All amounts are expressed in K'000*

	Note	Group		Bank	
		2009	2008	2009	2008
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>					
Interest received		584,859	428,409	579,318	428,409
Fees and other income		249,399	244,319	232,578	236,763
Interest paid		(116,142)	(52,645)	(101,732)	(52,645)
Amounts paid to suppliers and employees		(327,522)	(234,383)	(300,651)	(221,749)
Operating cash flow before changes in operating assets	29	<b>390,594</b>	<b>385,700</b>	<b>409,513</b>	<b>390,778</b>
Decrease/(increase) in loans		(535,954)	(783,161)	(532,554)	(783,161)
Decrease/(increase) in bills receivable and other assets		28,679	19,356	(26,047)	19,356
(Decrease)/increase in deposits		920,295	728,423	961,889	729,268
(Decrease)/increase in bills payable and other liabilities		(126,547)	4,251	62,175	4,251
<b>Net cash flow from operations before income tax</b>		<b>677,067</b>	<b>354,569</b>	<b>874,976</b>	<b>360,492</b>
Income taxes paid	6(b)	(101,403)	(102,370)	(101,372)	(100,829)
<b>Net cash flow from operating activities</b>		<b>575,664</b>	<b>252,199</b>	<b>773,604</b>	<b>259,663</b>
<b>CASH FLOW FROM INVESTING ACTIVITIES</b>					
Decrease/(increase) in Government securities		(281,094)	(443,717)	(273,963)	(443,717)
Expenditure on property, plant and equipment		(32,747)	(28,124)	(27,822)	(27,830)
Proceeds from disposal of property, plant and equipment		2,472	7,552	1,184	7,423
Movement in share trading activities		3,575	2,985	-	-
Additional funding in associate		(800)	(883)	(800)	(883)
Net cash flow on acquisition of subsidiary		8,622	-	(180,100)	-
<b>Net cash flow from investing activities</b>		<b>(299,972)</b>	<b>(462,187)</b>	<b>(481,501)</b>	<b>(465,007)</b>
<b>CASH FLOW FROM FINANCING ACTIVITIES</b>					
Issue of share capital		-	46,478	-	46,478
Proceeds from subordinated debt securities		75,525	-	75,525	-
Proceeds from other financial activities		-	2,183	-	-
Client Management Trust		(6,745)	937	-	-
Dividends paid	24	(100,305)	(99,509)	(100,305)	(99,509)
<b>Net cash flow from financing activities</b>		<b>(31,525)</b>	<b>(49,911)</b>	<b>(24,780)</b>	<b>(53,031)</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>244,167</b>	<b>(259,899)</b>	<b>267,323</b>	<b>(258,375)</b>
Effect of exchange rate movements on cash and cash equivalents		(3,135)	(5,504)	(3,135)	(5,504)
Cash and cash equivalents at the beginning of the period-subsiary		213,466	-	-	-
Cash and cash equivalents at the beginning of the year		707,189	972,592	706,462	970,341
<b>Cash and cash equivalents at the end of the year</b>	26	<b>1,161,687</b>	<b>707,189</b>	<b>970,650</b>	<b>706,462</b>

The attached notes form an integral part of these financial statements

BSP TENNIS PROGRAM



## ACCOUNTING POLICIES for the Year Ended 31 December 2009

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 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.

The financial statements are presented in Papua New Guinea Kina, expressed in thousands of Kina, as permitted by Papua New Guinea Accounting Standards.

### 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 2009, 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 purchase method of accounting, where:

- acquisition cost is measured at fair value of assets acquired, 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

Associates are entities over which the Group has significant, but not controlling influence, generally accompanied by a shareholding conferring 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 post acquisition profits or losses are recognised in the statement of comprehensive income, and the Group's share of post acquisition reserve movements are recognised in reserves; Cumulative post acquisition movements are adjusted against the carrying value of the investment.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### D Derivative financial instruments and acceptances

Forward foreign exchange contracts entered into for trading purposes are initially recognised 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.

### E Revenue

#### Interest income and expense

Interest income and expense are recognised in the Statement of Comprehensive Income on an accrual basis using the effective yield method. The income arising from the various forms of instalment 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 Colonial Health Care (Fiji) Limited, a wholly owned subsidiary of the Group.

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 policy holder. 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 on in-force contracts that relates to unexpected 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 and are sold and underwritten by Colonial Fiji Life Limited, a wholly owned subsidiary. 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.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### E Revenue (continued)

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

Some of the 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.

A liability for contractual benefits that are expected to be incurred in the future is recorded when the premiums are recognised.

Firstly a base 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 Service 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 revised regularly and adjusted for actually experience on claims, expense, mortality and investment returns.

The base policy liability is then recalculated to arrive at a statutory policy liability, based on assumptions which anticipate more adverse experience than the best estimate experience. Allowance is made for future bonuses (if any) in line with these adverse assumptions. The statutory policy liability is calculated as follows:

For policies with a Discretionary Participation Feature the maximum of:

- the base policy liability calculated on adverse assumptions and with the use of discretions
- the base policy liability calculated on best estimate assumptions including policy holder retained earnings
- the current surrender value

For other policies the maximum of:

- the base policy liability calculated on adverse assumptions and with the use of discretions
- the current surrender value, or unearned premium reserve

The statutory policy liability is then increased by the solvency margin required under the Insurance Act 1998 and by the value of inadmissible assets.

### Claims, surrenders and maturities

Claims under insurance contracts are recognised in the financial statements when notified. Claims in respect of insurance contracts remaining in force at balance date are included in insurance contract liabilities.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### **F 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 capitalised and deferred over the expected term of the financial instrument.

### **G 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.

### **H 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.

### **I 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.

### **J 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.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### K 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 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 profit or loss. 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 lives, 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 % p a
Plant and equipment	Straight line basis	10 - 25% pa
Equipment under operating lease	Straight line basis	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.

### L 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 (Note 14) 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.



## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### **L Leases (continued)**

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.

### **M 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.

### **N Provisions**

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company 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.

### **O Employee benefits**

A liability is required for benefits accruing to employees in respect of wages and salaries, annual leave, long service leave when it is probable that settlement will be required and they 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.

#### **Post 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 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.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### P 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 Company 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 Company intends to settle its current tax assets and liabilities on a net basis.

#### 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.

### Q 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 income statement in the period in which they arise.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### R Foreign currency

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

In preparing the financial statements, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rate 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 asset 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.

### S 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.

#### 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. This 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.

## ACCOUNTING POLICIES for the Year Ended 31 December 2009

### T 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.

### U 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.

### V Comparatives

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

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## FINANCIAL RISK MANAGEMENT for the Year Ended 31 December 2009

### A 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 adverse 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 raise 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 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.

### B Capital adequacy

The Bank and the Group is required to comply with various prudential standards issued by the Bank of Papua New Guinea (BPNG), the official authority for the prudential supervision of banks and similar financial institutions in Papua New Guinea. One of the most critical prudential standards is the capital adequacy requirement. All banks are required to maintain at least the minimum 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 introduces the leverage capital ratio. In all months, the Bank and the Group complied with the prevailing prudential requirements for total capital and leverage capital. As at 31 December 2009, 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 as 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, un-audited 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.

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.

## B Capital adequacy (continued)

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

	Balance sheet/ notional amount		Risk-weighted amount	
	2009	2008	2009	2008
<i>All amounts are expressed in K'000</i>				
<b>Balance sheet assets (net of provisions)</b>				
Currency	999,683	439,866	-	-
Loans and advances	3,638,562	2,343,844	3,239,995	2,235,944
Investments and short term securities	3,838,282	3,363,056	-	-
All other assets	921,294	661,102	692,030	466,173
Off-balance sheet items	1,200,968	1,644,252	416,132	601,977
<b>Total</b>	<b>10,598,789</b>	<b>8,452,120</b>	<b>4,348,157</b>	<b>3,304,094</b>
<b>Capital Ratios</b>	Capital (K'000)		Capital Adequacy Ratio (%)	
	2009	2008	2009	2008
<b>a) Before YTD profits included in Tier 1 Capital</b>				
Tier 1 capital	598,310	479,999	12.6%	14.2%
Tier 1 + Tier 2 capital	1,054,789	772,427	22.1%	22.8%
<b>b) After YTD profits included in Tier 1 Capital</b>				
Tier 1 capital	855,428	708,333	18.0%	20.9%
Tier 1 + Tier 2 capital	1,054,789	772,427	22.1%	22.8%
<b>c) Leverage Capital Ratio – Before YTD profits included in Tier 1 Capital</b>			6.4%	7.1%
<b>d) Leverage Capital Ratio – After YTD profits included in Tier 1 Capital</b>			9.1%	10.4%

## FINANCIAL RISK MANAGEMENT

for the Year Ended 31 December 2009

**C 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.

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 H – 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 2009, the 25 largest exposures totaled K997 million, accounting for over 58.1% of the Bank and the Group's total loan portfolio (2008: K923 million, accounting for over 54.5%).

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.



## FINANCIAL RISK MANAGEMENT for the Year Ended 31 December 2009

### C Credit risk and asset quality (continued)

#### Economic sector risk concentrations

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

*All amounts are expressed in K'000*

	2009	%	2008	%
<b>As at 31 December</b>				
Commerce, finance and other business	1,855,439	51	1,166,424	49
Private households	463,963	13	409,463	17
Government and Public Authorities	8,214	-	5,795	1
Agriculture	260,051	7	256,940	11
Transport and communication	276,230	8	123,546	6
Manufacturing	397,624	11	174,607	7
Construction	377,041	10	207,069	9
Net loan portfolio balance	3,638,562	100	2,343,844	100

### D 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 2009.

The maturity profile of material Assets and Liabilities as at 31 December 2009 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 exploit 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. All commercial banks are required to hold a minimum of 25% of the value of total customer deposits in the form of prescribed liquid assets. As at 31 December 2009, the Bank and the Group's Liquid Asset Ratio was approximately 50.14% (2008: 47.57%), significantly in excess of the minimum requirement of 25%;

**FINANCIAL RISK MANAGEMENT**  
for the Year Ended 31 December 2009

**D Liquidity risk (continued)**

- The CRR specifies that a bank must hold an amount equal to 3% 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 11, Cash and Balances with Central Bank, and Note 26, Cash and cash equivalents.

**Maturity of assets and liabilities**

All amounts are expressed in K'000

As at 31 December 2009	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
<b>Assets</b>						
Cash and Central Bank assets	996,393	-	-	-	-	996,393
Treasury & Central Bank bills	1,731,100	187,543	407,070	-	-	2,325,713
Due from other banks	191,888	-	-	-	-	191,888
Loans and advances	655,024	397,321	577,755	1,289,713	718,749	3,638,562
Investments	-	35,000	87,349	567,150	823,070	1,512,659
Total assets	3,574,405	619,864	1,072,174	1,856,863	1,541,819	8,665,125
<b>Liabilities</b>						
Due to other banks	26,594	-	-	-	-	26,594
Due to customers	6,009,457	940,767	443,656	23,799	76,100	7,493,779
Other liabilities	648,389	22,566	-	-	75,525	746,480
Other provisions	156,006	26,553	-	-	14,312	196,871
Total liabilities	6,840,446	989,886	443,656	23,799	165,937	8,463,724
<b>Net liquidity gap</b>	<b>(3,266,041)</b>	<b>(370,022)</b>	<b>628,518</b>	<b>1,833,064</b>	<b>1,375,882</b>	<b>201,401</b>
<b>As at 31 December 2008</b>						
Total assets	1,897,169	638,560	1,149,322	1,547,702	1,192,752	6,425,505
Total liabilities	5,667,820	290,860	85,580	1,542	17,812	6,063,614
<b>Net liquidity gap</b>	<b>(3,770,651)</b>	<b>347,700</b>	<b>1,063,742</b>	<b>1,546,160</b>	<b>1,174,940</b>	<b>361,891</b>

**E 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. 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 organisation's compliance with them.

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

## FINANCIAL RISK MANAGEMENT

for the Year Ended 31 December 2009

### F 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.

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

All amounts are expressed in K'000

As at 31 December 2009	USD	AUD	EURO	PGK	Other	Total
<b>Assets</b>						
Cash and Central Bank assets	5,682	5,000	225	778,457	207,029	996,393
Treasury & Central Bank bills	-	-	-	2,305,708	20,005	2,325,713
Due from other banks	45,063	86,809	3,910	42,183	13,923	191,888
Loans and advances	15,980	1,796	-	2,840,808	779,978	3,638,562
Investments	-	-	-	1,331,311	181,256	1,512,567
Other assets	-	-	-	592,289	140,409	732,698
<b>Total assets</b>	<b>66,725</b>	<b>93,605</b>	<b>4,135</b>	<b>7,890,756</b>	<b>1,342,600</b>	<b>9,397,821</b>
<b>Liabilities</b>						
Due to other banks	-	-	-	(12,202)	(14,392)	(26,594)
Due to customers	(117,692)	(120,373)	(789)	(6,520,544)	(734,381)	(7,493,779)
Other liabilities	-	-	-	(413,253)	(530,098)	(943,351)
<b>Total liabilities</b>	<b>(117,692)</b>	<b>(120,373)</b>	<b>(789)</b>	<b>(6,945,999)</b>	<b>(1,278,871)</b>	<b>(8,463,724)</b>
<b>Net on-balance sheet position</b>	<b>(50,967)</b>	<b>(26,768)</b>	<b>3,346</b>	<b>944,757</b>	<b>63,729</b>	<b>934,097</b>
<b>Off-balance sheet net notional position</b>						
Credit commitments	16,648	9,269	7,105	-	10,237	43,259
	-	-	-	1,111,273	-	-
<b>As at 31 December 2008</b>						
Total Assets	59,002	171,567	2,012	6,531,434	43,853	6,807,868
Total Liabilities	88,396	86,688	753	5,624,885	262,892	6,063,614
<b>Net on-balance sheet position</b>	<b>(29,394)</b>	<b>84,879</b>	<b>1,259</b>	<b>906,549</b>	<b>(219,039)</b>	<b>744,254</b>
<b>Off-balance sheet net notional position</b>						
Credit commitments	45,340	7,488	6,419	-	5,914	66,179
	-	-	-	1,730,411	-	-

**FINANCIAL RISK MANAGEMENT**  
for the Year Ended 31 December 2009

**G 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 2009 and prevailing rates of interest, a 1% increase in rates will result in a K1.29 million decrease in net interest income, whilst a 1% decrease in rates will result in a K0.005 million increase in net interest income.

**Effective interest rates as at 31 December**

*Amounts are expressed in % p.a.*

	2009	2008
<b>Assets</b>		
Cash and Central Bank assets	7.00	6.00
Treasury and Central Bank bills	7.05	7.34
Due from other banks	7.00	6.00
Loans and advances	13.30	11.02
Investments	9.50	9.12
<b>Liabilities</b>		
Due to other banks	7.00	6.00
Due to customers	3.00	2.00

## FINANCIAL RISK MANAGEMENT for the Year Ended 31 December 2009

### G Interest rate risk (continued)

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

All amounts are expressed in K'000

As at 31 December 2009	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non interest bearing
<b>Assets</b>						
Cash and Central Bank assets	-	-	-	-	-	996,393
Treasury & Central Bank bills	1,731,100	187,543	407,070	-	-	-
Due from other banks	191,888	-	-	-	-	-
Loans and advances	1,599,968	401,010	697,185	576,658	363,737	4
Investments	-	35,000	87,349	567,150	823,070	-
Other assets	-	-	-	-	-	732,696
<b>Total assets</b>	<b>3,522,956</b>	<b>623,553</b>	<b>1,191,604</b>	<b>1,143,808</b>	<b>1,186,807</b>	<b>1,729,093</b>
<b>Liabilities</b>						
Due to other banks	26,594	-	-	-	-	-
Due to customers	4,575,913	574,476	309,656	23,799	76,100	1,933,835
Other liabilities	-	-	-	-	75,525	867,826
<b>Total liabilities</b>	<b>4,602,507</b>	<b>574,476</b>	<b>309,656</b>	<b>23,799</b>	<b>151,625</b>	<b>2,801,661</b>
<b>Interest sensitivity gap</b>	<b>(1,079,551)</b>	<b>49,077</b>	<b>881,948</b>	<b>1,120,008</b>	<b>1,035,185</b>	<b>-</b>
<b>As at 31 December 2008</b>						
<b>Assets</b>						
Cash and Central Bank assets	-	-	-	-	-	434,627
Treasury & Central Bank bills	717,500	443,540	672,870	-	-	-
Due from other banks	283,978	-	-	-	-	-
Loans and advances	1,213,320	206,279	425,186	379,809	119,246	4
Investments	-	89,884	117,459	629,992	691,811	-
Other assets	-	-	-	-	-	382,363
<b>Total assets</b>	<b>2,214,798</b>	<b>739,703</b>	<b>1,215,515</b>	<b>1,009,801</b>	<b>811,057</b>	<b>816,994</b>
<b>Liabilities</b>						
Due to other banks	11,416	-	-	-	-	-
Due to customers	4,163,431	410,751	85,572	11,525	26	1,110,715
Other liabilities	-	-	-	-	-	270,178
<b>Total liabilities</b>	<b>4,174,847</b>	<b>410,751</b>	<b>85,572</b>	<b>11,525</b>	<b>26</b>	<b>1,380,893</b>
<b>Interest sensitivity gap</b>	<b>(1,960,049)</b>	<b>328,952</b>	<b>1,129,943</b>	<b>998,276</b>	<b>811,031</b>	<b>-</b>

**FINANCIAL RISK MANAGEMENT**  
for the Year Ended 31 December 2009

**H 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 2009, stated at the face value of the respective contracts are:

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

<b>As at 31 December 2009</b>		<b>USD</b>	<b>AUD</b>	<b>EURO</b>	<b>GBP</b>	<b>Other</b>	<b>Total</b>
Selling	FCY	1,831	15,874	100	4,500	1,287	-
	<b>Kina</b>	<b>5,504</b>	<b>38,279</b>	<b>368</b>	<b>7,353</b>	<b>2,497</b>	<b>54,001</b>
Buying	FCY	(45,382)	(32,500)	(20)	(5,161)	-	-
	<b>Kina</b>	<b>(120,585)</b>	<b>(29,631)</b>	<b>(77)</b>	<b>(22,501)</b>	<b>-</b>	<b>(172,794)</b>
<b>As at 31 December 2008</b>							
Selling	FCY	11,681	49,468	200	-	74,778	-
	<b>Kina</b>	<b>31,346</b>	<b>98,019</b>	<b>823</b>	<b>-</b>	<b>10,078</b>	<b>140,266</b>
Buying	FCY	(7,255)	-	-	(8,240)	-	-
	<b>Kina</b>	<b>(19,184)</b>	<b>-</b>	<b>-</b>	<b>(32,939)</b>	<b>-</b>	<b>(52,123)</b>

**I Policy liabilities**

Key assumptions used in determining this liability are as follows:

**(i) Discount Rates**

For contracts which have a Discretionary Participation Feature (DPF), the discount rate used is linked to the assets which back those contracts. For 31 December 2009 this was 4.46% per annum (30 June 2009: 6.02% per annum), based on 5 year government bond rate and expected earnings from the investment portfolio. For contracts without DPF, a rate of 2.80% per annum was used at 31 December 2009 (30 June 2009: 5.71% per annum). For Accident business a rate of 2.76% per annum was used at 31 December 2009 (30 June 2009: 5.62% per annum). These rates were based on the 5 year government bond rate.

**(ii) Investment and Maintenance Expenses**

Future maintenance and investment expenses have been derived from budgeted expenses. Future inflation has been assumed to be 3.5% per annum (30 June 2009 3.5% per annum) for determining future expenses.

**(iii) Taxation**

The rates of taxation enacted or substantially enacted at the date of the valuation (i.e. 31%) are assumed to continue into the future.

The reduction in tax rates from financial year 2010 would have an immaterial impact on policy liabilities with any reduction in the liability materially offset by an increase in bonus rate.

## FINANCIAL RISK MANAGEMENT for the Year Ended 31 December 2009

### I Policy liabilities (continued)

#### (iv) Mortality and Morbidity

Projected future rates of mortality for insured lives are based on the Fiji Mortality Statistics performed in 1998. These are then adjusted by comparing with the Group's own experience. For the reported months, the mortality rates used was 85% of the mortality statistics. Assumptions are reviewed based on annual experience studies. There have been no changes to mortality assumptions for the current year.

#### (v) 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:

	31 Dec 2009	30 Jun 2009
Whole of Life and Endowment Insurance	14%	14%
Term Insurance	15%	15%
Accident Insurance	13%	13%

#### (vi) 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.

#### (vii) 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% (30 June 2009: 20%). For business written 1995 and 1998 the shareholder receives 11% of distributions.

In applying the contract holders' share of profits to provided bonuses, consideration is given to equity between generations of policyholders and 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 shareholders right to participate in distributions.

Assumed future bonus rates per annum for the major classes of participating businesses range from 1.60% to 3.50% per annum (30 June 2009: 1.60% to 3.50% per annum).

#### Reinsurance

Contracts entered into by the Group with Reinsurers under which the Group is compensated for losses on one or more contracts issued by the Group, 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 Income Statement when they become due and payable in accordance with the reinsurance agreements.

Reinsurance recoveries for claims are recognised as Reinsurance recoveries under claims. Reinsurance premiums re recognised as Reinsurance Expenses.

**NOTES TO THE FINANCIAL STATEMENTS  
for the Year Ended 31 December 2009**

1	Net interest income	Group		Bank	
		2009	2008	2009	2008
	<i>All amounts are expressed in K'000</i>				
	<b>Interest income</b>				
	Cash and short term funds	1,167	6,368	1,167	6,368
	Public Securities: Treasury bills and Inscribed stock	282,801	211,996	282,406	211,996
	Loans and advances	298,196	216,604	293,106	216,604
	Other	698	1,006	275	688
		582,862	435,974	576,954	435,656
	Less:				
	<b>Interest expense</b>				
	Customer deposits	103,555	58,374	101,408	58,374
	Other banks	1,666	457	1,666	457
	Subordinated debt securities	3,664	-	3,664	-
	Other borrowings	8	43	8	43
		108,893	58,874	106,746	58,874
		473,969	377,100	470,208	376,782
2	<b>Net fee and commission income</b>				
	Fee and commission income				
	Credit related	38,941	33,444	38,561	33,444
	Trade and international related	165	208	165	208
	Electronic banking related	8,735	6,004	8,735	6,004
	Brokerage & fee income	1,996	2,064	-	-
	Other	59,293	45,960	58,890	43,629
		109,130	87,680	106,351	83,285
	Less:				
	Fee and commission expenses				
	Agencies	321	371	321	371
		321	371	321	371
		108,809	87,309	106,030	82,914



## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

3	<b>Other income</b> <i>All amounts are expressed in K'000</i>	<b>Group</b>		<b>Bank</b>	
		<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	Foreign Exchange related	104,338	127,074	104,338	127,074
	Net insurance premium income	6,621	-	-	-
	Other	31,975	29,445	21,285	26,639
		<b>142,934</b>	<b>156,519</b>	<b>125,623</b>	<b>153,713</b>
	<b>Included in other income:</b>				
	Profit/(loss) on sale of fixed assets	1,184	6,665	1,184	6,665
	Change in fair value of assets held through profit and loss	2,755	-	-	-
	Foreign Exchange related income includes gains and losses from spot and forward contracts and translated foreign currency assets.				
4	<b>Bad and doubtful debts (expense)/recovery</b>				
		29,498	8,787	29,584	8,787
	Bad debts recovered - net	(44,518)	(20,140)	(45,960)	(20,140)
	Net charge to doubtful debts provision	(15,020)	(11,353)	(16,376)	(11,353)
5	<b>Other operating expenses</b>				
		74,508	43,525	73,291	41,908
	Administration	1,178	966	1,153	913
	Auditors' remuneration	16,332	15,819	16,332	15,819
	Computing	37,371	26,766	36,556	26,636
	Depreciation	1,684	696	1,684	696
	Amortisation of computer development	886	1,339	886	1,339
	Non-executive Directors' costs	25,683	8,166	24,900	8,166
	Non-lending losses	1,397	(68)	1,397	(68)
	Fixed asset write off	37,953	22,861	37,953	22,833
	Premises and equipment	7,556	-	-	-
	Increase/(decrease) in policy liabilities	4,782	-	-	-
	Claims, surrender and maturities	209,330	120,070	194,152	118,242
	<b>Staff costs</b>	4,236	3,707	4,236	3,707
	Defined contribution plans	5,808	3,970	5,467	3,970
	Statutory benefits contributions	89,056	80,231	86,662	77,446
	Wages and salaries	26,716	21,621	18,167	20,689
	Other	125,816	109,529	114,532	105,812
		<b>335,146</b>	<b>229,599</b>	<b>308,684</b>	<b>224,054</b>

**NOTES TO THE FINANCIAL STATEMENTS  
for the Year Ended 31 December 2009**

6(a)	Income tax expense	Group		Bank	
		2009	2008	2009	2008
	<i>All amounts are expressed in K'000</i>				
	Current tax	128,170	104,441	127,783	103,679
	Deferred tax	(13,463)	(4,998)	(14,045)	(4,848)
	Current year	114,707	99,443	113,739	98,831
	Prior year adjustments	6,318	1,021	6,487	1,214
		121,025	100,464	120,226	100,045
	Tax calculated at 30% of profit before tax (2008: 30%)	113,052	98,639	113,389	98,047
	Tax calculated at 29% of profit before tax - subsidiary	842	-	-	-
	Expenses not deductible for tax	2,050	1,283	1,398	1,217
	Deductible expenses not recognised for accounting purposes	(1,049)	(479)	(1,049)	(433)
	Net insurance income not subject to tax	2,974	-	-	-
	Tax benefit not brought to account - subsidiary	(3,162)	-	-	-
	Prior year under provision	6,318	1,021	6,487	1,214
		121,025	100,464	120,226	100,045
	Further information about deferred taxes is presented in note 17.				
6(b)	<b>Income tax recoverable / (provision for income tax)</b>				
	<b>Recoverable / (provision) comprise:</b>				
	At 1 January	(68,416)	(68,164)	(68,355)	(67,134)
	Opening balance – subsidiary	(5,898)	-	-	-
	Income tax provision	(128,170)	(98,639)	(127,784)	(98,047)
	Deferred tax movement	-	(4,998)	-	(4,848)
	Expenses not deductible for tax	(1,398)	(1,284)	(1,398)	(1,215)
	Deductible expenses not recognised for accounting purposes	1,049	479	1,049	443
	Prior year over / (under) provision	(8,261)	1,820	(8,261)	1,627
	Foreign tax paid	4,866	4,321	4,866	4,321
	Tax payments made	96,537	98,049	96,506	96,508
	<b>At 31 December</b>	<b>(109,691)</b>	<b>(68,416)</b>	<b>(103,377)</b>	<b>(68,355)</b>

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

### 7 Acquisition of Subsidiaries

In November 2009, Bank of South Pacific Limited under its investment plans purchased the National Bank of Fiji Limited and Colonial Fiji Life Limited for K180.100 million. The previous shareholder of these entities was the Commonwealth Bank of Australia. The bank is one of the largest in Fiji. This acquisition provides strategic opportunities for the Bank and the Group and would now be regarded as one of the largest business entities in the region. For consolidation purposes of its 2009 results, only the December 2009 operating results have been incorporated into the Group's profit and loss.

Subsidiaries acquired	Principal activity	Date of acquisition	Proportion of shares acquired	Consideration transferred* K'000
Colonial Fiji Life Ltd	Insurance	30 November 2009	100%	80,714
National Bank of Fiji Ltd	Banking	30 November 2009	100%	99,386
				180,100
*consideration transfer in cash				

#### Asset and liabilities acquired at the date of acquisition:

All amounts are expressed in K'000

	Colonial Fiji Life Ltd	National Bank of Fiji Ltd	Total
Cash and cash equivalents	94,840	93,882	188,722
Loans & advances to customers	110,387	675,285	785,672
Other assets	301,699	136,451	438,150
Amounts due to customers	-	(774,263)	(774,263)
Other liabilities	(422,332)	(27,191)	(449,523)
Net assets & liabilities	84,594	104,164	188,758

#### Net cash inflow on acquisition of subsidiaries:

	2009 K,000
Consideration paid in cash	180,100
Less: cash and cash equivalent balances acquired	(188,722)
Net cash inflow	8,622

### 8 CDO Provision

6,860

50,000

In 2008 and prior periods, BSP Capital Limited, a subsidiary of the Bank, marketed certain collateralised debt obligation investment products issued or arranged by Lehman Brothers. The value of the notes was seriously impaired following the unfolding global financial crisis, particularly the demise of Lehman Brothers, which was the primary issuer or promoter in the majority of cases. Value remains subject to great uncertainty, because of the status of the issuer/promoter, because the general level of financial asset prices have declined dramatically over the last year as the global financial crisis has developed, and because of the complex investment structures and contractual relationships causing difficulties in identifying the nature and quality of the assets underlying these instruments.

The K50 million asset impairment adjustment/provision in respect of these events was arrived at as a prudent estimate of the cost to BSP Group of protecting against reputation risk & risk of financial loss.

In 2009 and up to the date of these financial statements, approximately K43.140 million of these anticipated losses have been realized.

**NOTES TO THE FINANCIAL STATEMENTS  
for the Year Ended 31 December 2009**
**9 Intangible asset**

	Group		Bank	
	2009	2008	2009	2008
<i>All amounts are expressed in K'000</i>				
Gross carrying amount	21,333	-	-	-
Impairment adjustment	-	-	-	-
	21,333	-	-	-

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 is considered not materially impaired.

**10 Investments in Associates**

Name of Associates	Principal activity	Place of incorporation and operation	Proportion of ownership and voting power held	
			2009	2008
PNG Micro Finance Limited	Micro Finance	PNG	32%*	32%*
Suva Central Limited	Property Rental	Fiji	50%*	-
Richmond Limited	Hotel operation	Fiji	61%** , 50%***	-
Williams and Gosling	Freight forwarding	Fiji	20.4%*	-

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

	Group		Bank	
	2009	2008	2009	2008
<i>All amounts are expressed in K'000</i>				
Investment in associate	46,708	2,121	1,826	2,121
Additional funding	800	883	800	883
Share of loss for year ending 31 December 2009	225	(1,178)	(1,209)	(1,178)
Net investment in associate	47,733	1,826	1,417	1,826
<b>Summarised financial information of associates:</b>				
Total assets	217,421	51,693	39,924	51,693
Total liabilities	(122,925)	(46,053)	(37,533)	(46,053)
Net assets	94,496	5,640	2,391	5,640
Net profit/(loss)	3,228	(2,944)	(3,779)	(2,944)
<b>Share of associate's profit or loss:</b>				
Share of associate's profit/(loss)	225	(1,178)	(1,209)	(1,178)
<b>11 Cash and balances with Central Bank</b>				
Notes and coins	233,722	106,542	152,762	105,815
Balances with Central Bank other than statutory deposit	401,872	156,358	378,016	156,358
Included in cash and cash equivalents	635,594	262,900	530,778	262,173
Statutory deposits with Central Bank	360,799	171,727	265,419	171,727
	996,393	434,627	796,197	433,900
<b>12 Treasury &amp; Central Bank Bills</b>				
Treasury & Central Bank Bills - face value	2,357,862	1,882,157	2,337,857	1,882,157
Discount for interest receivable	(32,149)	(48,247)	(32,149)	(48,247)
	2,325,713	1,833,910	2,305,708	1,833,910

Treasury & Central Bank bills are debt securities issued by the Central Bank. These Bills are classified as assets held for trading and carried at fair value.

# NOTES TO THE FINANCIAL STATEMENTS

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

13	<b>Amounts due from other banks</b> <i>All amounts are expressed in K'000</i>	<b>Group</b>		<b>Bank</b>	
		<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	Items in the course of collection	84,874	241,378	84,874	241,378
	Placements with other banks	107,014	42,600	101,781	42,600
	Included in cash and cash equivalents	191,888	283,978	186,655	283,978
<b>14</b>	<b>Loans and advances to customers</b> <b>Loans originated by the Bank</b>				
	Overdrafts	614,085	462,795	566,655	462,795
	Leases	182,142	127,320	182,142	127,320
	Term loans	2,296,478	1,671,466	2,043,497	1,671,466
	Mortgages	629,187	132,759	153,252	132,759
	Policy loans	46,430	-	-	-
	Gross loans and advances net of reserved interest	3,768,322	2,394,340	2,945,546	2,394,340
	Less allowance for losses on loans and advances	(129,760)	(50,496)	(85,524)	(50,496)
		3,638,562	2,343,844	2,860,022	2,343,844
	<b>Allowance for losses on loans and advances</b>				
	Movement in allowance for losses on loans and advances:				
	Balance at 1 January	50,496	41,174	50,496	41,174
	Opening balance – subsidiary	42,382	-	-	-
	New provision	23,581	6,364	22,225	6,364
	Loans written off against provisions/write back of provisions no longer required	13,301	2,958	12,803	2,958
	Balance at 31 December	129,760	50,496	85,524	50,496

### Loans and advances to customers includes finance lease receivables, analysed as follows:

	Investment in finance leases receivable				
	Not later than 1 year	15,061	13,199	15,061	13,199
	Later than 1 year and not later than 5 years	177,246	129,156	182,142	129,156
	Later than 5 years	-	-	-	-
		192,307	142,355	197,203	142,355
	Unearned future finance income	(12,974)	(15,035)	(12,974)	(15,035)
	Net investment in finance leases	179,333	127,320	184,229	127,320
	The net investment in finance leases is analysed as follows:				
	Not later than 1 year	14,580	12,738	14,580	12,738
	Later than 1 year and not later than 5 years	169,649	114,582	169,649	114,582
	Later than 5 years	-	-	-	-
		184,229	127,320	184,229	127,320
<b>15(a)</b>	<b>Properties held for sale</b>				
	Premises	9,011	119	-	119
	Accumulated depreciation	-	(119)	-	(119)
		9,011	-	-	-

Assets held for sale have been identified and have not been depreciated during the year and are expected to be sold within the next 12 months.

**NOTES TO THE FINANCIAL STATEMENTS  
for the Year Ended 31 December 2009**

15(b)	Property, plant and equipment <i>All amounts are expressed in K'000</i>	Group		Bank	
		2009	2008	2009	2008
(i)	Carrying value				
	Capital works in progress	58,347	38,787	46,284	38,787
	Premises	209,859	139,913	200,378	139,913
	Accumulated depreciation	(32,781)	(26,336)	(32,107)	(26,336)
		177,078	113,577	168,271	113,577
	Equipment	200,349	154,225	182,134	153,830
	Accumulated depreciation	(153,528)	(131,146)	(153,387)	(131,146)
		46,821	23,079	28,747	22,684
		282,246	175,443	243,302	175,048
(ii)	Reconciliations				
	<b>Capital WIP</b>				
	At 1 January	38,787	38,569	38,787	38,569
	Opening balance – subsidiary	13,135	-	-	-
	Additions	38,194	24,094	35,989	24,094
	Transfers	(31,769)	(24,159)	(28,492)	(24,159)
	Adjustments	-	283	-	283
	<b>At 31 December</b>	58,347	38,787	46,284	38,787
	<b>Premises</b>				
	At 1 January	113,577	112,613	113,577	112,613
	Opening balance – subsidiary	9,120	-	-	-
	Additions	3,383	9,381	2,726	9,381
	Disposals	(2,052)	(3,248)	(1,756)	(3,248)
	Adjustments prior year	2,354	-	2,354	-
	Revaluation Increases	57,141	-	57,141	-
	Depreciation expense	(6,445)	(5,169)	(5,771)	(5,169)
	<b>At 31 December</b>	177,078	113,577	168,271	113,577
	<b>Equipment</b>				
	At 1 January	22,684	19,067	22,684	19,067
	Opening balance – subsidiary	17,614	-	-	-
	Additions	25,652	14,274	24,494	14,274
	Disposals	(3,552)	(56)	(2,600)	(56)
	Adjustments prior year	6,410	-	6,410	-
	Depreciation expense	(22,382)	(10,206)	(22,241)	(10,601)
	<b>At 31 December</b>	46,821	23,079	28,747	22,684

**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 capitalisation of the notional income stream approach on the Market Value basis. The effective date of the valuation is 9<sup>th</sup> October 2009.

The carrying amount of land and buildings had they been recognised under the cost model are as follows:

	2009	2008	2009	2008
Freehold land	11,461	4,405	11,461	4,405
Buildings	75,906	42,869	75,906	42,869
	87,367	47,274	87,367	47,274

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

15(c)	<b>Assets subject to operating lease</b> <i>All amounts are expressed in K'000</i>	<b>Group</b>		<b>Bank</b>	
		<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
<b>(i)</b>	<b>Carrying value</b>				
	Aircraft	115,041	115,041	115,041	115,041
	Accumulated depreciation	(29,017)	(20,473)	(29,017)	(20,473)
		<b>86,024</b>	<b>94,568</b>	<b>86,024</b>	<b>94,568</b>
	Reconciliation				
	Aircraft				
	At 1 January	94,568	91,397	94,568	91,397
	Additions	-	11,715	-	11,715
	Depreciation	(8,544)	(8,544)	(8,544)	(8,544)
	<b>At 31 December</b>	<b>86,024</b>	<b>94,568</b>	<b>86,024</b>	<b>94,568</b>
<b>(ii)</b>	<b>Future minimum lease payments</b>				
	Not later than one year	13,164	13,164	13,164	13,164
	Later than 1 year and not later than 5 years	9,240	22,404	9,240	22,404
	Later than 5 years	-	-	-	-
		<b>22,404</b>	<b>35,568</b>	<b>22,404</b>	<b>35,568</b>
<b>15(d)</b>	<b>Investment Properties</b>				
	Opening net book value	-	-	-	-
	Opening net book value – subsidiary	79,703	-	-	-
	Additional	298	-	-	-
	Transfer to properties held for sale	(9,011)	-	-	-
	<b>At 31 December</b>	<b>70,990</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>16</b>	<b>Other financial assets</b>				
	<b>Securities - held to maturity</b>				
	Inscribed stock - issued by Bank of Papua New Guinea	1,491,431	1,529,146	1,331,311	1,529,146
	<b>Financial assets carried at fair value through profit and loss:</b>				
	Equity securities	21,138	-	-	-
	<b>At 31 December</b>	<b>1,512,569</b>	<b>1,529,146</b>	<b>1,331,311</b>	<b>1,529,146</b>

### 17 Deferred tax asset

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 30% applicable from 1 January 2009 (2008: 30%). Deferred income taxes are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable. At 31 December 2009, the net benefit reflects the estimated future tax benefits at applicable income tax rates of the following:

Specific allowance for losses on loans and advances	15,332	7,196	9,760	7,196
General allowance for losses on loans and advances	19,669	7,870	15,897	7,870
Employee related provisions	9,531	6,311	7,878	6,214
Prepaid expenses	-	(30)	-	(20)
Other provisions	4,005	5,791	3,693	5,622
Depreciation and amortisation	(23,542)	(13,268)	(22,566)	(13,264)
Unrealised foreign exchange gains	(9,314)	(3,859)	(9,314)	(3,859)
Deferred expenditure	5,041	41	3,982	41
	<b>20,722</b>	<b>10,052</b>	<b>9,329</b>	<b>9,800</b>

**NOTES TO THE FINANCIAL STATEMENTS**  
for the Year Ended 31 December 2009

**17 Deferred tax asset (continued)**

The movements on the deferred income tax accounts are as follows:

<i>All amounts are expressed in K'000</i>	<b>Group</b>		<b>Bank</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
At 1 January	10,052	5,365	9,800	5,266
Specific allowance for losses on loans and advances	8,136	1,044	2,564	1,044
General allowance for losses on loans and advances	11,799	2,528	8,027	2,528
Employee related provisions	3,220	807	1,663	768
Depreciation and amortisation	(10,274)	222	(9,302)	221
Prepaid expenses	30	224	20	228
Other provisions	(1,786)	1,175	(1,929)	1,058
Unrealised foreign exchange gains	(5,455)	(1,295)	(5,455)	(1,295)
Deferred expenditure	5,000	(18)	3,941	(18)
<b>At 31 December</b>	<b>20,722</b>	<b>10,052</b>	<b>9,329</b>	<b>9,800</b>
<b>Represented by:</b>				
Future income tax benefit	52,603	27,146	41,210	26,881
Deferred tax liability	(31,881)	(17,094)	(31,881)	(17,081)
<b>At 31 December</b>	<b>20,722</b>	<b>10,052</b>	<b>9,329</b>	<b>9,800</b>

Taxable & deductible temporary differences arise from the following:

<i>All amounts are expressed in K'000</i>							
<b>Group</b>							
<b>2009</b>	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Subsidiary-opening balance	Closing balance
Gross deferred tax liabilities	(17,094)	(271)	2,625	(17,141)	-	-	(31,881)
Gross deferred tax assets	27,146	13,734	-	-	-	11,723	52,603
	<b>10,052</b>	<b>13,463</b>	<b>2,625</b>	<b>(17,141)</b>	<b>-</b>	<b>11,723</b>	<b>20,722</b>

<b>Group</b>							
<b>2008</b>	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Others	Closing balance
Gross deferred tax liabilities	(16,238)	(532)	(324)	-	-	-	(17,094)
Gross deferred tax assets	21,603	5,531	12	-	-	-	27,146
	<b>5,366</b>	<b>4,998</b>	<b>(312)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>10,052</b>



# NOTES TO THE FINANCIAL STATEMENTS

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

### 17 Deferred tax asset (continued)

*All amounts are expressed in K'000*

<b>Bank</b>							
<b>2009</b>	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Others	Closing balance
Gross deferred tax liabilities	(17,081)	(284)	2,625	(17,141)	-	-	(31,881)
Gross deferred tax assets	26,881	14,329	-	-	-	-	41,210
	9,800	14,045	2,625	(17,141)	-	-	9,329

**Bank**

<b>2008</b>	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Others	Closing balance
Gross deferred tax liabilities	(16,238)	(529)	(314)	-	-	-	(17,081)
Gross deferred tax assets	21,504	5,377	-	-	-	-	26,881
	5,266	4,848	(314)	-	-	-	9,800

### 18 Other assets

*All amounts are expressed in K'000*

	<b>Group</b>		<b>Bank</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Items in transit and other assets	46,143	28,166	34,765	3,259
Accrued income	51,777	50,130	44,161	50,130
Intercompany account	-	-	-	5,511
Computer development costs	2,934	708	2,934	708
Outstanding premiums	23,566	-	-	-
Inventory	4,676	-	-	-
Prepayments	6,409	4,103	6,409	4,103
Accounts receivable	28,251	273	411	273
	162,756	83,380	88,680	63,984

### 19 Amounts due to other banks

Items in the course of collection	26,594	11,416	12,202	11,416
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### 20 Amounts due to customers

Demand / current	5,471,424	4,336,231	5,106,154	4,340,356
Term	2,022,355	1,445,789	1,653,472	1,445,789
	7,493,779	5,782,020	6,759,626	5,786,145

**NOTES TO THE FINANCIAL STATEMENTS  
for the Year Ended 31 December 2009**

**21(a) Other liabilities**

*All amounts are expressed in K'000*

	2009	2008	2009	2008
Creditors and accruals	36,672	12,557	27,760	12,557
Items in transit and all other liabilities	186,071	92,987	174,500	95,436
Policy liabilities	423,258	-	-	-
Premiums received in advance	4,432	-	-	-
Outstanding claims	5,451	-	-	-
Claims incurred but not reported (IBNR)	1,624	-	-	-
Borrowings	13,447	-	-	-
	<b>670,955</b>	<b>105,544</b>	<b>202,260</b>	<b>107,993</b>

**21(b) 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. The Group has not had any defaults of interest or other breaches with respect to its debt securities in 2009.

**22 Other provisions**

Staff related	34,461	21,865	26,708	20,979
Provision for non lending loss	12,539	54,146	10,771	54,146
Provision for dividend payable	-	2	-	2
Provision for offshore creditors' GST	8,299	3,111	8,299	3,111
	<b>55,299</b>	<b>79,124</b>	<b>45,778</b>	<b>78,238</b>
<b>Staff related provisions</b>				
At 1 January	21,865	18,515	20,979	18,149
Provisions charge	17,202	6,391	7,440	6,279
Payouts	(4,606)	(3,041)	(1,713)	(3,449)
At 31 December	<b>34,461</b>	<b>21,865</b>	<b>26,708</b>	<b>20,979</b>

**23 Ordinary shares - Bank**

*Number of shares in '000s, book value in K'000*

	Number of Shares	Book Value
At 31 December 2007/1 January 2008	451,624	271,536
Dividend re-investment plan	36,168	43,762
Exercise of EMSOP for prior year	100	31
Exercise of EMSOP	6,818	2,685
Sharesplit (1/10)	4,064,618	-
At 31 December 2008/1 January 2009	4,559,328	318,014
Movement during the year	-	-
<b>At 31 December 2009</b>	<b>4,559,328</b>	<b>318,014</b>

In 2009, the Dividend Re-Investment Plan was not implemented. The executive management did not exercise their 2007 EMSOP options in 2009. Instead, an amount equal to the cash benefit, had the options been exercised, was paid to option holders.

The issued capital of Bank of South Pacific Limited comprises ordinary shares. Following is a summary of principal shareholders as at 31 December 2009 and their respective percentage holdings.

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

### 23 Ordinary shares – Bank (continued)

<b>Major shareholders: % shareholding</b>	<b>2009</b>	<b>2008</b>
Independent Public Business Corporation	23.49	23.49
Nominees Niugini Limited	11.63	11.63
Nambawan Super Limited	10.49	10.66
Petroleum Resources Kutubu Limited	10.12	10.12
Credit Corporation (PNG) Limited	8.43	8.54
National Superannuation Fund Limited	7.13	7.10
PNG Sustainable Development Program Limited	6.43	6.38
PNG Teachers Savings and Loans Society Limited	4.01	4.01
Comrade Trustee Services	3.42	3.42
Tropicana Limited	1.09	1.09
	86.24	86.44
All Others	13.76	13.56
	100.00	100.00

#### Share Options - Executive Management Share Option Plan

An Executive Management Share Option Plan was established at the Annual General Meeting of 27 May 2004. The first tranche of options of 1,121,818 were exercised on 30 June 2006. These options were valued at Mark to Market. The second tranche of options of 1,481,818 were exercised on 30 June 2007.

The third tranche of options remaining of 781,818 with a vesting date of 1 July 2008, and an exercise price of K3.38 were exercised on 30 June 2008. As per the ordinary shares being split 1/10 in 2008, these options were also split to 7,818,180 and exercised price was adjusted at K0.338.

On 1 July 2007, the Board under this plan, granted the fourth tranche of options over ordinary shares of Bank of South Pacific Limited and the Group to the executives only. These options were issued for nil consideration, are not transferable, and cannot be quoted on any stock exchange.

On 1 July 2009, the 2007 EMSOP was not exercised. Instead, an amount equal to the cash benefit, had the options been exercised, was paid to option holders.

On 1 July 2008, the Board under this plan, granted the fifth tranche of options over ordinary shares of Bank of South Pacific Limited and the Group to the executives only. These options were issued for nil consideration, are not transferable, and cannot be quoted on any stock exchange.

At balance date there are 8,000,000 of these options issued, with a vesting date of 1 July 2010, and an exercise price of K1.26. The overriding exercise conditions of these options are performance hurdles.

The 2008 share options have been valued in compliance with IFRS 2 and classified as equity on the balance sheet.

NOTES TO THE FINANCIAL STATEMENTS  
 for the Year Ended 31 December 2009

## 23 Ordinary shares – Bank (continued)

Options 2009	Opening balance	Share split	Issued	Exercised	Forfeited	Others	Closing Balance
2007	7,000	-	-	-	7,000	-	-
2008	8,000	-	-	-	-	-	8,000
2009	-	-	-	-	-	-	-
<b>Total</b>	15,000	-	-	-	7,000	-	8,000
<b>Weighted average exercise price</b>	0.91	-	-	-	0.505	-	1.26
Options 2008	Opening balance	Share split	Issued	Exercised	Forfeited	Others	Closing Balance
2006	782	7,818	-	6,818	1,000	-	-
2007	700	7,000	-	-	-	-	7,000
2008	-	-	8,000	-	-	-	8,000
<b>Total</b>	1,482	14,818	8,000	6,818	1,000	-	15,000
<b>Weighted average exercise price</b>	4.20	0.42	1.26	0.33	0.33	-	0.91

## 24 Reserves and retained earnings/(accumulated losses)

All amounts are expressed in K'000

	Group		Bank	
	2009	2008	2009	2008
<b>Reserves comprise:</b>				
Revaluation reserve	68,774	31,146	68,774	31,146
Capital reserve	635	635	635	635
Options reserve	1,311	1,560	1,311	1,560
Exchange reserve	(11,424)	(4,343)	(7,156)	(294)
General reserve	2,875	2,875	2,875	2,875
	62,171	31,873	66,439	35,922
<b>Movement in reserves for the year:</b>				
<b>Revaluation reserve</b>				
At 1 January	31,146	32,165	31,146	32,165
Asset revaluation	54,769	-	54,769	-
Deferred tax on asset revaluation	(17,141)	-	(17,141)	-
Disposal of properties	-	(1,019)	-	(1,019)
<b>At 31 December</b>	68,774	31,146	68,774	31,146
<b>Capital reserve</b>				
At 1 January	635	635	635	635
<b>At 31 December</b>	635	635	635	635

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

24 Reserves and retained earnings (continued) <i>All amounts are expressed in K'000</i>	Group		Bank	
	2009	2008	2009	2008
<b>Options reserve</b>				
At 1 January	1,560	616	1,560	616
Movement during the year	(249)	944	(249)	944
<b>At 31 December</b>	<b>1,311</b>	<b>1,560</b>	<b>1,311</b>	<b>1,560</b>
<b>General reserve</b>				
At 1 January	2,875	2,875	2,875	2,875
<b>At 31 December</b>	<b>2,875</b>	<b>2,875</b>	<b>2,875</b>	<b>2,875</b>
<b>Exchange reserve</b>				
At 1 January	(4,348)	(982)	(294)	4
Movement during the year	(7,076)	(3,361)	(6,862)	(298)
<b>At 31 December</b>	<b>(11,424)</b>	<b>(4,348)</b>	<b>(7,156)</b>	<b>(294)</b>
<b>Retained earnings</b>				
At 1 January	394,367	264,855	394,461	264,434
Net profit for the year	257,118	228,334	257,738	226,779
Dividend paid	(100,305)	(99,509)	(100,305)	(99,509)
Deferred income prior year	2,732	2,757	(269)	2,757
Exchange reserve adjustments	-	959	-	-
NBSI Final dividend paid	-	(3,029)	-	-
<b>At 31 December</b>	<b>553,912</b>	<b>394,367</b>	<b>551,625</b>	<b>394,461</b>
<b>25 Contingent liabilities and commitments</b>				
<b>Off balance sheet financial instruments</b>				
Standby letters of credit	41,641	41,641	41,641	41,641
Guarantees and indemnities issued	(34,932)	222,777	(34,932)	222,777
Trade letters of credit	24,538	24,538	24,538	24,538
Commitments to extend credit	1,080,026	1,441,455	1,080,026	1,441,455
	<b>1,111,273</b>	<b>1,730,411</b>	<b>1,111,273</b>	<b>1,730,411</b>

### Legal Proceedings

A number of legal proceedings against the Bank and the Group were outstanding as at 31 December 2009. No provision has been made as existing management information and professional advice indicate that it is unlikely that any significant loss will arise. Based on information available at 31 December 2009, the Bank and the Group estimates a contingent liability of K65.689 million (2008: K1.534 million) in respect of these proceedings.

### Statutory deposits with the central bank

Cash reserve requirement - 3% of all amounts due to customers (2008: 3%)

### Commitments for capital expenditure

Amounts with firm commitments, and not reflected in the accounts

### Operating lease commitments

Not later than 1 year

Later than 1 year and not later than 5 years

Later than 5 years

360,799	171,726	265,419	171,726
7,145	8,417	7,145	8,417
7,991	5,604	7,991	5,604
60	120	60	120
92	184	92	184
<b>8,143</b>	<b>5,908</b>	<b>8,143</b>	<b>5,908</b>

**NOTES TO THE FINANCIAL STATEMENTS  
for the Year Ended 31 December 2009**

**26 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.

<i>All amounts are expressed in K'000</i>	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Cash and balances with Central Bank (note 11)	996,393	434,627	796,197	433,900
Due from other banks (note 13)	191,888	283,978	186,655	283,978
Due to other banks (note 19)	(26,594)	(11,416)	(12,202)	(11,416)
	<b>1,161,687</b>	<b>707,189</b>	<b>970,650</b>	<b>706,462</b>

**27 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 2009, balances and transactions of accounts for Directors were as follows:

<i>All amounts are expressed in K'000</i>	<b>2009</b>	<b>2008</b>
<b>Deposits</b>		
Opening balances	14,623	20,763
Net movement	7,135	(6,140)
Closing balance	<b>21,758</b>	<b>14,623</b>
Interest paid	3,365	116
<b>Loans and advances</b>		
Opening balances	29,262	21,764
Loans issued	48,399	15,169
Interest	580	588
Charges	5,065	118
Loan repayments	(17,511)	(8,377)
Closing balance	<b>65,795</b>	<b>29,262</b>

Incentive-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 2009, staff account balances were as follows:

<i>All amounts are expressed in K'000</i>	<b>2009</b>	<b>2008</b>
Housing loans	10,560	9,180
Other loans	10,503	9,497
	<b>21,063</b>	<b>18,677</b>
Cheque accounts	3,791	2,249
Foreign currency accounts	4	125
Savings accounts	2,725	2,089
	<b>6,520</b>	<b>4,463</b>

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

### 27 Related party transactions (continued)

#### Interests Register

The following are transactions recorded in the interests register:

Name	Nature of Interest	
N. N. Beangke	Director	Credit Corporation (Fiji) Ltd, New Guinea Islands Produce Ltd <sup>5</sup> , PNG Coffee Exports Ltd <sup>1,5</sup> , Credit Corporation (PNG) Ltd <sup>3</sup> , Boroma Ltd, Bank of South Pacific Ltd <sup>1</sup> , General Holdings Ltd <sup>5</sup> , Credit Corporation (SI) Ltd, BSP Capital Ltd <sup>1</sup> .
	Shareholder	Credit Corporation (PNG) Ltd <sup>5</sup> , New Guinea Islands Produce <sup>5</sup> , Boroma Ltd, Credit Corporation (Vanuatu).
T. E. Fox	Director	Kramer Group Ltd, Kramer Pacific Ltd <sup>5</sup> , Teyo No.1 Ltd <sup>5</sup> , Bank of South Pacific Ltd <sup>2</sup> , International Project Management Pty Ltd <sup>5</sup> , Capital Life Insurance Company Ltd, PNG Sustainable Infrastructure Ltd, BSP Capital Ltd
	Shareholder	Kramer Pacific Ltd, Teyo No.1 Ltd, Bank of South Pacific Ltd, International Project Management Pty Ltd, Citigold Corporation Ltd, Mining Projects Group, Marengo Gold Limited.
	Trustee/Member	Institute of National Affairs <sup>8</sup> , PNG Institute of Directors
I. B. Clyne	Director	Bank of South Pacific Ltd <sup>9</sup> , BSP Capital Ltd, Capital Life Insurance Company Ltd.
	Member	Commercial Bankers Association.
J. G. Jeffery	Director	National Superannuation Fund Ltd <sup>1,5</sup> , Employers Federation of PNG, Bank of South Pacific Ltd, Jayliss Ltd, City Pharmacy Ltd, Airlines PNG Ltd.
	Shareholder	Highlands Pacific Ltd, Oil Search Ltd, Jayliss Ltd <sup>1</sup> .
G. Aopi	Director	Oil Search Ltd <sup>7</sup> , Bank of South Pacific Ltd, Steamships Trading Co Ltd, POMSoX Ltd, Hirad Ltd, Marsh Ltd, Wahinemo Ltd, National Roads Authority, FM Morobe Ltd, CDI Foundation, Telikom PNG Ltd <sup>1</sup> , Kumuls Hotels Ltd, Independent Public Business Corporation <sup>1</sup> , BSP Capital Ltd.
	Shareholder	Oil Search Ltd <sup>7</sup> , Lihir Gold Ltd, Hirad Ltd, Wahinemo Ltd, Highlands Pacific Ltd, Melanesian Trustees (ICPNG), Bank of South Pacific Ltd.
	Member	Institute of National Affairs, Business Council of PNG, National Events Council.
Dr. I. Temu	Director	Bank of South Pacific Ltd, Tipi Enterprise Ltd, BSP Capital Ltd.
	Shareholder	Telstra Ltd.
	Employee	Barrick Gold Ltd.
	Committee member	Divine Word University.
Sir N. Bogan	Director	Bank of South Pacific Ltd, Nambawan Super Ltd <sup>1,5</sup> , Coprez Communications Ltd <sup>1</sup> , Coprez Holdings Ltd, Inventive Nook Ltd, James Cook Ltd, Niugini Cocoa Factory, In Touch Media Ltd <sup>1</sup> , Ahi Holdings Ltd.
	Shareholder	Coprez Holdings Ltd, Inventive Nook Ltd, James Cook Ltd, Niugini Cocoa Factory, In Touch Media Ltd
	Member	Evangelical Lutheran Church Finance Committee
C. C. Procter	Director	Bank of South Pacific Ltd, Sun Hung Kai Ltd, Quality Health Care Asia Ltd, BSP Capital Ltd.

**NOTES TO THE FINANCIAL STATEMENTS**  
for the Year Ended 31 December 2009

**27 Related party transactions (continued)**

**Interests Register**

The following are transactions recorded in the interests register:

Name	Nature of Interest	
J.K. Natto	Director	Bank of South Pacific Ltd, Petroleum Resources Kutubu Ltd <sup>1</sup> , Kutubu Security Services Ltd <sup>3</sup> , Welgris Fuel Distributors Ltd, Hekari Security Services Ltd, Hekari Properties Ltd, Namó'aporo Landowners Association Inc <sup>1</sup> , BSP Capital Ltd.
	Member	Australian Institute of Company Directors
K. Constantinou	Director	Bank of South Pacific Ltd, BSP Capital Ltd. Airways Hotel & Apartments Ltd, Lamana Hotel Ltd, Lamana Development Ltd, Hebou Constructions Ltd, Heritage Park Hotel Ltd, Gazelle International Hotel Ltd, Airlines PNG Ltd, Oil Search Ltd.
	Shareholder	Airways Hotel & Apartments Ltd, Lamana Hotel Ltd, Lamana Development Ltd, Hotel Technical Services Ltd, Heritage Park Hotel Ltd, C.G.A Properties, Fairhaven No.57 Ltd, Gazelle International Hotel, City Centre Development Ltd, Coastwatchers Court Ltd, Alotau International Hotel Ltd, Kimbe Bay Hotel Limited.
	Member	Australian Institute of Company Directors, PNG Institute of Directors

<sup>1</sup>Chairman, <sup>2</sup>Deputy Chairman, <sup>3</sup>Managing Director, <sup>4</sup>Executive Director, <sup>7</sup>General Manager, <sup>8</sup>Councillor,

<sup>5</sup>Company is shareholder of Bank of South Pacific Limited, or shareholder of company that is shareholder,

<sup>6</sup>Companies have banking facilities with BSP, <sup>9</sup>Chief Executive Officer.

**28 Directors' and executive remuneration**

Directors' remuneration

Directors of the Company received remuneration including benefits during 2009 as detailed below:

*All amounts are in K'000*

Name of Director	Meetings attended/ total held	Appointed/ (Resigned)	Base emolument	Total remuneration	
				2009	2008
N. N. Beangke	8/8		94,500	94,500	100,534
T. E. Fox	8/8		91,350	91,350	98,247
Dr. I. Temu	7/8		67,200	67,200	72,372
C. C. Procter	5/8		88,800	88,800	94,633
Sir N. Bogan	6/8		60,900	60,900	66,072
I. B Clyne*	8/8		-	-	-
J. G. Jeffery	8/8		79,800	79,800	86,697
G. Aopi	7/8		70,350	70,350	75,522
K. Constantinou	6/6	22/04/09	60,900	60,900	-
V. Reva	2/2	(22/04/09)	70,350	70,350	76,384
J. K. Natto	5/8		60,900	60,900	65,210

Directors Gereia Aopi and John Kapi Natto 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 the 22<sup>nd</sup> May 2009 Annual General Meeting.



## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

### 28 Directors' and executive remuneration (continued)

Vai Reva resigned in April 2009 and the Board appointed Kostas Constantinou on 22 April 2009.

Bank of Papua New Guinea deemed Mr Constantinou a Fit & Proper Person in accordance with the Prudential Standards and the provisions of the Banks & Financial Institutions Act 2000. Mr Constantinou's appointment was confirmed by the shareholders on the 22<sup>nd</sup> May 2009 Annual General Meeting.

Non Executive Board Members of the Board – Beangke, Fox, Temu, Procter, Constantinou, Aopi and Kapi Natto will receive an allowance of K46,324 as Board of Directors of BSP Capital Ltd which forms part of the Group.

\*Managing Director/Chief Executive Officer receives no fees for his services as Director during the year.

#### 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	2009 No.	2008 No.	Remuneration K'000	2009 No.	2008 No.	Remuneration K'000	2009 No.	2008 No.
100-110	12	3	310-320	1	-	490-500	1	-
110-120	3	5	320-330	1	1	500-510	1	1
120-130	3	2	330-340	3	-	510-520	-	-
130-140	3	2	340-350	1	1	530-540	1	-
140-150	9	2	350-360	-	2	540-550	-	-
150-160	4	2	360-370	-	1	560-570	2	-
160-170	1	3	370-380	1	1	570-590	-	-
180-190	4	-	380-390	2	5	590-670	1	-
190-200	1	-	390-400	1	1	670-700	1	-
210-220	2	-	400-410	1	1	750-790	-	1
220-240	-	-	410-420	2	1	790-800	-	-
240-250	-	-	420-430	3	3	810-830	1	1
250-260	1	-	430-440	-	-	830-850	1	-
260-269	-	-	440-450	2	-	850-860	-	-
270-280	-	-	450-460	3	1	920-930	1	1
280-290	-	-	460-470	1	1	930-1,020	2	2
290-300	-	-	470-480	2	-	1,220-1,260	-	2
300-310	-	-	480-490	-	-	1,540-2,230	1	1
Total							80	47

Executives' remuneration stated includes exercised options (refer to Note 23).

The specified executives during the year were:

Ian B Clyne	Robin Fleming	Hans Abma
Johnson Kalo	Peter Dixon	Frans Kootte
Kevin McCarthy	Lew Kenah	
Aho Baliki	Giau Duruba	

**NOTES TO THE FINANCIAL STATEMENTS**  
for the Year Ended 31 December 2009

**28 Directors' and executive remuneration (continued)**

**Specified executives remuneration in aggregate (K'000)**

	Primary			Post-employment			Other		Total
	Salary	Bonus	Non-monetary	Super	Pre-scribed benefits	Other	Equity options	Other benefits	
<b>2009</b>	4,778	1,539	100	130	-	-	-	133	6,680
<b>2008</b>	4,711	1,725	80	301	-	-	3,034	526	10,377

**29 Reconciliation of operating cash flow**

All amounts are expressed in K'000

	Group		Bank	
	2009	2008	2009	2008
<b>Reconciliation of operating profit/(loss) after tax to operating cash flow before changes in operating assets</b>				
Operating profit/(loss) after tax	257,118	228,334	257,738	226,779
Add: Tax expense	121,025	100,464	120,226	100,045
Operating profit before income tax	378,143	328,798	377,964	326,824
<b>Major non cash amounts</b>				
Depreciation	37,371	26,493	36,556	26,363
Amortisation of deferred acquisition and computer development costs	1,684	(696)	1,684	(696)
Net (profit)/loss on sale of fixed assets	(1,184)	6,665	(1,184)	6,665
Gain on property revaluation	(2,372)	-	(2,372)	-
Sundry write off	32,372	(159)	32,372	1,815
CDO buy-back provision	-	50,000	-	50,000
Movement in forex income accrual	(3,135)	(5,504)	(3,135)	(5,504)
Movement in provision for doubtful debts	(16,645)	(5,017)	(16,376)	(4,748)
Movement in payroll provisions	(5,345)	(615)	(5,232)	(502)
Net effect on other accruals	(30,295)	(14,265)	(10,764)	(9,439)
<b>Operating cash flow before changes in operating assets</b>	<b>390,594</b>	<b>385,700</b>	<b>409,513</b>	<b>390,778</b>

**30 Earnings per share**

Basic earning per share is 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 share equals diluted earnings per share.

	2009	2008	2009	2008
Net Profit attributable to shareholders (K'000)	257,118	228,334	257,738	226,779
Weighted average number of ordinary shares on issue ('000)	4,559,328	4,559,328	4,559,328	4,559,328
Basic and diluted earning /(loss) per share (expressed in toea)	5.6	5.0	5.7	4.9

**31 Segment information**

Bank of South Pacific Limited and the Group comprises two segments, this being the provision of banking services and products and stock broking services. For management purposes, segment information determination is based on the risks involved with the provision of core banking services and products and the Bank and Group's management reporting system. The four main divisions for management purposes are core banking services of Retail Bank, Paramount Banking, Corporate & International and Others non core banking (stock broking, rentals and other non-core banking activities). The Bank of South Pacific Limited and Group's business segments operate in Papua New Guinea and has branches in Niue, Fiji and Solomon Islands. Inter segment adjustments reflects elimination entries in respect of inter segment income and expense allocations including funds transfer pricing.

## NOTES TO THE FINANCIAL STATEMENTS for the Year Ended 31 December 2009

### 31 Segment Information (continued)

All amounts are expressed in K'000

Analysis by business segments:

#### Year ended 31 December 2009

	Retail	Paramount	Corporate & International	Others	Colonial entities	Adjust Inter Segment	Total
<b>Revenue</b>	232,837	183,415	510,863	4,288	22,456	(229,796)	724,063
<b>Costs</b>	(247,493)	(9,442)	(57,124)	(7,012)	(19,553)	(5,296)	(345,920)
<b>Operating results</b>	(14,656)	173,973	453,739	(2,724)	2,903	(235,092)	378,143
<b>Income tax expense</b>							(121,025)
<b>Profit after tax</b>							<b>257,118</b>

#### Year ended 31 December 2008

	Retail	Paramount	Corporate & International	Others	Colonial entities	Adjust Inter Segment	Total
<b>Revenue</b>	178,075	101,587	460,994	7,519	-	(127,247)	620,928
<b>Costs</b>	(218,486)	(9,378)	(51,199)	(56,723)	-	43,656	(292,130)
<b>Operating results</b>	(40,411)	92,209	409,795	(49,204)	-	(83,591)	328,798
<b>Income tax expense</b>							(100,464)
<b>Profit after tax</b>							<b>228,334</b>

### 32 Events occurring after balance sheet date

In March 2010, BSP announced an issue of Mandatorily Convertible Notes to Sophisticated Investors in Fiji, through its Fiji subsidiary BSP Convertible Notes Limited. The issue is in line with BSP Group's overall capital management strategy, which includes capital support of the Group's growth in the Pacific region.

The notes are classed as debt and carry a coupon interest rate of 7% per annum, paid six-monthly, and a term of three years, after which they are mandatorily converted to shares in BSP Convertible Notes Limited (Fiji Class Shares). These shares will be treated as equity and receive a dividend stream equivalent to BSP ordinary shares. BSP will make application to have the Convertible Notes, and on conversion the Fiji Class Shares, listed on the South Pacific Stock Exchange.

**Deloitte Touche Tohmatsu**

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## INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF BANK OF SOUTH PACIFIC LIMITED AND ITS SUBSIDIARIES

We have audited the accompanying consolidated financial statements of Bank of South Pacific Limited and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December 2009, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### Management's Responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with the Companies Act 1997 and International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### 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 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 and fair presentation of the consolidated financial statements 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 have obtained all required information and explanations, and believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Audit Opinion

In our opinion,

- a) the consolidated financial statements give a true and fair view of the financial position of Bank of South Pacific limited and its subsidiaries as at 31 December 2009, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards; and comply with the Company's Act 1997.
- b) proper accounting records have been kept by the company.

### Other Information

We do not provide any other services to Bank of South Pacific Limited and its subsidiaries.

Port Moresby, this 16<sup>th</sup> day of March 2010.

*Deloitte Touche Tohmatsu*  
DELOITTE TOUCHE TOHMATSU

*Suzaan Theron*  
By: Suzaan Theron

Partner

Registered under the Accountants Act 1996

### for the year ended 31 December Shareholder information

The following is a summary of pertinent issues relating to a shareholding in the Company. The Constitution of BSP may be inspected during normal business at the Registered Office.

#### Rights attaching to ordinary shares

The rights attaching to shares are set out in Bank of South Pacific Limited's Constitution and in certain circumstances, are regulated by the Companies Act 1997, the POMS0X Listing Rules and general law.

There is only one class of share. All shares have equal rights.

Other rights attached to ordinary shares include:

**(a) General meeting and notices**

Each member is entitled to receive notice of, and to attend and vote at, general meetings of BSP and to receive all notices, accounts and other documents required to be sent to members under BSP's constitution, the Companies Act or the Listing Rules.

**(b) Voting rights**

At a general meeting of shareholders every holder of fully paid ordinary shares present in person or by an attorney, representative or proxy has one vote on a show of hands (unless a member has appointed two proxies) and one vote per share on a poll.

A person who holds a share which is not fully paid is entitled, on a poll, to a fraction of a vote equal to the proportion which the amount paid bears to the total issue price of the share.

Where there are two or more joint holders of a share and more than one of them is present at a meeting and tenders a vote in respect of the share, the Company will count only the vote cast by the member whose name appears first in BSP's register of members.

**(c) Issues of further shares**

The Directors may, on behalf of BSP, issue, grant options over or otherwise dispose of unissued shares to any person on the terms, with the rights, and at the times that the Directors decide. However, the Directors must act in accordance with the restrictions imposed by BSP's constitution, the POMS0X Listing Rules, the Companies Act and any rights for the time being attached to the shares in any special class of those shares.

**(d) Variation of rights**

Unless otherwise provided by BSP's constitution or by the terms of issue of a class of shares, the rights attached to the shares in any class of shares may be varied or cancelled only with the written consent of the holders of at least three-quarters of the issued shares of that class, or by special resolution passed at a separate meeting of the holders of the issued shares of the affected class.

**(e) Transfer of shares**

Subject to BSP's constitution, the Companies Act and the POMS0X Listing Rules, ordinary shares are freely transferable. The shares may be transferred by a proper transfer effected in accordance with the POMS0X Business Rules, by any other method of transferring or dealing with shares introduced by POMS0X and as otherwise permitted by the Companies Act or by a written instrument of transfer in any usual form or in any other form approved by either the Directors or POMS0X that is permitted by the Companies Act.

The Directors may decline to register a transfer of shares (other than a proper transfer in accordance with the POMS0X Business Rules) where permitted to do so under the POMS0X Listing Rules or the transfer would be in contravention of the law. If the Directors decline to register a transfer, BSP must give notice in accordance with the Companies Act and the POMS0X Listing rules, give the party lodging the transfer written notice of the refusal and the reason for refusal. The Directors must decline to register a transfer of shares when required by law, by the POMS0X Listing Rules or by the POMS0X Business Rules.

**(f) Partly paid shares**

The Directors may, subject to compliance with BSP's constitution, the Companies Act and the POMS0X Listing Rules, issue partly paid shares upon which there are outstanding amounts payable. These shares will have limited rights to vote and to receive dividends.

**(g) Dividends**

The Directors may from time to time determine dividends to be distributed to members according to their rights and interests. The Directors may fix the time for distribution and the methods of distribution. Subject to the terms of issue of shares, each share in a class of shares in respect of which a dividend has been declared will share in the dividend equally.

Each share carries the right to participate in the dividend in the same proportion that the amount for the time being paid on the share (excluding any amount paid in advance of calls) bears to the total issue price of the share.

Dividend payouts over the last seven years are disclosed in the schedule of Historical Financial Performance elsewhere in this Annual Report.

**(h) Liquidation**

Subject to the terms of issue of shares, upon liquidation assets will be distributed such that the amount distributed to a shareholder in respect of each share is equal. If there are insufficient assets to repay the paid up capital, the amount distributed is to be proportional to the amount paid up.

**(i) Directors**

BSP's constitution states that the minimum number of directors is three and the maximum is ten.

**(j) Appointment of directors**

Directors are elected by the shareholders in general meeting for a term of three years. At each general meeting, one third of the number of directors (or if that number is not a whole number, the next lowest whole number) retire by rotation. The Board has the power to fill casual vacancies on the Board, but a director so appointed must retire at the next annual meeting.

**(k) Powers of the Board**

Except as otherwise required by the Companies Act, any other law, the POMSx Listing Rules or BSP's constitution, the Directors have power to manage the business of BSP and may exercise every right, power or capacity of BSP to the exclusion of the members.

**(l) Share buy backs**

Subject to the provisions of the Companies Act and the POMSx Listing Rules, BSP may buy back shares in itself on terms and at times determined by the Directors.

**(m) Officers' indemnities**

BSP, to the extent permitted by law, indemnifies every officer of BSP (and may indemnify any auditor of BSP) against any liability incurred by the person, in the relevant capacity, to another person unless the liability arises out of conduct involving lack of good faith.

BSP may also make a payment in relation to legal costs incurred by these persons in defending an action for a liability, or resisting or responding to actions taken by a government agency or a liquidator.

## SHAREHOLDER INFORMATION

### Twenty largest registered fully paid ordinary shareholders

At the 31 December 2009, the twenty largest registered fully paid shareholders of the Company were:

	Shares Held	%
1. Independent Public Business Corporation	1,071,082,400	23.49
2. Nominees Niugini Limited	530,105,100	11.63
3. Nambawan Super Limited	478,117,344	10.49
4. Petroleum Resources Kutubu Limited	461,538,400	10.12
5. Credit Corporation (PNG) Limited	384,141,375	8.43
6. National Superannuation Fund Limited	325,051,165	7.13
7. PNG Sustainable Development	293,027,664	6.43
8. Teachers Savings and Loans Society Limited	182,783,400	4.01
9. Comrade Trustee Services Limited	155,747,742	3.42
10. Tropicana Limited	49,836,525	1.09
11. Lamin Trust Fund	35,181,316	0.77
12. Credit Corporation (PNG) Ltd (CC Finance Ltd A/C)	30,000,000	0.66
13. Solomon Islands National Provident Fund Board	29,445,550	0.65
14. Catholic Diocese of Kundiawa	21,656,880	0.48
15. Mineral Resources OK Tedi No.2	21,000,000	0.46
16. Southern Highlands Provincial Government	20,000,000	0.44
17. Society of Divine Word	19,424,725	0.43
18. PNG Power Staff Savings and Loan Society Limited	15,951,140	0.35
19. Mineral Resources Star Mountains Ltd	12,428,571	0.27
20. Petroleum Resources Gobe Limited	12,383,021	0.27
Other shareholders	410,426,431	8.98
	4,559,328,749	100.00

### Distribution of shareholdings

At the 31 December 2009, the Company had 6,767 shareholders. The distribution of shareholdings is as follows:

Range (number)	Number of Shareholders	Number of Shares
1 - 1,000	1,184	899,789
1,001 - 5,000	3,566	8,002,148
5,001 - 10,000	808	5,993,558
10,001 - 100,000	932	25,087,800
100,001 and above	277	4,519,345,454
	<u>6,767</u>	<u>4,559,328,749</u>

### Dividend reinvestment scheme

The Company has a dividend reinvestment scheme. It was not implemented in 2009.

### Employee share scheme

The Company resolved on 27 May 2004 that a maximum of 1% of the total number of shares held in the Company may be allocated to employees each year at the discretion of the Board.

### Interest in shares in the Bank

Directors hold the following shares in the Bank:

Director	Shares Held	%
T. E. Fox	5,080,581	0.11
Gerea Aopi	100,000	0.00

N. Beangke holds an indirect shareholding of 8,000,000 in the Company through a family trust, General Holdings Limited. This indirect shareholding represents 0.17% of the Company's issued capital.

Registered Office	Share Registry	Website
Bank of South Pacific Limited PO Box 78, PORT MORESBY National Capital District PAPUA NEW GUINEA Telephone: +675 322 9700	PNG Registries Limited PO Box 1265, PORT MORESBY National Capital District PAPUA NEW GUINEA Telephone: +675 321 6377	<a href="http://www.bsp.com.pg">www.bsp.com.pg</a>

SENIOR MANAGEMENT

Chief Executive Officer  
Ian B Clyne

General Manager Retail Bank  
Frans Kootte

Deputy CEO and  
General Manager Credit and Risk  
Robin Fleming

General Manager Corporate and International  
Peter Dixon

General Manager Paramount Banking  
Aho Baliki

General Manager Human Resources  
Giau Duruba

Chief Operating Officer  
Hans Abma

Deputy CEO and  
Chief Financial Officer  
Johnson Kalo



## BRANCH NETWORK

BRANCHES	PHONE NUMBERS	BRANCHES	PHONE NUMBERS
<b>AITAPE (PNG)</b> Branch Manager Joe Makinta	(675) 457 2042	<b>LAE COMMERCIAL (PNG)</b> Branch Manager Agnes Mark	(675) 473 9808
<b>ALOTAU (PNG)</b> Branch Manager Stanley Bole	(675) 641 1284	<b>LAE MARKET (PNG)</b> Branch Manager Darius Manjali	(675) 473 9606
<b>BIALLA (PNG)</b> Branch Manager Marco Hamen	(675) 983 1095	<b>LAE OPERATIONS CENTRE (PNG)</b> Branch Manager Eileen Goviro	(675) 473 9866
<b>BOROKO (PNG)</b> Branch Manager Anne Baniyamai	(675) 323 2288	<b>LIHIR (PNG)</b> Branch Manager Bobby Aeron	(675) 986 4052
<b>BUKA (PNG)</b> Branch Manager Benjamin Kiwai	(675) 973 9042	<b>LORENGAU (PNG)</b> Branch Manager Karen George	(675) 970 9050
<b>BULOLO (PNG)</b> Branch Manager Jacinta McKinnon	(675) 474 5366	<b>MADANG (PNG)</b> Branch Manager Cecilia Pasum	(675) 422 2477
<b>COMMERCIAL CENTRE (PNG)</b> Manager Operations Madeleine Topelemu	(675) 325 5999	<b>MAPRIK (PNG)</b> Branch Manager Annette Poka	(675) 458 1317
<b>DARU (PNG)</b> Branch Manager Ivy David	(675) 645 9062	<b>MENDI (PNG)</b> Branch Manager David Wasape	(675) 549 1070
<b>DOUGLAS STREET (PNG)</b> Branch Manager Wesley Hosea	(675) 321 2444	<b>MORO (PNG)</b> Branch Manager Peter Tikot	(675) 275 5808
<b>GOROKA (PNG)</b> Branch Manager Maria Kipau	(675) 532 1633	<b>MT HAGEN (PNG)</b> Branch Manager Alex Kuna	(675) 542 1877
<b>KAINANTU (PNG)</b> Branch Manager Agnes Veata	(675) 537 1065	<b>POPONDETTA (PNG)</b> Branch Manager Joe Ururu	(675) 629 7171
<b>KAVIENG (PNG)</b> Branch Manager Maureen Wanu	(675) 984 2066	<b>PORT MORESBY (PNG)</b> Branch Manager Stenard Wai	(675) 322 9790
<b>KIMBE (PNG)</b> Branch Manager Misbil Alfred	(675) 983 5166	<b>RABAU (PNG)</b> Branch Manager Ben Umba	(675) 982 1744
<b>KIUNGA (PNG)</b> Branch Manager Norman Aser	(675) 649 1073	<b>TABUBIL (PNG)</b> Branch Manager Tony Waningu	(675) 649 9179
<b>KOKOPO (PNG)</b> Branch Manager Albert Burua	(675) 982 9088	<b>VANIMO (PNG)</b> Branch Manager Josephine Komoru	(675) 457 1209
<b>KUNDIAWA (PNG)</b> Branch Manager Albert Seri	(675) 535 1025	<b>WABAG (PNG)</b> Branch Manager Cecilia Raepa	(675) 547 1176
<b>LAE (PNG)</b> Branch Manager Mary Kundi	(675) 473 9801	<b>WAIGANI BANKING CENTRE (PNG)</b> Branch Manager Leslie Wagiam	(675) 300 9600

BRANCHES	PHONE NUMBERS	BRANCHES	PHONE NUMBERS
<b>WAIGANI DRIVE (PNG)</b> Branch Manager Mathias Manowo	(675) 325 6788	<b>BA (Fiji)</b> Branch Manager Salim Buksh	(679) 667 4599
<b>WEWAK (PNG)</b> Branch Manager Magai Kavailon	(675) 456 2344	<b>RAKIRAKI (Fiji)</b> Branch Manager Anand Nair	(679) 669 4200
<b>FIJI (Fiji)</b> Country Head Kevin McCarthy	(679) 323 4867	<b>TAVUA (Fiji)</b> Branch Manager Tina Lilo	(679) 668 1507
<b>SUVA (Fiji)</b> Branch Manager Susie Fesaitu	(679) 330 4011	<b>LABASA (Fiji)</b> Branch Manager Sera Petueli	(679) 881 1888
<b>TOP TOWN NADI (Fiji)</b> Branch Manager Curtis Mar	(679) 670 5111	<b>SAVUSAVU (Fiji)</b> Relieving Branch Manager Praveen Chand	(679) 885 0199
<b>PACIFIC HOUSE (Fiji)</b> Branch Manager Viliame Varasikete	(679) 321 4580	<b>TAVEUNI (Fiji)</b> Branch Manager Ropate Toroca	(679) 888 0433
<b>SUVA - CENTRAL (Fiji)</b> Branch Manager Mohammed Arif	(679) 321 4455	<b>NIUE (Niue)</b> Country Head Cathy Pataturana	(683) 4220
<b>DOMINION HOUSE (Fiji)</b> Branch Manager Jennifer Morris	(679) 321 4672	<b>SOLOMON ISLANDS (SI)</b> Country Head Mark Corcoran	(677) 21874
<b>SAMABULA (Fiji)</b> Branch Manager Sefanaia Qalilawa	(679) 338 7999	<b>HONIARA (SI)</b> Branch Manager Michael Kahamana	(677) 21874
<b>CENTREPOINT (Fiji)</b> Branch Manager Viviana Veisaca	(679) 334 2333	<b>POINT CRUZ (SI)</b> Branch Manager Joy Vave	(677) 21874
<b>NAUSORI (Fiji)</b> Branch Manager Rajesh Chand	(679) 347 8499	<b>RANADI (SI)</b> Branch Manager Rose Funa	(677) 39403
<b>PACIFIC HARBOUR (Fiji)</b> Branch Manager Manjila Goundar	(679) 345 2030	<b>AUKI (SI)</b> Branch Manager Samuel Misi	(677) 40199
<b>LEVUKA (Fiji)</b> Officer In Charge Naomi Waqa	(679) 344 0300	<b>GIZO (SI)</b> Branch Manager Rose Abana	(677) 60539
<b>LAUTOKA (Fiji)</b> Branch Manager Josefa Tuitubou	(679) 666 2466	<b>NORO (SI)</b> Branch Manager Clotilda Londeka	(677) 61008
<b>NADI (Fiji)</b> Branch Manager Ann Pesamino	(679) 670 0988	<b>MUNDA (SI)</b> Branch Manager Rebecca Hickie	(677) 61177
<b>NAMAKA (Fiji)</b> Branch Manager Madhur Kumar	(679) 672 8950		
<b>SIGATOKA (Fiji)</b> Relieving Branch Manager Kelera Kamikamica	(679) 650 0900		







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