

# 2004

## annual report



## The Fund

The Defence Force Retirement Benefits Fund (DFRBF) is established by an Act of Parliament with the primary objective of providing benefits to members of the Defence Force on retirement and to their families in the event of death and for related purposes.

Unlike other fund operating in the country, DFRBF is a defined benefits fund. This means that benefits are usually determined by a formula provided in the enabling legislation and paid at retirement from the Defence Force after qualifying for pension.

Since members benefits are determined by a formula, rather than reflecting what is in the members' individual accounts, the funds held in a defined benefits fund is normally kept as a single pool for members.

Members are required to compulsorily contribute 6% of their salary to the fund. The employer or State share is not paid each fortnight as in the case of an accumulation fund. Instead the State assumes all residual pension liability after allowing for member contribution, investment income and expenses of administering the fund.

Because of the uncertainties of the extent of residual liability assumed by the State, an actuarial evaluation is undertaken every three (3) years. The last actuarial evaluation was undertaken in May 2005 covering the three (3) year period ended on 31st December 2004, which reported that the fund was in a sound financial state. The next actuarial evaluation will be undertaken in 2008 to cover the period ended on 31st December 2007.



## Chairman's Statement

Dear Members,

It gives me great pleasure to present the 2004 Annual Report of the Defence Force Retirement Benefits Fund which also contains the audited Financial Statements for the year ended 31st December 2004.

This represents my second report to members in fulfillment of the trustee's reporting obligation pursuant to the Superannuation (General Provisions) Act 2000.

The superannuation reforms which began with the enactment by Parliament of the Superannuation Act 2000 has resulted in the unprecedented growth of the superannuation industry. The Governor of the Bank of Papua New Guinea recently reported that total superannuation fund assets have grown to over K1.5 billion by September 2004 and the industry's growth is forecast to surpass all others in the banking and finance sector within a few years time.

Your Fund has benefited from these reforms which are reflected in the continued growth in both profitability and size.

The Fund recorded a gross operating income of K22,626,115 (investment income K21,219,517 and contributions K1,871,445) and net profit after tax of K10,534,283 which underpinned the continued growth of the Fund from K101.6 million in 2003 to K112.2 million as at 31st December 2004. This represents a growth rate of 10%.

Income from interest and dividends continued to be the mainstay of the Fund's revenue source, however the biggest improvement was attributable to capital gains amounting to K10,773,204 for the period under consideration. This is the result of enhanced scrutiny and prudential supervision by the Bank of Papua New Guinea of the Fund's investment



activities and a diligent and professional approach to investment of Fund assets by the trustee. Income from contributions continued its decline during the year as the retrenchment exercise took its toll but is anticipated to stabilize when the Defence Force is "right-sized".

Overall, greater financial discipline was exercised by the trustee that saw a reduction in all operational expenditure with the exception of expenditure relating to the write-down in the value of the Fund's 70% ownership of land in Hunter Limited erroneously taken up at 100% and benefit payments which continued to be a major expenditure but saw a marked reduction from prior year as the retrenchment exercise winds down.

All the achievements that I have enumerated earlier could not have happened without the commitment, hard work and determination of the Trustees, management and staff, fund administrator, investment manager, legal and business advisors and all other persons whose individual and collective efforts contributed towards the realization of our corporate objectives.

Finally, I take this opportunity to extend my gratitude to the officers of the Bank of Papua New Guinea and the Department of Finance and Treasury for their assistance and guidance throughout the year.

Thank you.

A handwritten signature in black ink, appearing to read 'Chris Alu', written over a faint circular stamp.

Chris Alu  
Chairman

22 April 2005



## Board of Trustees



*(Standing left to right) – K. Posman, J. Kalo, B. Hull, Col R. Renagi, OBE (Rtd), Col D. Takendu, OBE (Rtd)*  
*(Seated left to right) Capt Tom Ur, C. Alu.*

### **Chris Alu – Chairman Independent Director**

Appointed to the Board of DFRBF (predecessor to Comrade Trustee Services Limited) as Chairman in June 2000 and served in that position until 31st December 2002, when the Board ceased to exist by operation of the Superannuation Act 2000. He was subsequently appointed to the Board upon the formation of CTSL as licensed corporate trustee to the Fund on 19th December 2002.

Mr. Alu presided over the Board that successfully managed the transition to full compliance with the requirements of the Superannuation Act 2000, and upon the formation of Comrade Trustee Services Limited as trustee to DFRBF was elected Chairman in January 2003 and occupies that position to the present time.

Mr. Alu has 23 years of extensive private and public sector experience and brings with him invaluable accounting experience to the Board.

Mr. Alu graduated with a degree in accounting from the PNG University of Technology in 1981 and holds a Certificate in Commercial Audits from the Darling Downs Institute of Advanced Education, Queensland, Australia.

He is also Chairman of Unitech Development & Consultancy Limited – the business arm of the University of Technology, a member of Council of the University of Technology and President of the Fellowship of Companies for Christ International, PNG Chapter. He is also involved with many charity groups and considers this as his contribution towards the less fortunate in society.

Mr. Alu is a member of the PNG Institute of Directors and was appointed pursuant to Clause 10 of the Company Constitution as an independent director.



**Colonel David L.Y. Takendu, OBE, BE (Civil), psc (Aust), psc (Indon), jssc (Aust) (Rtd.)**

Appointed to the Board of DFRBF (predecessor to Comrade Trustee Services Limited) as Deputy Chairman in June 2000 and served in that position until 31st December 2002, when the Board ceased to exist by operation of the Superannuation Act 2000. He was subsequently appointed to the Board upon the formation of CTSL as the licensed corporate trustee to the Fund on 19th December 2002.

He was a member of the Change Management Committee that was instrumental in managing the transition to full compliance with the requirements of the Superannuation Act 2000.

Col Takendu joined the Australian Army, Papua New Guinea Command, in 1968 as an officer cadet and worked his way up to the rank of Colonel and held the position of Chief of Staff at the time of retirement in December 2002. He represents pensioners on the Fund Board.

He previously served on the Post and Telecommunications Board from 1990 to 1993 and more recently served as Chairman of Banora Trading Limited.

Colonel Takendu graduated from the PNG University of Technology in 1978 with a degree in Civil Engineering. During the course of his employment with the Defence Force he has also attended military staff colleges in Australia, New Zealand, Indonesia and United States notably, the Australian Staff College, Queenscliffe, Victoria, in 1981, the Indonesian Military Staff College, Bandung, between 1986 and 1987, the JFK School of Government, Harvard University, Boston, Mass, USA in International Conflict Resolution Strategies, 2001 and Defence Resources Management Institute, at the US Naval Post Graduate School, Monterrey, California, USA in 1991. He speaks Bahasa Indonesia fluently.

He is a member of the PNG Institute of Directors.





**Captain (Navy) Reginald Renagi, OBE, psc, jssc (Aust), (Rtd.)**

Appointed to the Board of DFRBF (predecessor to Comrade Trustee Services Limited) in 1994 and retained that position until 31st December 2002, when the Board ceased to exist by operation of the Superannuation Act 2000. He was subsequently appointed to the CTSB Board on 19th December 2002. Captain Renagi has earned the distinction of being the longest serving member on the Board.

He was the Chairman of the Change Management Committee that presided over and was instrumental in managing the transition to full compliance with the requirements of the Superannuation Act 2000.

Captain Renagi joined the Papua New Guinea Division of the Royal Australian Navy in December 1971 as a cadet midshipman, graduated and was commissioned in Australia. He progressed to the rank of Captain (Navy), or Colonel equivalent at time of retirement from the Defence Force.

Captain Renagi has held several sea commands and commanded naval shore establishments during the 1970's and 80's. Key staff appointments during his period of service were; Acting Chief of Operations, Chief of Personnel, Chief of Plans, Manager Commercial Support Program and Acting Chief of Staff. During his military career, he has also attended senior staff colleges in Australia and the United States notably, the Australian Army Command and Staff College, Queenscliffe, Victoria, in 1980, and Defence Resources Management Institute, at the US Naval Post Graduate School, Monterey, California, USA in 1992, and the following senior executive programs: the Australian Defence Force Academy Canberra, ACT, Australia in 1995, the JFK School of Government, Harvard University, Boston, Mass, USA in International Conflict Resolution Strategies in 2000 and the Asia-Pacific Centre for Security Studies, Honolulu, Hawaii, USA.

He also serves as a Director on the Boards of the following subsidiaries - Hunter Limited, Pacific Capital Limited and Banora Trading Limited.

He represents members of the fund on the Board and is a member of the PNG Institute of Directors.



**Captain Alois Tom Ur, MBE (Navy)**

Appointed to the Board on 19th December 2002, Captain Tom Ur represents members of the Fund on the Board.

Captain Tom Ur was appointed Chief of Staff in July 2002 and has occupied that position in the Defence Force to the present time. His primary role is to provide logistical and management support to the Commander of the PNG Defence Force.

Currently he is a member of the Defence Force Supplies and Tenders Board and Chairman of the Disciplined Forces Housing Committee.

Captain Tom Ur has had considerable hands on experience in all facets of naval duties including attachments in the United States and Australian navies.

Captain Tom Ur is a graduate of the University of PNG with a Bachelor of Commerce (Accounting) degree, a graduate Diploma in Strategic Studies and a visiting Fellow to the Royal Australian Navy's Maritime Studies Program at the Joint Services Staff College in Canberra. He is a member of the PNG Institute of Directors.



**Johnson Kalo**  
**Independent Director**

Appointed to the Board on 7th July 2003, he is a nominee of the Bankers Association pursuant to Clause 10 of the Company Constitution. Mr. Kalo holds a degree in accounting from the PNG University of PNG.

Since his graduation in 1988, Mr. Kalo has had extensive working experience in all facets of accounting and auditing having worked with KPMG for 7 years ascending to the position of Assistant Manager at the time of leaving to take up the position of Internal Auditor with Motor Vehicles Insurance Limited in 1995. Upon the creation of Finance Pacific Limited, which eventually assumed control of MVIL and PNGBC, Mr. Kalo continued to perform accounting and auditing functions. In 2000, Mr. Kalo was appointed as Senior Accountant within the Financial Analysis Unit of the PNGBC and with the subsequent sale and merger of the bank in 2002 with Bank of South Pacific Mr. Kalo was retained as Senior Accountant and his duties expended to include new accounting and reporting challenges brought about by the merger of the two banks in the areas of integration and financial systems.

Mr. Kalo brings to the Board not only his accounting expertise but the added benefit of a banker's perspective to Board deliberations which will enhance corporate governance.

Mr. Kalo is an Associate Member of the PNG CPA and a member of the PNG Institute of Directors.



**Brian Hull**  
**Independent Director**

Appointed to the Board on 7th July 2003, as nominee of the PNG Institute of Directors pursuant to Clause 10 of the Comrade Trustees Services Limited Constitution.

Brian Hull served on the Board of Bank of Papua New Guinea from October 1986 thru to December 2000. Apart from Sir Henry ToRobert, Brian was the longest serving member of this board.

As Executive Chairman he founded Eda Ranu in 1996 and served in this capacity till 1988.

Currently Brian Hull is the Executive Chairman of Century 21 Siule Real Estate and



his extensive experience in the real estate and property industry benefits the fund significantly. This is in addition to his contribution to enhancing and strengthening corporate governance.

Brian Hull holds a Diploma from the Australian School of Pacific Administration, attended the University of Papua New Guinea and has completed various business related courses in Australia, New Zealand, Singapore, USA and Papua New Guinea. In April this year Brian participated in the inaugural "International Company Directors Course" staged by the Australian Institute of Company Directors in Sydney, Australia.

Brian Hull is presently a Fellow of the Australian Institute of Company Directors, a Founding Member of PNG Institute of Directors and a Founding Member of the Real Estate Agents Association.



**Kisikiu Posman**  
**Independent Director**

Appointed to the Board on 4th June 2004 he was nominated by the PNG Law Society pursuant to Clause 10 of the Company Constitution.

Mr. Posman graduated from the University of PNG in 1983 with a Bachelor of Law and also graduated with a Master of Law degree from the University of Ottawa, Canada in 1986.

Mr. Posman has had a varied employment history having commenced employment with Bougainville Copper Limited in 1974, then to teaching law at the University of PNG between 1983 and 1989 then to private practice. His stint in private practice started with Warner Shand Lawyers, then with Mallesons Stephen Jaques at their Sydney office for two years then with Carter Newell Lawyers in Port Moresby for a further three years.

In 1993, he left Carter Newell Lawyers to start the law firm Fiocco Posman Kua Lawyers in partnership with Messrs Rio Fiocco and Kerenga Kua. The firm has undergone significant changes since then having merged with Tharwell Aisi Lawyers and is now one of the largest national legal firms. Mr. Posman is the managing partner of the firm.

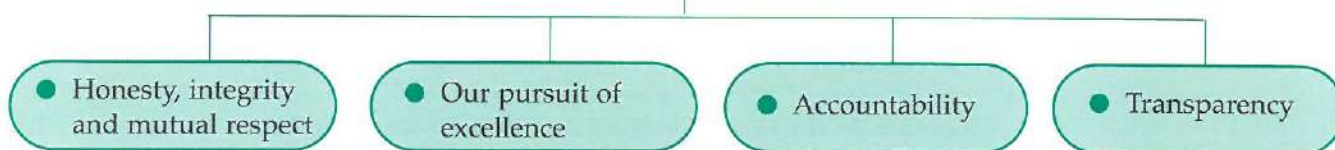
In addition to his legal background, Mr. Posman has had some prior commercial experience having served on the Boards of the Investment Corporation of PNG and Air Niugini and is also a member of Council of the Legal Training Institute, and a council member of the PNG Law Society.

Mr. Posman is a member of the PNG Law Society and the PNG Institute of Directors.





### Our corporate values



These will be realized by requiring and instilling in our Directors, employees and core service providers the need to embrace and adhere to the following ethical standards:





## Corporate Governance Disclosure Statement

The Board is committed to upholding and implementing the principles of good corporate governance. This is considered critical as recent experiences have shown that the lack of good corporate governance has contributed directly to corporate frauds and in worst case scenarios, corporate failures leading to a serious erosion of confidence in those entrusted with the responsibility of managing companies - the directors. The enhanced accountability, transparency and integrity flowing from improved corporate governance creates value for shareholders and other stakeholders, reduces costs, increases competitiveness and restores confidence.

The Board is responsible for the corporate governance of the Fund, including its corporate planning, establishing goals for management and monitoring achievement of these goals.

This statement sets out the principle corporate governance practices and disclosures that were in operation during the year.

## The Trustee

Comrade Trustee Services Limited (CTSL) is the successor in law to the DFRBF Board and has been approved by the Bank of Papua New Guinea (BPNG) as the licensed trustee for the fund. As a licensed trustee, it has ultimate legal responsibility for the prudent management of the fund, and subject to the requirements of the Superannuation Act and the governing rules of the fund has the power, authority and the discretion generally to do all such acts as it considers necessary or expedient for the sound administration, maintenance, investment and preservation of the fund.

## The Board

CTSL is managed under the direction of the Board of Directors. The Board has the ultimate legal responsibility for the sound management of the fund, and subject to the requirements of the Superannuation Act and the governing rules of the Fund.

The Board comprises of seven Directors, three of whom represent members of the Fund and four independent Directors. Strict appointments criteria, including a "fit and proper" test ensures that persons appointed to the Board are legally eligible and possess skills, knowledge, experience or expertise in the management of commercial entities and whose inclusion on the board will add value and enhance corporate governance. Board appointments are subject to Bank of Papua New Guinea approval. Directors hold office for a term of three years at the expiry of which they are eligible to nominate for re-election subject however to any restrictions contained in the Company Constitution and Central Bank approval.

The management of the company is delegated to the Chief Executive Officer (CEO) who oversees its daily operations and implements Board policies.

All Board and Committee meeting are convened in Port Moresby and therefore members of the Board must be residents of the National Capital District.

The names of members of the Board at the date of this report, including their remuneration, status on the Board and information relating to their attendance at meetings for the twelve months to 31st December 2004 are as follows:-



Name of Director	Fee Received*	Board Status	Date of Appointment	Attendance of Meetings		
				Board	Audit Committee	Appointments Committee
Chris Alu	K15,800	Current	19/12/02	4/4	1/1	-
Col D. Takendu, OBE (Rtd)	K12,150	Current	19/12/02	3/4	-	1/1
Col R. Renagi, OBE (Rtd)	K12,450	Current	19/12/02	4/4	-	1/1
Capt Tom Ur, MBE	K12,100	Current	01/01/03	3/4	1/1	-
Brian Hull	K12,100	Current	07/07/03	3/4	-	1/1
Johnson Kalo	Nil	Current	07/07/03	2/4	1/1	-
Kisikiu Posman	K 6,050	Current	04/06/04	2/3	0/1	1/1

\* Fees shown above are before tax.

The Board complied with its approved Calendar of Meetings planned for the year. The Board formally met four times during the year and the two Committees each met once.

All meeting papers are circulated seven days in advance to all Directors. This enables adequate time to read and understand the matters requiring Board action, thus ensuing informed decisions are made for the ultimate benefit of the Fund.

### Audit & Compliance Committee

The Committee was established on 28th July 2004, and met once during the year. The role of the Committee includes review of the Fund's financial statement, review of audit reports, review of the company's accounting policies, review of internal control systems and procedures including risk assessment and management strategies, tenders, annual budgets, investment policy guidelines and related matters.

### Appointments & Remuneration Committee

The Committee was established on 28th July 2004, and met once during the year. The role of the Committee includes succession planning, review and recommendation of candidates for Board vacancies, review of Board fees and remuneration, appraise and recommend short list of executive appointments, review of salary and remuneration including terms of employment of senior management and related matters.

### External Board Positions

As at 31st December 2004, the following external Board positions were held by Directors and staff of CTSL.

Name	Status	Position	Company
Col David Takendu, OBE	Director	Director / Chairman	Banora Trading Limited
Col Reginald Renagi, OBE	Director	Director	Banora Trading Limited
Col Reginald Renagi, OBE	Director	Director	Hunter Limited
Col Reginald Renagi, OBE	Director	Director	Pacific Capital Limited
George Uware	Employee	Director	Banora Trading Limited
George Uware	Employee	Director	Hunter Limited

Employees of the company appointed to the Boards of subsidiary companies are not paid any fees.



## Independent Professional Advise

With the approval of the Chairman, a Director is entitled to seek independent professional legal and accounting advice at the expense of the Fund, regarding any aspect of that Director's duties and/or issues of concern about the Fund's operations.

## Code of Conduct and Ethical Standards

The Board has adopted several codes relating to the conduct of Directors, management and staff including the management of conflicts of interest and confidentiality. CTSL recognizes and acknowledges the requirement for Directors and employees to observe and uphold the highest standards of behaviour and ethical standards in the performance of their duties.

## Fund Administration

The fund administration function is delegated to and performed by Kina Investment & Superannuation Services Limited (KISSL) in compliance with the Superannuation Act 2000. The engagement of KISSL is for a term of three years commencing 1st January 2003. At least three months prior to the expiry of contract, further engagement will be determined by tender.

## Investment Management

The investment management function is delegated to and performed by Kina Funds Management Limited (KFML) in compliance with the Superannuation Act 2000. The engagement of KFML is for a term of three years. At least three months prior to the expiry of the contact further engagement will be determined by tender.

The investment manager is required to manage the Fund's investment portfolio in accordance with the investment policy approved by the trustee from time to time and subject to prudential standards issued by the Bank of Papua New Guinea and the Superannuation Act.

The Fund's investment objective is to maximize returns over the medium to long term at low to moderate risk levels.

## Employee Remuneration

During the year, the number of employees or former employees (not being Directors of the company) who received remuneration and other benefits in excess of K100,000 per annum from the company stated in bands of K10,000 are:-

	2002	2003	2004
K100,000 – K110,000	-	1	1
K110,000 – K120,000	-	-	-
K120,000 – K130,000	-	-	-
K130,000 – K140,000	1	-	-
K140,000 – K150,000	-	1	1

The above amounts exclude performance bonus paid to employees of amounts ranging between one to six weeks annual leave entitlements approved in November 2004. Gross bonus payment amounted to K31,393.

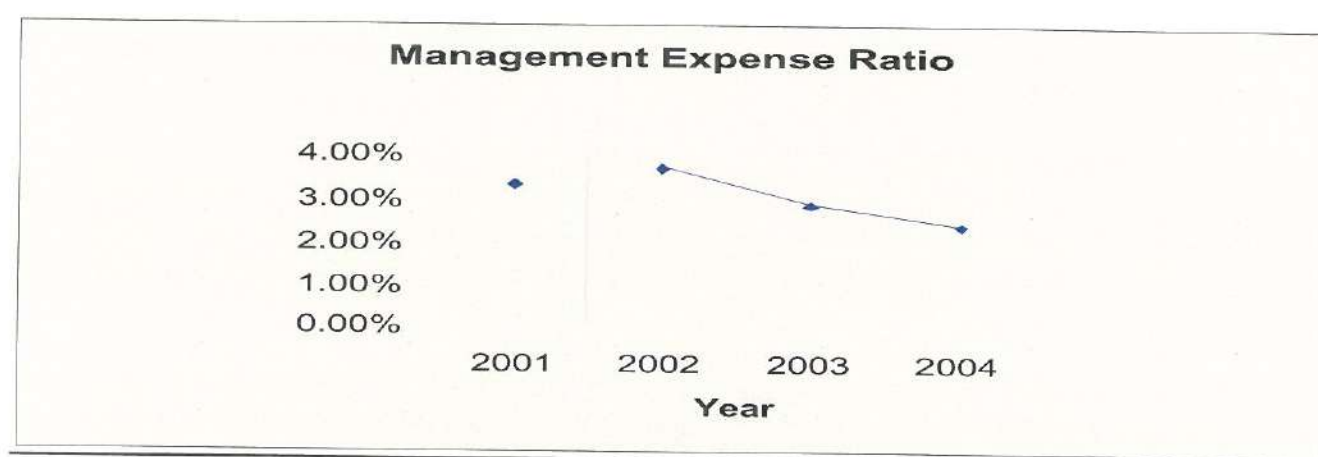


## Management Expense Ratio

Management expense ratio (MER) is an underlying key financial performance indicator used to measure the performance of the fund relative to industry standards and also to assist identifying adverse deviation and take corrective action.

The MER is determined by taking the sum of all expenses (excluding pension and related benefit payments) divided by the average net asset value of the Fund expressed as a percentage. The net asset values are based on audited accounts and after allowing for net changes in market values, depreciation and taxation.

	2001	2002	2003	2004
Management expense ratio	3.34%	3.73%	2.88%	2.39%





## Staff Employment Policy

CTSL is an equal opportunity employer and does not discriminate on the basis of sex, race, colour, religion or sexual orientation. Employment is merit based. A total of eighteen staff were employed by the company during the year.

### Investment transactions (excluding cash and treasury notes)

Name of Entity	Transaction Type	Classification	Settlement Date	Number of Shares	Amount
Hombrum Piggery Ltd	Mortgagee Sale	Equity / loan	15-Dec-2004	–	K249,751
Henao Drive flats	Sale	Property	29-April-2004	N / A	K390,000
Metal Refining Holdings Ltd	Share sale	Equity	1-July-2004	1,500,000	K178,000
Monier Ltd	Share sale	Equity	5-May-2004	4,500	K6,428
Bank of South Pacific Ltd	Share acquisition	Equity	15-July-2004	929,190	K971,002
Ramu Sugar Ltd	Share acquisition	Equity	13-Jan -2004	50,000	K76,500
Ramu Sugar Ltd	Share acquisition	Equity	19-May-2004	50,053	K74,078
Ramu Sugar Ltd	Share acquisition	Equity	20-May-2004	50,000	K74,000
Ramu Sugar Ltd	Share acquisition	Equity	17-May-2004	418,000	K618,640
Telstra Corporation	Share acquisition	Equity	17-Sept-2004	20,000	AUD\$97,000
Commonwealth Bank	Share acquisition	Equity	11-Aug-2004	5,000	AUD\$155,300
Commonwealth Bank	Share acquisition	Equity	13-Aug-2004	5,000	AUD\$154,500
AMP China Fund	Unit acquisition	Mutual fund	10-Aug-2004	149,250	AUD\$149,250
Mahogany Capital Fund	Unit acquisition	Mutual fund	30-Nov-2004	2,500	AUD\$250,000

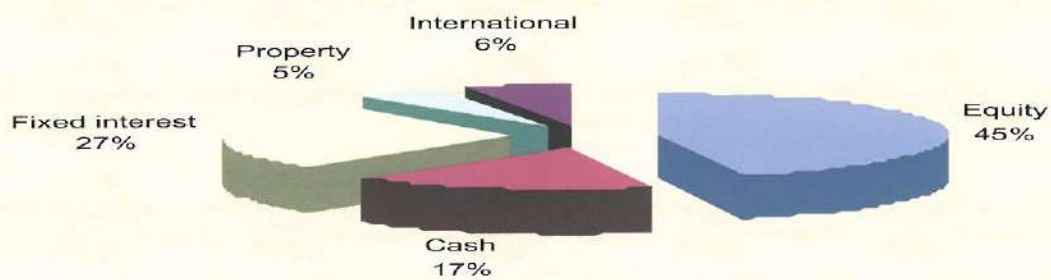
## Investment Guidelines

Asset allocation as at 31 December 2004

Asset Class	Asset Allocation		
	Kina	% Holding	Neutral Allocation
Cash	K18,987,345	17.01%	15%
Fixed interest	K29,734,614	26.64%	30%
Equity	K50,652,161	45.38%	30%
Property	K5,865,505	5.26%	15%
International	K6,368,404	5.71%	10%



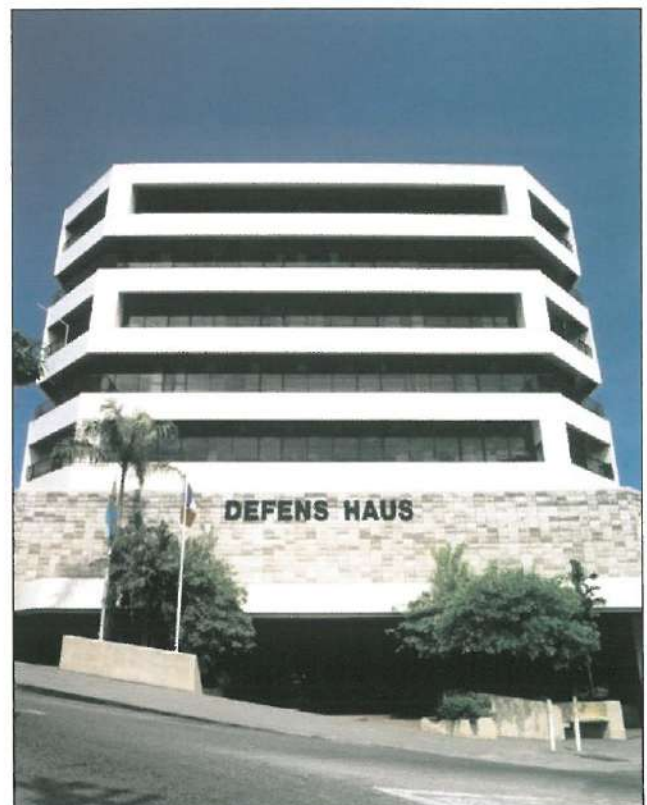
Asset Allocation as at 31 December 2004



### Valuation methodology

The valuation methodology adopted by the trustee is as follows:-

Listed equities	- Closing market price as quoted by the relevant stock exchange at balance date
Unlisted equities	- Price as determined by independent professional valuation
Property	- Value as determined by a registered property valuer
Government securities	- At purchase price/face value





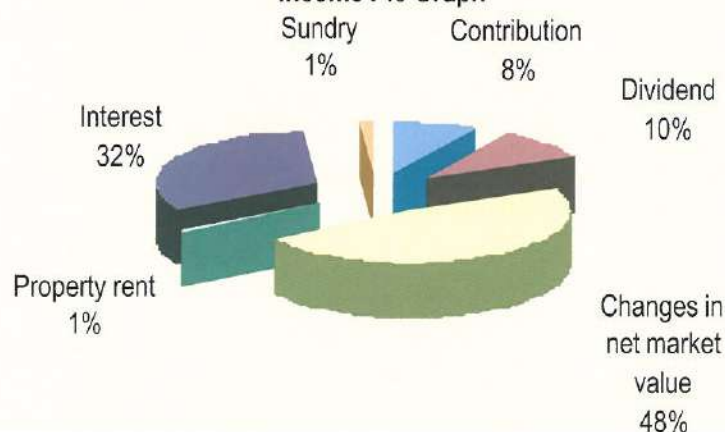
## Highlights of 2004

## Financial Performance Summary

	2004	2003	Variance
● Total income	K22,626,115	K20,376,210	+K2,249,905
● Net profit (after tax)	K10,534,283	K6,664,376	+K3,869,907
● Total Fund net assets	K112,234,185	K101,699,902	+K10,534,283
● Total benefits paid (net)	K3,778,399	K6,652,830	-K2,874,431
● Interest crediting rate	5%	5%	+%
● CPI indexation rate*	5%	5%	+%
● MER	2.39%	2.88%	-0.49%

\* Note: Last CPI indexation awarded in 2001 and subject to actuarial evaluation.

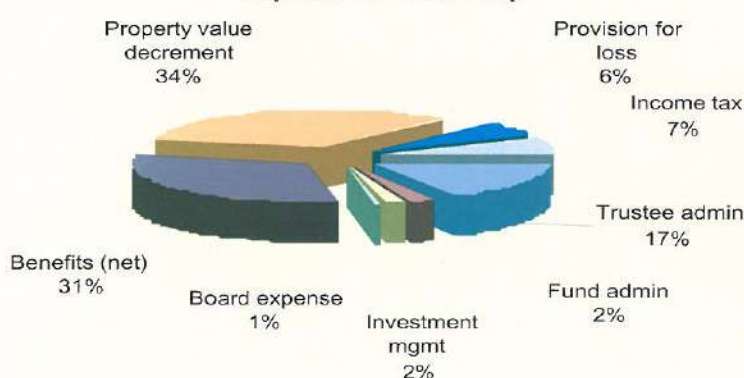
## Income Pie Graph



## Income Summary (Kina)

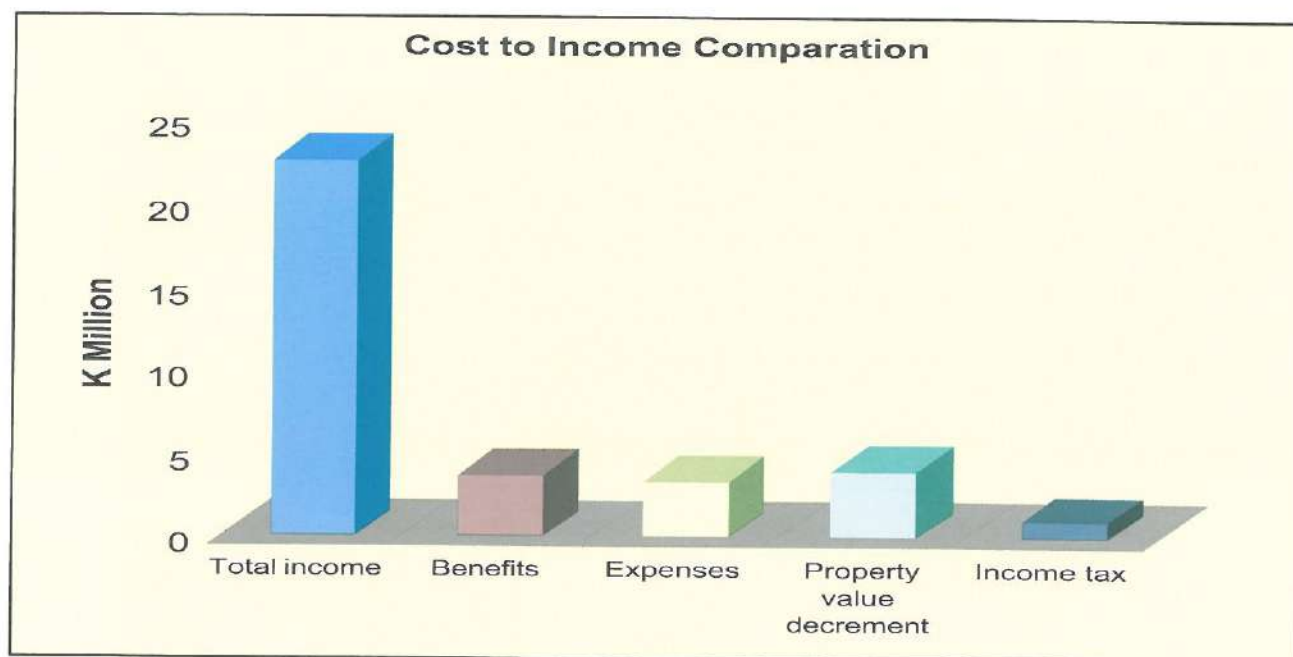
● Interest	K 7,242,610
● Sundry	K 285,398
● Contribution	K 1,871,445
● Dividend	K 2,270,179
● Property rent	K 183,279
● Changes in net market value	K10,773,204
<b>Total Income</b>	<b>K22,626,115</b>

## Expenditure Pie Graph



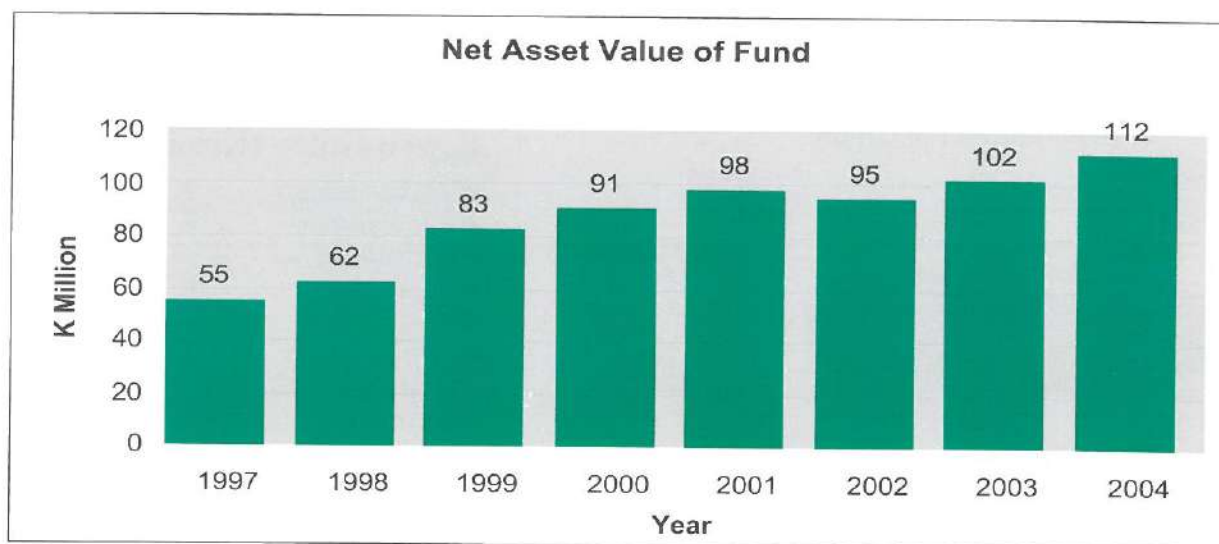
## Expenditure (Kina)

● Trustee admin	K 2,112,126
● Fund admin	K 275,261
● Investment	K 229,291
● Board exp	K 75,191
● Benefits (net)	K 3,778,399
● Extraordinary	K 4,037,509
● Provision for loss	K 684,971
● Income tax	K 899,084
<b>Total Expense</b>	<b>K12,091,832</b>



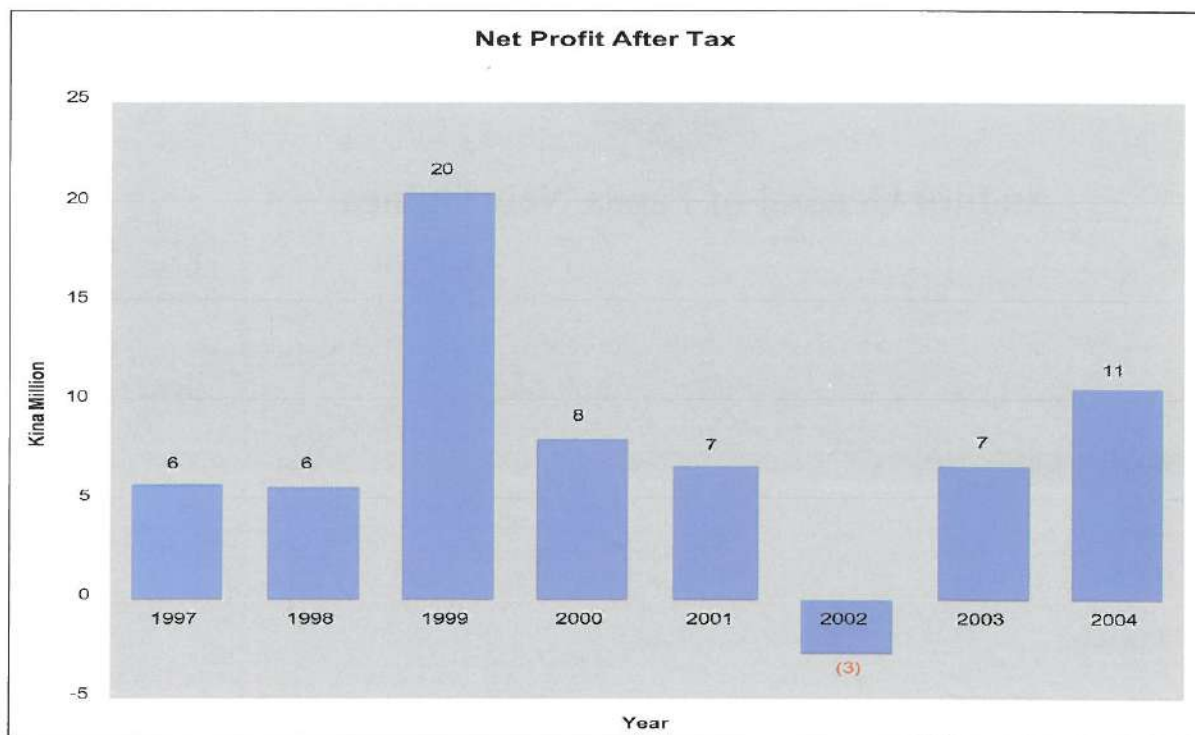
The cost to income ratio is 25.78%, however the Trustees are confident that with improved financial discipline and greater cost efficiencies coupled with a sustained growth in investment income of at least 7% per annum this ratio is expected to reduce further to levels comparable with industry standards.

## Fund Growth Trend



The above bar graph shows that the fund has grown steadily from K54,888,588 in 1997 to K112,234,185 as at 31st December 2004. This represents an incredible growth in the net asset value of the fund by over 100% since 1997. Your Trustees are confident that with prudent and diligent management such growth can be sustained and therefore assuring members financial security at retirement.





Except for 1999 when the fund posted a net profit in excess of K20.0 million and 2002 when the fund recorded a net loss of nearly K3.0 million the above graph illustrates that overall, net profit after tax has steadily grown from K6.0 million in 1997 to K10.5 million in 2004. The Trustees are confident that with careful and prudent management, fund profitability is forecast to grow.

The exceptional net profit of K20.0 million recorded in 1999 resulted from the high interest rates prevailing during the year. The write-down of K4.0 million in the Sandaun Motel investment contributed significantly to the loss of K2.8 million recorded in 2002.





## Auditor General of Papua New Guinea

Telephone: 302 2200  
Fax: 325 2872

Level 6, TISA HAUS  
P.O. Box 423, Waigani  
Papua New Guinea

12 April 2005  
30-28-4

*The Honourable Mathew Gubag, MP*  
*Minister for Defence*  
*Office of the Minister*  
*P.O. Parliament Haus*  
*Waigani*  
*National Capital District*

Dear Sir

### COMRADE TRUSTEE SERVICES LIMITED (Trustee for the Defence Force Retirement Benefits Fund)

I have audited and inspected the accounts and records of the financial transactions, and records relating to the assets and liabilities, and assets in the custody of Comrade Trustee Services Limited for the year ended 31 December, 2004. My report on the Company's financial statements for the year ended 31 December, 2004 was forwarded to you under separate cover on even date. My report did not contain any qualifications.

### OTHER MATTERS

I wish to bring to your attention the following matter, which in my opinion is significant:

#### 1.0 Actuary Report

The Fund is expected to obtain an independent Actuary's valuation every three years to ascertain the sufficiency of funds to meet future obligations in terms of pension and lump sum payments. The valuation is also to provide guidance as to whether additional benefits may be offered or the existed benefits can be maintained in future.

The Fund has engaged the services of an Actuary for this exercise but the Actuary's report was not ready for my perusal at the time of finalising my audit report.

Yours faithfully,

GEORGE W. SULLIMAN  
Auditor General



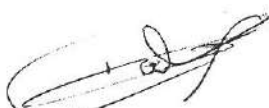
## Declaration by the Trustees

In our opinion, the Fund's accounts set out on pages 21 to 39 are drawn up so as to give a true and fair view of the state of affairs as at 31st December 2004, and the surplus before distribution for the year ended on that date, of the Defence Force Retirement Benefits Fund so far as they concern members of the Fund. Further, all risk management systems and processes are in place and operating effectively.

The financial statements have been drawn up in accordance with the requirements of the Superannuation (General Provisions) Act 2000 and the requirements of the Trust Deed of the Defense Force Retirement Benefits Fund dated the 19th December 2002.

DATED at Port Moresby this 31st day of March 2005.

For and on behalf of the Board of Directors of the Trustee.



Chris Alu  
Chairman – Board of Trustees



Captain (Navy) Alois Tom Ur  
Director

## Declaration by Management

In our opinion, the Fund's accounts set out on pages 21 to 39 are drawn up so as to give a true and fair view of the state of affairs as at 31st December 2004, and the surplus before distribution for the year ended on that date, of the Defence Force Retirement Benefits Fund so far as they concern members of the Fund. Further, all risk management systems and processes are in place and operating effectively.

The financial statements have been drawn up in accordance with the requirements of the Superannuation (General Provisions) Act 2000 and the requirements of the Trust Deed of the Defense Force Retirement Benefits Fund dated the 19th December 2002.

In our opinion, the accompanying financial statements have been properly drawn up and show the true state of affairs of the Fund as at the date. We are of the opinion that:

- a) the result of the Fund's operations for the year have not been materially affected by items, transactions or events of an abnormal character;
- b) no circumstances have arisen which would render any amount in the financial statements misleading;
- c) there are no contingent liabilities that could materially affect the ability of the Fund to meet its obligations as and when they become due.

DATED at Port Moresby this 31st day of March 2005.

For and on behalf of the management,



George B. Uware  
Chief Executive Officer



Richard Sinamoi  
General Manager

## INCOME STATEMENT

	Note	2004 K	2003 K
Income from Investment Activities			
Interest income	2	7,242,610	7,592,503
Dividend income		2,270,179	1,846,721
Property rental	3	648,126	679,835
Changes in net market value of investments	17	10,773,204	8,403,478
Other operating income	5	285,398	196,761
<b>Total Investment Income</b>		<b>21,219,517</b>	<b>18,719,298</b>
Less Direct Investment Expenses			
Provision for impairment	21	684,971	2,560,462
Property value decrement	19(a)	4,037,509	0
Other direct investment cost		0	0
Property rental expenses	3	464,847	324,193
<b>Total Direct Investment Expenses</b>		<b>5,187,327</b>	<b>2,884,655</b>
<b>Net Income from Investment Activities</b>		<b>16,032,190</b>	<b>15,834,643</b>
Contributions			
Contributions received		1,871,445	1,981,105
<b>Total Operating Income</b>		<b>17,903,635</b>	<b>17,815,748</b>
<b>Expenditure</b>			
Benefits (net)	6	3,778,399	6,652,830
Operational expenses			
Staff expenses	10	514,262	535,772
Trustee fees & Board expenses	11	75,191	74,874
Fund administration fee	7(a)	275,261	252,247
Investment management fee	7(b)	229,291	317,990
Operating expenses	9	1,597,864	1,513,483
<b>Total Operational Expenses</b>		<b>2,691,869</b>	<b>2,694,366</b>
<b>Total Expenses</b>		<b>6,470,268</b>	<b>9,347,196</b>
<b>Net Operating Surplus before income tax</b>		<b>11,433,367</b>	<b>8,468,552</b>
Income tax expense	13(a)	899,084	1,804,176
<b>SURPLUS/(DEFICIT) AFTER TAX</b>		<b>10,534,283</b>	<b>6,664,376</b>

The income statement is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 27 to 40



## STATEMENT OF NET ASSETS

	Note	2004 K	2003 K
<b>Investments</b>			
Treasury bills	15	19,598,687	31,535,262
Investment securities held-to-maturity	18	19,578,434	0
Investment securities-available-for-sale	17	52,585,315	38,048,968
Investment properties	19	7,041,130	11,450,124
Loans	16	7,454,740	12,389,342
		<hr/>	<hr/>
		106,258,306	93,423,696
<b>Other Assets</b>			
Cash and due from other banks	14	6,549,498	6,425,247
Other assets	21	1,452,383	2,537,527
Property, plant & equipment	20	615,693	628,273
Deferred income tax	13(c)	146,768	0
		<hr/>	<hr/>
<b>Total Other Assets</b>		8,764,342	9,591,047
		<hr/>	<hr/>
<b>Total Assets</b>		115,022,648	103,014,743
<b>Liabilities</b>			
Current income tax payable	13(b)	490,703	78,018
Deferred income tax liabilities	13	0	280,908
Other liabilities	22	2,297,760	955,912
		<hr/>	<hr/>
<b>Total liabilities</b>		2,788,463	1,314,838
		<hr/>	<hr/>
<b>Net Assets</b>		112,234,185	101,699,902
		<hr/>	<hr/>
<b>Represented By:</b>			
Balance of Members fund at beginning of year		101,699,902	95,035,526
Surplus during the year		10,534,283	6,664,376
		<hr/>	<hr/>
<b>Total Members Fund</b>		112,234,185	101,699,902
		<hr/>	<hr/>

The statement of net assets is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 25 to 40

## STATEMENT OF CASH FLOW

	Note	2004 K	2003 K
Cash flow from operating activities			
Interest received		8,113,489	6,785,348
Dividends received		2,270,179	1,846,721
Property income received		418,914	302,821
Other operating income received	5	199,201	25,208
Cash payments to employees and suppliers		(2,348,439)	(2,847,706)
Income tax paid	13(b)	(914,076)	(1,076,939)
Cash flow from operating profit before changes in operating assets and liabilities		7,739,268	5,035,453
Changes in operating assets and liabilities			
Net decrease in loans to customers (members)	15	214,200	564,792
Net increase in other assets	16	(201,012)	(153,998)
Net increase/(decrease) in other liabilities		34,758	(213,588)
Net Cash provided by operating activities		7,787,214	5,232,659
Cash flow from investing activities			
Placement of term deposits (net)	14	780,000	0
Placement of treasury bills (net)	15	12,860,801	(13,838,901)
Purchase of investment securities held to maturity	18	(19,625,628)	0
Proceeds on maturity of investment securities held to maturity		0	2,000,000
Purchase of property and equipment	20(a)	(137,456)	(331,817)
Proceeds from disposal of property and equipment		43,000	12,000
Purchase of investment properties	19(a)	(85,585)	(718,182)
Proceeds from sale of investment properties		370,573	0
Purchase of securities	17(b)	(3,789,810)	(320,992)
Proceeds from sale of securities	17(b)	33,334	874,447
Net cash used in investing activities		(11,110,771)	(12,323,445)
Cash flows from activities with Contributors			
Contributions received from members		1,871,445	1,981,105
Benefits paid (including State share)		(8,556,267)	(15,224,608)
Net Cash used in activities with Contributors		(6,684,822)	(13,243,503)
Cash from activities with the State			
Cash receipt of State share (benefits)		10,278,856	7,747,164
Net Increase/(Decrease) in Cash and Cash Equivalent		268,477	(12,587,125)
Cash and Cash Equivalents at beginning of year	23	24,121,608	36,708,733
Cash and Cash Equivalents at end of year	23	24,390,085	24,121,608

The statement of net assets is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 25 to 40



*Notes to and forming part of the financial statements***1. SIGNIFICANT ACCOUNTING POLICIES**

The principle accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

**a) Statement of compliance**

The financial statements of the Defence Force Retirement Benefits Fund ("the fund") have been prepared in accordance with the International Financial Reporting Standards ("IFRS") and the accounting standards as adopted by the Accounting Standards Board of Papua New Guinea (ASB).

The ASB has adopted International Accounting Standards and Interpretations as issued by the Standing Interpretations Committee as the applicable reporting framework.

**b) Basis of preparation**

The financial statements have been prepared under the historical cost convention, however market valuations have been used in accordance with International Financial Reporting Standards where appropriate.

In accordance with the Board's policy, the fund's investments are revalued every three years, except shares which are adjusted to market price at year end.

No consolidated accounts have been prepared on the basis that the inclusion of the operating results of companies controlled by the Fund is not appropriate.

The Fund's financial statements have been prepared on a going concern basis.

All figures are rounded to the nearest Kina.

**c) Recognition of income and expenditure**

Income is recognized in the income statement on an accrual basis except dividend and interest income from member housing advance ("MHA") and tertiary education assistance ("TEA") which are brought to account when received. Prior to 2000, the interest income from MHA was deducted from the member entitlement when they were discharged from the Defence Force. However after 2000, interest is deducted from the loan once the loan has been released. The interest from TEA is recognized once the loan has been released.

Interest income includes coupons earned on fixed income investment and trading securities and accrued discount and premium on treasury bills and other discounted instruments. Interest income is suspended when loans become doubtful for collection, such as when over due by more than 30 days, or when the borrower defaults, if earlier than 30 days. Such income is excluded from interest income until received.

Contributions from members are brought to account as income when receivable.

The Fund accounts for expenditure on an accrual basis, except pension, lump sum, refund of contributions and related government contributions which are brought to account as they become payable. Accrual of benefit liabilities are based on the history of payment.

**d) Members accounts**

Contributions are accounted for, and members accounts credited with their contributions on a cash basis upon receipt of reconciled contribution schedules.

## Notes to and forming part of the financial statements

Accounting for interest credited to members' accounts is on the basis of the period to which the contributions relate and at a rate of interest as determined by the Board of Directors each year calculated on the daily balance of the member's account.

### e) Income tax

The Fund adopts the principles of tax effect accounting whereby the income tax expense for the year in the Income Statement is matched with the accounting result (after allowing for permanent differences). Where the realization of the future tax benefit relating to timing differences is not considered to be virtually certain, the future tax benefit is not brought to account.

Tax on the surplus or deficit for the year comprises current tax and change in deferred tax.

Current tax comprises tax payable calculated on the basis of the expected taxable income for the year using the tax rates enacted by the balance date, and any adjustment of tax payable for previous years.

Deferred tax is provided using the balance sheet liability method on all temporary differences between the carrying amounts for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax assets are recognized to the extent that it is probable that the future taxable profit will be available against which the temporary differences can be recognized.

Income tax payable on profits based on the applicable tax laws in each jurisdiction is recognized as an expense in the period in which the profits arise. The tax effects of income tax losses available to be carried forward are recognized as an asset when it is probable that future taxable profits will be available against which these losses can be recognized.

### f) Property, plant and equipment and depreciation

Property, plant and equipment are stated at historical cost less accumulated depreciation. The straight line method of depreciation is used to calculate depreciation so as to write-off the cost of such assets to their residual values over their estimated useful lives as follows:

	Used in Operations	Investment Properties
Land and buildings	Nil	Nil
Furniture and fittings	15%	11.25 to 30%
Plant and equipment	Nil	15 to 30%
Motor vehicle	30%	Nil
Office equipment	20%	Nil
Renovation	10%	Nil
Software	33%	Nil

The asset's residual values and useful lives are reviewed and adjusted, if appropriate at each balance sheet date.

Profits and losses on disposal (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. Repairs and maintenance costs are charged to the income statement when the expenditure is incurred.

### g) Financial assets

The Fund investment securities are classified into two categories; available-for-sale and held-to-maturity. Management determines the appropriate classification of its investments at the time of purchase.



## Notes to and forming part of the financial statements

Investment securities 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, exchange rates, or equity prices are classified as available-for-sale.

Investments are valued as at 31st December 2004 as follows:

- i) Listed shares are valued at 31 December 2004 at last sale price on that date. Off-shore investments are converted using the ANZ Bank exchange rate.
- ii) Unlisted shares are valued as at 31 December 2004 as adopted by the Board. This valuation was performed by Deloitte Touche Tohmatsu as an independent professional valuer. The main factor used in the analysis was a combination of earnings, dividends and an orderly recognition of assets, as appropriate.
- iii) Land and buildings are valued at 31 December 2004. This valuation was performed by Professional Valuer of PNG Limited, Ashton Brunswick and McCann Property and Planning. The valuation reports indicate that several methods have been considered for the valuation process and includes; capitalization method, summation method and discounted cash flow method.
- iv) The net movement on revaluation is reflected in the income statement.

Available-for-sale financial assets are subsequently re-measured at fair value based on quoted bid price. Gains and losses arising from changes in the fair value of securities classified as available-for-sale are recognized in the income statement in the period in which they arise.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payment and fixed maturities that the Fund's management determines it has both the intention and the ability to hold to maturity. If the Fund were to sell (other than insignificant amounts of held-to-maturity assets), the entire category would be tainted and re-classified as available-for-sale.

Held-to-maturity investments are carried at amortized cost using effective interest rate method of valuation.

Interest calculated using the effective interest method is recognized in the income statement.

### h) Loans and impairment losses

Loans are non-derivative financial assets with fixed or determinable payments that are not quoted in any active market. They arise when the Fund provides money, goods or services directly to a debtor with no intention of trading the receivable.

Loans originated by the Fund by providing money directly to the borrower are recognized as loans originated by the Fund and are carried at cost, which is defined as the fair value of cash consideration given to originate those loans as is determinable by reference to market price at origination date. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction.

### i) Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise of balances less than 90 days maturity from date of acquisition including cash, treasury bills and amounts due from other banks.

## Notes to and forming part of the financial statements

### j) Foreign currency

### i) Functional presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The financial statements are presented in the currency of the Independent State of Papua New Guinea, the Kina, which is the Fund's functional and presentation currency.

### ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rate prevailing at the dates of the transactions or at balance sheet date. Foreign currency gains and losses resulting from the settlement of such transactions and from the transaction at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement.

### k) Funding arrangement

Serving members of the Defence Force contributed 6% of their gross salary to the Fund during the year. Due to the defined benefits nature of the Fund, the employer or State is not required to pay its share of superannuation contribution until the member exits the Fund and only after the member qualifies for pension at which time it assumes all residual pension liability after allowing for the member's contribution, investment income and expenses of administering the Fund.

### l) Provisions

Provisions are recognized when the Fund has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefit will be required to settle the obligation.

### m) Changes in accounting policies and comparatives

When necessary, comparative figures have been adjusted to conform to changes in presentation and accounting policies in the current year. There have been no changes to accounting policy in the current year.



## Notes to and forming part of the financial statements

	Note	2004 Kina	2003 Kina
<b>2. Interest income</b>			
Cash and short term funds		462,074	771,271
Loans and advances		2,833,743	838,311
Treasury bills		3,555,663	5,906,822
Investment securities		391,130	76,099
Total interest income		<u>7,242,610</u>	<u>7,592,503</u>
<b>3. Property income</b>			
Gross rental income		648,126	679,835
Less: expenses			
- Impairment losses	21	196,384	0
- Depreciation	19(b)	26,370	72,961
- Other maintenance costs		242,093	251,232
Total expenses		<u>464,847</u>	<u>324,193</u>
Net property income		<u>183,279</u>	<u>355,642</u>
<b>4. Dividend income</b>			
Available-for-sale securities		2,270,179	1,846,721
Total dividend income		<u>2,270,179</u>	<u>1,846,721</u>
<b>5. Other operating income</b>			
Recovery on investment securities previously written off		184,929	0
Gain on sale of investment securities available-for-sale	16	6,667	171,553
Gain on valuation of off-shore deposits		79,530	0
Others		14,272	25,208
Total other operating income		<u>285,398</u>	<u>196,761</u>
<b>6. Benefit payment</b>			
Pension and back pension		4,859,813	3,831,244
Refund		572,090	601,559
Gratuity		10,320	41,808
Death claim		6,015	0
Lump sum 50% pension commutation		3,108,029	10,749,997
		<u>8,556,267</u>	<u>15,224,608</u>
Less: Government share		4,777,868	8,571,778
Net benefit payment		<u>3,778,399</u>	<u>6,652,830</u>

## Notes to and forming part of the financial statements

	Note	2004 Kina	2003 Kina
<b>7. Management fee</b>			
a) Fund administration fee		274,200	248,607
Benefit payment fee		1,061	3,640
		<u>275,261</u>	<u>251,247</u>
b) Investment management fee		229,291	317,990
		<u>504,552</u>	<u>570,237</u>
<b>8. Impairment losses</b>			
Loans and advances to customers	15	250,249	0
Investment in properties	17	0	1,407,742
Investment securities available-for-sale	15	0	919,742
Other assets	20	434,722	232,978
		<u>684,971</u>	<u>2,560,462</u>
<b>9. Operating expenses</b>			
Administrative expenses	12	1,169,737	839,213
Depreciation	19	150,036	157,320
Computer software costs		9,872	500
Operating lease		131,740	290,213
Others		136,479	226,237
		<u>1,597,864</u>	<u>1,513,483</u>
<b>10. Employment expenses</b>			
Staff salaries and wages		349,108	351,344
Superannuation contributions		14,067	12,577
Staff accommodation		100,720	79,275
Traveling cost		8,056	4,816
Others		42,311	87,760
		<u>514,262</u>	<u>535,772</u>
As at the year end, the company had 17 (2003 - 17) full-time employees.			
<b>11. Board of trustee expenses</b>			
Board fees and allowances		75,191	74,874
		<u>75,191</u>	<u>74,874</u>



## Notes to and forming part of the financial statements

	Note	2004 Kina	2003 Kina
<b>12. Administrative expenses</b>			
Advertising		26,907	61,989
Internet service provider		16,307	11,892
ASF license		452,818	0
Printing and stationery		59,655	48,913
Professional fees:			
- Audit fee		80,000	80,00
- Legal costs		133,871	150,245
- Consultation		106,762	119,001
- Commission of inquiry		203,250	300,022
Telephone		33,140	28,143
Others		57,027	39,008
		<u>1,169,737</u>	<u>839,213</u>
		=====	=====

**13. Income tax**

Income tax on the Fund's profit before tax differs from the amount calculated on the operating profit. The differences are reconciled as follows:

## a) Income tax expense for the year:

Current tax	1,035,697	1,099,193
Deferred tax	5,511	0
Change in tax rate	0	(56,152)
Prior year adjustment	(142,124)	761,165
	<u>899,084</u>	<u>1,804,176</u>
	=====	=====

## b) Current Income tax payable:

Prima facie tax at 30% (2003 – 30%)	2,858,342	2,541,766
Tax effect of permanent differences	(1,822,645)	(1,442,573)
Net effect of timing difference	439,508	1,348,351
	<u>1,475,205</u>	<u>2,447,544</u>
Balance at beginning of year	78,018	(796,668)
Prior year adjustment	(148,444)	(495,919)
Income tax paid	(914,076)	(1,076,939)
	<u>490,703</u>	<u>78,018</u>
	=====	=====

**14. Cash and dues from other banks**

Cash on hand (Petty cash)		700	700
Loans and advances to banks		252,417	535,115
Placement with other banks (< 90 days maturity)		5,516,381	5,889,432
		<u>5,769,498</u>	<u>6,425,247</u>
Included in cash and cash equivalents	22	5,769,498	6,425,247
Placement with other banks (>90 days maturity)		780,000	0
		<u>6,549,498</u>	<u>6,125,247</u>
		=====	=====

## Notes to and forming part of the financial statements

	Note	2004 Kina	2003 Kina
<b>15. Treasury bills</b>			
Less than 90 days (included in cash and cash equivalents)	22	18,620,587	17,696,361
More than 90 days		978,100	13,838,901
		<u>19,598,687</u>	<u>31,535,262</u>
		=====	=====

Treasury bills are debt securities issued by the Bank of Papua New Guinea for a term of one, two, three and six months. Bills are categorized as assets held for trading and carried at fair value.

**16. Loans to members and others**

## a) Loans and advances

Members housing advance	937,547	1,151,747
Others:		
- State share of pension benefits	577,442	5,047,595
- Burns Peak and Waigani Drive project loan	5,000,000	5,000,000
- Hunter Limited	690,000	690,000
- Hombrum Piggery Limited	500,000	500,000
Gross loans and advances	<u>7,704,989</u>	<u>12,389,342</u>
Less specific allowance for losses	250,249	0
Net loans and advances	<u>7,454,740</u>	<u>12,389,342</u>
	=====	=====

Loans are at fixed interest rates.

## b) Movement in specific allowance for losses

Balance at beginning of year	0	0
Impairment losses during the year	250,249	0
Balance at end of the year	<u>250,249</u>	<u>0</u>
	=====	=====

The aggregate amount of non-performing loans on which interest was not accrued amounted to K690,000 during the year (2003 – K5,737,595).

Unrecognized interest amounted to K102,662 as at the end of the year (2003 – K1,561,521). Uncollected interest accrued on impaired loans amounted to K434,722 (2003 – K435,560).

**17. Investment securities available-for-sale**

## a) Equity securities at fair value

Listed securities	42,002,827	29,179,915
Unlisted securities	11,481,980	9,788,795
Specific allowance for losses	(899,492)	(919,742)
Net equity securities available-for-sale	<u>52,585,315</u>	<u>38,048,968</u>
	=====	=====



## Notes to and forming part of the financial statements

	Note	2004 Kina	2003 Kina	
b) Movement in investment securities available-for-sale:				
Balance at beginning of year		38,048,968	30,947,134	
Gains from changes in fair value		10,773,204	8,403,478	
Purchases		3,789,810	320,992	
Disposals		(33,334)	(874,447)	
Impairment losses during the year		0	(919,742)	
Gains on sale	5	6,667	171,553	
Balance at end of the year		<u>52,585,315</u>	<u>38,048,968</u>	
c) Movement in specific allowance for losses:				
Balance at beginning of year		919,742	0	
Impairment losses during the year		0	919,742	
Write-off during the year as un-collectable		(20,250)	0	
Balance at end of the year		<u>899,492</u>	<u>919,742</u>	
<b>18. Investment securities held-to-maturity</b>				
a) Debt securities				
Principal		19,086,046	0	
Unamortized premium		492,388	0	
Net debt securities held-to-maturity		<u>19,578,434</u>	<u>0</u>	
b) Movement in investment securities held-to-maturity:				
Balance at beginning of year		0	0	
Purchases		19,625,628	0	
Amortized premium		(47,194)	0	
Balance at end of the year		<u>19,578,434</u>	<u>0</u>	
<b>19. Investment properties</b>				
	Land & Building	Furniture & Fittings	Plant & Equipment	Total
a) Cost				
Balance at beginning of year	11,241,297	249,334	192,220	11,682,851
Revaluation decrement	(4,037,509)	-	-	(4,037,509)
Additions	66,602	5,994	12,989	85,585
Disposals	(420,000)	(5,846)	(11,928)	(437,774)
Balance at end of year	<u>6,850,390</u>	<u>249,482</u>	<u>193,281</u>	<u>7,293,153</u>

## Notes to and forming part of the financial statements

## b) Accumulated depreciation

Balance at beginning of year	0	(131,376)	(101,354)	232,730
Charged during year (note 3)	0	(12,932)	(13,438)	(26,370)
Disposals	0	658	6,419	7,077
Balance at end of year	0	(143,650)	(108,373)	(252,023)
Book value 31 December 2004	6,850,390	105,832	84,908	7,041,130
Book value 31 December 2003	11,241,297	117,958	90,866	11,450,121

## c) Movement in specific allowance for losses:

The provision of K5.4 million represents the carrying value of the investment in Sandaun Motel. Movements in specific allowance for losses are as follows:

	Note	2004 Kina	2003 Kina
Balance at beginning of year		5,407,742	4,000,000
Impairment losses during the year	7	0	1,407,742
Balance at end of the year		5,407,742	5,407,742

## 20. Property and equipment

	Motor Vehicle	Furniture & fittings	Office equipment	Renovation	Computer Software	Total
a) Cost						
Balance at beginning of year	113,250	534,181	308,913	223,508	19,180	1,199,032
Additions	18,182	1,003	91,011	17,223	10,037	137,456
Disposal	(113,250)	0	0	0	0	(113,250)
Balance at end of year	18,182	535,184	399,924	240,731	29,217	1,223,238
b) Accumulated depreciation						
Balance at beginning	(113,250)	(209,208)	(228,363)	(19,418)	(320)	(570,759)
Charged during year	(4,545)	(80,152)	(34,974)	(22,351)	(8,014)	(150,036)
Disposal	(113,250)	0	0	0	0	(113,250)
Balance at end of year	(4,545)	(289,560)	(263,337)	(41,769)	(8,334)	(607,545)
Book value 31 Dec 2004	13,637	245,624	136,587	198,962	20,883	615,693
Book value 31 Dec 2003	0	324,773	80,550	204,090	18,860	628,273



## Notes to and forming part of the financial statements

	Note	2004 Kina	2003 Kina
<b>21. Other assets</b>			
a) Other assets			
Prepayments		51,178	9,963
Advances			
- Individual		2,387	2,387
- Corporate		994,996	822,620
Security deposit		46,944	43,710
Accrued interest			
- Treasury bills		25,040	980,911
- Due from other banks		14,396	132,231
- Loans		434,722	435,560
- Investment securities		250,860	0
Others		495,944	343,123
Total		2,316,467	2,770,505
Less specific allowance for losses		(864,084)	(232,978)
		<u>1,452,383</u>	<u>2,537,527</u>
		=====	=====
b) Movement in specific allowance for losses:			
Balance at beginning of year		232,978	0
Impairment losses during the year :-			
-Interest	8	434,722	232,978
-Advance	3	196,384	0
		<u>864,084</u>	<u>232,978</u>
		=====	=====
<b>22. Other liabilities</b>			
Creditors		132,775	115,767
Retrenchment benefits due		1,782,724	736,139
Accruals		382,261	104,006
		<u>2,297,760</u>	<u>955,912</u>
		=====	=====
<b>23. Cash and cash equivalent</b>			
For purposes of the cash flow statement, cash and cash equivalents comprise of the following:			
Cash and due for other banks	13	5,769,498	6,425,247
Treasury bills	14	18,620,587	17,696,361
		<u>24,390,085</u>	<u>24,121,608</u>
		=====	=====

## Notes to and forming part of the financial statements

### 24. Related party transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

- a) During the year, the Fund earned interest on term deposits amounting to K156,401 (2003 – K348,730) from Kina Finance Limited, a finance company in which Kina Securities Limited and the Fund's Investment Manager, Kina Funds Management Limited are related. As at 31 December 2004, the term deposit placed with Kina Finance Limited was K836,989 (2003 – K2,480,000) and these transactions were carried out on commercial terms and market rates.
- b) At 31 December 2004, POSF Limited (trustee for Public Officers Superannuation Fund) owed K313,363 (2003 – K162,247).
- c) At 31 December 2004, Hunter Limited owed this Fund K1,338,284 (K1,345,276) comprising of:

	Note	2004 Kina	2003 Kina
Unsecured loan		1,124,722	1,125,560
Expenses paid on behalf of Hunter Ltd		213,562	219,716
		<u>1,338,284</u>	<u>1,345,276</u>
		=====	=====

The Fund owns 70% of Hunter Limited. Uncollected interest accrued on impaired loans of K690,000 amounted to K434,722 (2003 – K435,560) at 31 December 2004.

- d) At 31 December 2004, Banora Trading Limited owed the Fund K190,306 (K195,279).

### 25. Financial risk management

The Fund's strategy focuses on two primary objectives: to maximize long term fund returns and to manage and control business and investment risks. This strategy inherently requires the Fund to pursue a balanced investment strategy which seeks capital growth over the medium to long term with moderate income streams.

All investments undertaken must balance risk against returns. In other words, the investment strategy pursued must determine a mix of growth and defensive assets that best suits the needs of the members.

The trustees can achieve better returns through disciplined application of a good investment process, one that is based on the analysis of investment fundamentals followed by an assessment of relative value.

The Fund is exposed to liquidity risk, interest rate risk, foreign exchange risk, credit risk and sovereign and country risk.

- a) Liquidity risk

The Fund invests the majority of its assets in investments that are traded in an active market and can be readily be disposed of.

The Fund's listed securities are considered readily realizable, as they are listed on the Port Moresby Stock Exchange and the Australian Stock Exchange.

The liabilities of the Fund are long term in nature and are well structured in terms of benefits comprising of a mix of pension commutation and a fortnightly pension payable throughout the lifetime of the member.



Notes to and forming part of the financial statements

b) Interest rate risk

The Fund is exposed to risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows.

The table below summarizes the Fund's exposures to interest rate risks. It includes the Fund's assets and liabilities at fair market values, categorized by the earlier of contractual re-pricing or maturity dates:

	Up to 1 Year K	1 – 5 Years K	Non Over 5 Years K	Interest Bearing K	Total K
<b>31 December 2004</b>					
<b>Assets</b>					
- Cash and due from other banks	6,549,498	0	0	0	6,549,498
- Treasury bills	19,598,687	0	0	0	19,598,687
- Loans to members and others	577,442	5,939,751	937,547	0	7,454,740
- Deferred income tax assets	0	0	0	146,768	146,768
- Investment securities					
• Available-for-sale	0	589,000	0	51,996,315	52,585,315
• Held-to-maturity	0	19,578,434	0	0	19,578,434
- Investment properties	0	0	0	7,041,130	7,041,130
- Property and equipment	0	0	0	615,693	615,693
- Other assets	0	0	0	1,452,383	1,452,383
	<u>26,725,627</u>	<u>26,107,185</u>	<u>937,547</u>	<u>61,252,289</u>	<u>115,022,648</u>
<b>Liabilities</b>					
Current income tax payable	0	0	0	(490,703)	(490,703)
Other liabilities	0	0	0	(2,297,760)	(2,297,760)
	<u>0</u>	<u>0</u>	<u>0</u>	<u>(2,788,463)</u>	<u>(2,788,463)</u>
Interest sensitivity gap	<u>26,725,627</u>	<u>26,107,185</u>	<u>937,547</u>	<u>58,463,826</u>	<u>112,234,118</u>
<b>31 December 2003</b>					
<b>Assets</b>					
-Cash and due from other banks	6,425,247	0	0	0	6,425,247
-Treasury bills	31,535,262	0	0	0	31,535,262
-Loans to members and others	4,222,588	6,100,000	2,066,754	0	12,389,342
-Investment securities					
• Available-for-sale	0	0	0	38,048,968	38,048,968
• Held-to-maturity	0	0	0	0	0
- Investment properties	0	0	0	11,450,121	11,450,121
-Property and equipment	0	0	0	628,273	628,273
-Other assets	0	0	0	2,537,527	2,537,527
	<u>42,183,097</u>	<u>6,100,000</u>	<u>2,066,754</u>	<u>52,664,889</u>	<u>103,014,740</u>
<b>Liabilities</b>					
Current income tax payable	0	0	0	(78,018)	(78,018)
Deferred income tax liabilities	0	0	0	(280,908)	(280,908)
Other liabilities	0	0	0	(955,912)	(955,912)
	<u>0</u>	<u>0</u>	<u>0</u>	<u>(1,314,838)</u>	<u>(1,314,838)</u>
Interest sensitivity gap	<u>42,183,097</u>	<u>6,100,000</u>	<u>2,066,754</u>	<u>51,350,051</u>	<u>101,699,902</u>

## Notes to and forming part of the financial statements

## c) Foreign exchange risk

The Fund holds assets denominated in currencies other than Kina, the functional currency. The Fund is therefore exposed to currency risk, as the value of the securities and the dividends earned denominated in other currencies will fluctuate due to changes in exchange rates.

The table below summarizes the Fund's exposure to currency risks, concentration of assets and liabilities.

	Kina K	\$AUD K	Total K
<b>31 December 2004</b>			
<b>Assets</b>			
- Cash and due from other banks	3,317,143	3,232,355	6,549,498
- Treasury bills	19,598,687	0	19,598,687
- Loans to members and others	7,454,740	0	7,454,740
- Deferred income tax assets	146,768	0	146,768
- Investment securities			
• Available-for-sale	42,066,255	10,519,060	52,585,315
• Held-to-maturity	19,578,434	0	19,578,434
- Investment properties	5,865,501	1,175,629	7,041,130
- Property and equipment	615,693	0	615,693
- Other assets	1,452,383	0	1,452,383
	<u>100,095,604</u>	<u>14,927,044</u>	<u>115,022,648</u>
<b>Liabilities</b>			
Current income tax payable	(490,703)	0	(490,703)
Other liabilities	(2,297,760)	0	(2,297,760)
	<u>(2,788,463)</u>	<u>0</u>	<u>(2,788,463)</u>
<b>Net assets</b>	<u>97,307,141</u>	<u>14,927,044</u>	<u>112,234,185</u>
	=====	=====	=====
<b>31 December 2003</b>			
<b>Assets</b>			
- Cash and due from other banks	6,425,247	0	6,425,247
- Treasury bills	31,535,262	0	31,535,262
- Loans to members and others	12,389,342	0	12,389,342
- Investment securities			
• Available-for-sale	31,679,717	6,369,251	38,048,968
• Held-to-maturity	0	0	0
- Investment properties	10,727,845	722,276	11,450,121
- Property and equipment	628,273	0	628,273
- Other assets	2,537,527	0	2,537,527
	<u>95,923,213</u>	<u>7,091,527</u>	<u>103,014,740</u>
<b>Liabilities</b>			
Current income tax payable	(78,018)	0	(78,018)
Deferred income tax liabilities	(280,908)	0	(280,908)
Other liabilities	(955,912)	0	(955,912)
	<u>(1,314,838)</u>	<u>0</u>	<u>(1,314,838)</u>
<b>Net assets</b>	<u>94,608,375</u>	<u>7,091,527</u>	<u>101,699,902</u>
	=====	=====	=====

## d) Credit risk

The Fund is exposed to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment provisions are provided for losses that have been incurred by the balance sheet date, if any.



## Notes to and forming part of the financial statements

Assets	2004		2003	
	Kina	%	Kina	%
Cash and due from other banks	6,549,498	6	6,425,247	6
Treasury bills	19,598,687	17	31,535,262	32
Loans to members and others	7,454,740	7	12,389,343	12
Investment securities available-for-sale	52,585,315	47	38,048,968	38
Investment securities held-to-maturity	19,578,343	17	0	0
Investment properties	7,041,130	6	11,450,121	12
Total	112,807,804	100	99,848,941	100

The asset allocation range defines the high and low extremes within which each asset class may move in response to changing economic conditions. By approving an asset allocation range, the trustees still maintain ultimate control over investment policy at the macro level while the Investment Manager is given the flexibility needed at operational level to quickly respond to and take advantage of changing economic situations without the need to continuously revert back to the trustees for approval.

The investment manager shall manage and implement the investment strategy in accordance with the investment policy guidelines approved by the trustees and where such proposals are viable and are consistent with prudential standards issued by the Bank of Papua New Guinea.

## e) Sovereign risk

There is a history of protracted delays in government payments therefore the Fund is exposed to such risks through its large holding of government securities.

## f) Country risk

To the extent that the Fund holds assets in foreign jurisdictions, a variety of risks arise in addition to foreign exchange risks – such as changes in local economic conditions, local regulatory requirements or non-transparent governance arrangements.

## g) Fair value of financial assets and liabilities

The following table summaries the carrying amounts and fair values of those financial assets and liabilities not presented on the company's balance sheet at their fair value. Bid prices are used to estimate fair values of assets, whereas offer prices are applied for liabilities.

Assets	Carrying Value		Fair Value	
	2004	2003	2004	2003
Cash and due from other banks <sup>1</sup>	6,469,968	6,425,247	6,549,498	6,425,247
Treasury bills	19,598,687	31,535,262	19,598,687	31,535,262
Loans to members and others <sup>2</sup>	7,454,740	12,389,342	7,454,768	12,389,342
Deferred income tax assets	146,768	0	146,768	0
Investment securities available-for-sale <sup>3</sup>	19,609,225	5,852,749	52,585,315	38,048,968
Investment securities held-to-maturity <sup>3</sup>	19,578,343	0	19,578,434	0
Investment properties	11,078,643	11,450,121	7,041,130	11,450,121
Property and equipment	615,693	628,273	615,693	628,273
Other assets	1,452,383	2,537,527	1,452,383	2,537,527
Total	86,004,541	80,818,521	115,022,648	103,014,740

1 Cash and due from other banks

Cash and due from other banks includes inter-bank placements and items in the course of collection. The fair values of floating rate placements and overnight deposits are shown at their carrying amounts.

2 Loans and advances to customers (Note 16)

Loans and advances are net of losses.

3 Investment securities (Note 17)

In 2004, investment securities include assets available-for-sale and held-to-maturity which are now measured at fair value based on market price or broker/dealer price quotations.

26. Other

a) Actuarial report

Actuarial evaluation of the Fund is currently being undertaken by Financial Synergy Limited of Melbourne, Australia. As at the date of this report, Financial Synergy has not finalized the actuarial evaluation for the three years ended 31 December 2004.





# Corporate Directory

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## SENIOR MANAGEMENT

George B. Uware – Chief Executive Officer  
Richard Sinamoi – General Manager

## Notes







