

CENTRAL BANK OF SOLOMON ISLANDS
Financial Market Supervision Department

Prudential Guideline No. 3
On Foreign Currency Open Positions

Applicability

1. This Prudential Guideline is applicable to all financial institutions licensed by the Central Bank of Solomon Islands (CBSI).

Purpose of Prudential Guideline

2. The purpose of this Prudential Guideline is to (i) assure that foreign currency positions are maintained within prudent limits to avoid excessive risk of loss to a financial institution's capital as a result of fluctuations in foreign currency prices, (ii) promote maximum availability of foreign exchange at competitive rates; and (iii) allow financial institutions to conduct business in a profitable yet prudent manner.
3. The board of directors of each financial institution are responsible for ensuring compliance with the requirements of this Prudential Guideline and for establishing an appropriate policy to limit the amount of risk to the financial institution resulting from transactions in foreign currencies. The open foreign currency limits provided in this Prudential Guideline are the maximum acceptable levels for financial institutions which are fundamentally sound, well-managed and which have no material financial or operational weaknesses.
4. The CBSI may require a financial institution to reduce its open foreign currency positions if the financial institution has inadequate risk management systems to measure, monitor and control foreign exchange risk, or has less than satisfactory capital, asset quality, management, earnings, or liquidity.

Definitions

5. As used in this Prudential Guideline the following terms, unless otherwise clearly indicated by the context, have the meanings specified below:
6. **“Total Capital”** means total capital as reported in the CBSI Financial Institutions Prudential Return, Form 1, Balance Sheet.
7. **“Foreign currency”** means a currency other than the Solomon Islands Dollar (SBD).
8. **“Intra day”** means between the opening of any business day until the close of business that same day.
9. **“Open foreign currency position”** means an excess of assets (including off-balance sheet forward purchase contracts) over liabilities (including off-balance sheet forward sales contracts) (a “long position”) held by a financial institution denominated a foreign currency, or an excess of liabilities (including off-balance sheet forward sales contracts) over assets (including off-balance sheet forward purchase contracts) (a “short position”)

held by a financial institution denominated a foreign currency.

10. “**Overall open foreign currency position**” means the greater of the SBD equivalent of the total “long positions” or SBD equivalent of the total “short positions” held by a financial institution in all foreign currencies.

Foreign Currency Open Position Limits

11. No financial institution shall permit to be outstanding as of the close of any business day:
 - (a) an open foreign currency position of more than fifteen percent (15%) of the financial institution’s Total Capital, after deductions, in any single foreign currency; and
 - (b) an overall open foreign currency position of more than twenty-five percent (25%) of the financial institution’s Total Capital after deductions.
12. A financial institution’s intra day open foreign currency positions (that is in any single foreign currency as well as the overall open foreign currency position) shall be monitored and maintained within prudent limits which shall be established by the each financial institution’s board of directors in a written policy covering foreign exchange operations and transactions.

Computation of Foreign Currency Positions

13. Each financial institution which holds assets (including off-balance sheet forward purchase contracts) or liabilities (including off-balance sheet forward sales contracts), denominated in foreign currencies shall calculate its open foreign currency position in each foreign currency and its overall open foreign currency position as of the close of each business day.
14. The open foreign currency position in each currency shall be computed as of the close of business each day in the following manner:
 - (a) the difference between assets (including off-balance sheet forward purchase contracts) and liabilities (including off-balance sheet forward sales contracts) denominated in each foreign currency shall be calculated and categorised as either a long position or a short position;
 - (b) the open foreign currency position (that is, the long position or short position) in each foreign currency shall be converted into a SBD equivalent by multiplying the long or short open position of that foreign currency by the spot mid-rate;
 - (c) the SBD equivalent for each open foreign currency position shall be divided by the financial institution’s Total Capital for the most recent calendar month-end.
15. A financial institution’s compliance with the overall open foreign currency position shall be determined by adding separately all short positions and all long positions, comparing the two totals, taking the larger of the two totals as the overall open foreign currency position as a percentage of the financial institution’s Total Capital.

Reporting Requirements

16. Each financial institution which holds assets (including off-balance sheet forward

purchase contracts) or liabilities (including off-balance sheet forward sales contracts) denominated in foreign currencies shall submit to the CBSI a Report on Single and Overall Open Foreign Currency by not later than 20 days following the end of each calendar month. The Report shall be in such format and shall be prepared in accordance with written instructions as may be issued from time to time by the CBSI.

Responsibilities of the Board of Directors

17. The board of directors of each financial institution shall ensure that accounting systems and internal controls are in place to provide accurate and current information on all foreign exchange activities and are sufficient to ensure compliance with the requirements of the Prudential Guideline.

Record-keeping Requirements

18. Each financial institution shall **maintain a daily record** showing the close-of-business open foreign currency position for each foreign currency in which the financial institution holds assets or liabilities denominated and the financial institution's overall open foreign currency position. Each financial institution shall preserve every such record for a period of at least seven (7) years and such information shall be made available to the Central Bank of Solomon Islands or examining personnel of the Financial Market Supervision Department upon request.

Enforcement and Corrective Measures

19. A financial institution which fails to comply with the requirements contained in this Prudential Guideline or submits reports to the CBSI which are materially inaccurate will be considered as following unsound and unsafe practices as provided in Section 16 (1) (a) of the Financial Institutions Act 1998.
20. A financial institution shall immediately notify the CBSI in writing of and take action to correct any foreign currency open position which exceeds the limits outlined in this Prudential Guideline.
21. The CBSI may pursue any or all corrective measures as provided in Section 16 of the Financial Institutions Act 1998, including:
 - (a) issuance of an order to cease and desist from the unsound and unsafe practices and
 - (b) action to replace or strengthen the management of the financial institution.

Effective Date

22. The effective date of this Prudential Guideline is 1 January 2010.

Issued this *4th* day of *September*, 2009

Governor Denton Rarawa
Central Bank of Solomon Islands