

CENTRAL BANK OF IRAQ

Financial Statements

31 December 2012

(With Independent auditors' report Thereon)

CENTRAL BANK OF IRAQ

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Independent auditors' report

To the Ministry of Finance of Iraq and to the Governor of the Central Bank of Iraq (CBI)

We have audited the accompanying financial statements of Central Bank of Iraq (CBI), which comprise the statement of financial position as at 31 December 2012 and the statements of comprehensive income, changes in equity, and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

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

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the 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 financial statements.

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



Independent auditors' report (continued)

Basis for Qualified Opinion


- 1 As further explained in note (8) to the financial statements, the CBI's financial statements as at 31 December 2012 include old outstanding balances at foreign banks in the amount of IQD 1,736,474 million (2011: IQD 1,750,279 million) which are fully provided for as at 31 December 2012 and 2011. In addition, during the years 2005, 2006 and 2007 the CBI wrote off balances at foreign banks totaling IQD 1,071,942 million. The provided for and the written off accounts include an amount of IQD 401,310 million as at 31 December 2012 (2011: IQD 401,310 million) that have been transferred from certain foreign banks to the Development Fund for Iraq (DFI) account as required by the United Nations Security Council Resolution (UNSCR) 1483 (2003). The Ministry of Finance (MOF) has not returned the funds to the CBI although a resolution has been issued by the Council of Ministers ordering the return of the funds to the CBI. During 2012, a letter was sent to the Council of Ministers again requesting the return of these funds from the MOF.
- 2 As further discussed in note (28) to the financial statements, there are lawsuits in different countries against the CBI for the settlement of past due debts of the CBI and other Iraqi governmental institutions amounting to IQD 859,955 million (2011: IQD 837,591 million). The final outcome of these lawsuits and the effects on the CBI's financial statements as at 31 December 2012, if any, is uncertain and has not been quantified and provided for. We did not receive confirmations from the CBI's legal advisors and due to the unavailability of sufficient information we could not extend our audit procedures to ensure the completeness of these lawsuits and their effect on the financial statements as at 31 December 2012, if any.
- 3 We did not receive confirmations and reconciliations for the due to foreign banks and overdraft accounts at the CBI, disclosed in note (17) to the financial statements amounting to IQD 18,216 million (2011: IQD 73,119 million). We could not extend our audit procedures to ensure the completeness and accuracy of these balances as at 31 December 2012.

Qualified Opinion

In our opinion, except for the possible effects of the matters described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2012, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of a Matter

As further explained in note (1) to the financial statements, currently the CBI does not control the financial and administrative affairs of its Erbil and Sulaimaniyah branches, as these branches are technically related to CBI, while for all other matters they are related to Kurdistan Regional Government (KRG) and their operations are financed by KRG. In addition, the CBI did not receive the financial statements of its branches in Sulaimaniyah and Erbil and does not have access to their accounting records. Therefore, the accompanying financial statements do not include the financial statements of Sulaimaniyah and Erbil branches. The CBI does not have any information to quantify the significance of the branches financial statements and its effect on the CBI's financial statements as at 31 December 2012.


Baghdad - Iraq
8 August 2013

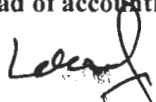
Central Bank of Iraq
Statement of financial position
As at 31 December

<i>In millions of IQD</i>	Note	2012	2011
Assets			
Gold reserve	6	1,860,236	348,808
Cash and balances with central banks	7	14,302,088	9,592,454
Balances with banks	8	10,469,338	11,955,411
Held to maturity investment securities	9	50,773,153	46,393,941
Due from Ministry of Finance	10	3,155,520	3,561,542
Foreign currencies investments at International Monetary Fund	11	4,140,272	4,161,675
Property and equipment	15	119,746	86,489
Other assets	12	421,854	440,977
Total Assets		85,242,207	76,541,297
Liabilities and equity			
Liabilities			
Currency issued	13	35,784,805	32,157,444
Treasury bills issued	14	745,471	496,092
Deposits of local and governmental banks	16	34,790,945	32,484,380
Due to foreign governments and banks	17	22,471	77,302
Due to International Monetary Fund	18	3,870,733	3,959,098
Balances due to governmental institutions	19	6,857,796	6,286,754
Other liabilities	20	36,762	38,294
Total liabilities		82,108,983	75,499,364
Equity			
Capital	21	100,000	100,000
General reserve	21	474,511	-
Emergency reserve	21	118,628	-
Gold revaluation reserve	21	446,794	348,793
Retained earnings	21	1,993,291	593,140
Total equity		3,133,224	1,041,933
Total liabilities and equity		85,242,207	76,541,297

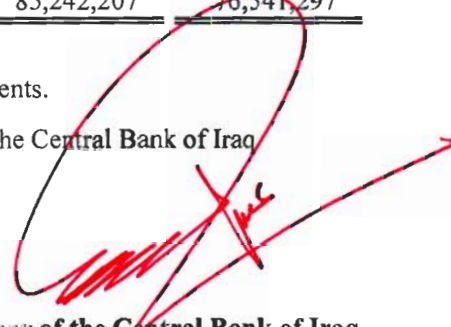
The notes on pages 7 to 36 are an integral part of these financial statements.

The financial statements were authorized for issue by the Governor of the Central Bank of Iraq on 8 August 2013.

Head of accounting department



Governor of the Central Bank of Iraq



Central Bank of Iraq

Statement of comprehensive income

For the year ended 31 December

<i>In millions of IQD</i>	Note	2012	2011
Revenues			
Interest income	22	552,120	531,621
Interest expense	23	(184,468)	(144,144)
Net interest income		367,652	387,477
Net fee and commission income	24	1,303,959	1,103,794
Gold revaluation gain	21	98,001	37,197
Gain (loss) on translation of foreign currency		328,703	(871,179)
Effect of derecognition of foreign creditors balances	17	54,858	168,954
Other income		8,308	73,393
Profit from operations		2,161,481	899,636
Personnel expenses		(29,369)	(28,228)
Depreciation		(2,460)	(2,069)
General and administrative expenses		(38,361)	(24,463)
Profit for the year		2,091,291	844,876
Total comprehensive income for the year		2,091,291	844,876

The notes on pages 7 to 36 are an integral part of these financial statements.

Central Bank of Iraq
Statement of changes in equity
For the year ended 31 December

In millions of IQD

	Notes	Capital	General reserve	Emergency reserve	Gold revaluation reserve	(Accumulated losses) retained earnings	Total
Balance at 1 January 2011		100,000	803,173	200,268	311,596	(1,217,980)	197,057
Total comprehensive income for the year							
Profit for the year		–	–	–	–	844,876	844,876
Total comprehensive income for the year		–	–	–	–	844,876	844,876
Transfers							
Transfer to general reserve	21	–	(803,173)	–	–	803,173	–
Transfer to emergency reserve	21	–	–	(200,268)	–	200,268	–
Gold revaluation reserve for the year	21	–	–	–	37,197	(37,197)	–
Total transfers		–	(803,173)	(200,268)	37,197	966,244	–
Balance at 31 December 2011		100,000	–	–	348,793	593,140	1,041,933
Balance at 1 January 2012		100,000	–	–	348,793	593,140	1,041,933
Total comprehensive income for the year							
Profit for the year		–	–	–	–	2,091,291	2,091,291
Total comprehensive income for the year		–	–	–	–	2,091,291	2,091,291
Transfers							
Transfer to general reserve	21	–	474,511	–	–	(474,511)	–
Transfer to emergency reserve	21	–	–	118,628	–	(118,628)	–
Gold revaluation reserve for the year	21	–	–	–	98,001	(98,001)	–
Total transfers		–	474,511	118,628	98,001	(691,140)	–
Balance at 31 December 2012		100,000	474,511	118,628	446,794	1,993,291	3,133,224

The notes on pages 7 to 36 are an integral part of these financial statements.

Central Bank of Iraq

Statement of cash flows

For the year ended 31 December

<i>In millions of IQD</i>	Notes	2012	2011
Cash flows from operating activities			
Profit for the year		2,091,291	844,876
Adjustments for:			
Effect of derecognition of foreign creditors balances	17	(54,858)	(168,954)
Depreciation	15	2,460	2,069
Revaluation of gold reserve	21	(98,001)	(37,197)
		<u>1,940,892</u>	<u>640,794</u>
Change in due from Ministry of Finance	10	406,022	407,548
Change in other assets	12	19,123	(8,707)
Change in currency issued	13	3,627,361	4,650,116
Change in deposits of local and governmental banks	16	2,306,565	1,867,168
Change in due to foreign governments and banks	17	27	2,559
Change in due to International Monetary Fund	18	(88,365)	117,883
Change in balances due to governmental institutions	19	571,042	4,140,063
Change in other liabilities	20	(1,532)	(24,875)
Net cash flows from operating activities		<u>8,781,135</u>	<u>11,792,549</u>
Cash flows from investing activities			
Held to maturity investment securities	9	(4,379,212)	(10,579,895)
Foreign currencies investments at IMF	11	21,403	55,018
Purchase of property and equipment	15	(35,717)	(5,284)
Purchase of gold		(1,413,427)	–
Proceeds from disposal of property and equipment		–	2,952
Net cash flows used in investing activities		<u>(5,806,953)</u>	<u>(10,527,209)</u>
Cash flows from financing activities			
Treasury bills issued	14	249,379	99,593
Net cash flows from financing activities		<u>249,379</u>	<u>99,593</u>
Net increase in cash and cash equivalents		3,223,561	1,364,933
Cash and cash equivalents as at 1 January		21,547,865	20,182,932
Cash and cash equivalents as at 31 December	25	<u>24,771,426</u>	<u>21,547,865</u>

The notes on pages 7 to 36 are an integral part of these financial statements.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(1) Activities

The Central Bank of Iraq ("CBI" - also referred to in these financial statements as "the Bank") is a governmental entity that was established under the Central Bank of Iraq Law Number 43 of 1947 as amended, and carrying out its activities under the Central Bank Law of 2004 issued by the Coalition Provisional Authority Order Number 56.

The primary objectives of the CBI are to achieve and maintain domestic price stability and to foster and maintain a stable and competitive market-based financial system. Subject to these objectives, the CBI shall promote sustainable growth, employment and prosperity in Iraq.

In accordance with the Central Bank Law, the main functions of the CBI for achieving its objectives include the following:

- a. Formulate and implement monetary policy, including exchange rate policy.
- b. Hold and manage all official foreign reserves of Iraq, other than working balances of the Government of Iraq.
- c. Hold gold and manage the Government of Iraq reserves of gold.
- d. Provide liquidity services to banks.
- e. Issue and manage Iraqi currency.
- f. Establish, oversee and promote sound and efficient payment systems.
- g. Issue licenses or permits to banks and to regulate and supervise banks.

The CBI's head office is located in Baghdad with four branches in Basrah, Mosul, Erbil and Sulaimaniyah. However, currently the CBI does not control the financial and administrative affairs of Erbil and Sulaimaniyah branches, as these branches are technically related to CBI, while for all other issues they are related to Kurdistan Regional Government (KRG) and they are financed by KRG.

As a result, the CBI does not have access to the accounting records of its Erbil and Sulaimaniyah branches. Therefore, the accompanying financial statements do not include the financial statements of Sulaimaniyah and Erbil branches. The CBI does not have any information to quantify the significance of the branches financial statements and its effect on the CBI's financial statements as at 31 December 2011 and 2012.

(2) Basis of preparation

a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) .

b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for the gold which is measured at fair value.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(2) Basis of preparation (continued)

c) Functional and presentation currency

The financial statements are presented in Iraqi Dinar (IQD), which is the Bank's functional currency. All financial information presented in IQD has been rounded to the nearest million.

d) Use of estimates and judgements

The preparation of the financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future years affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognized in the financial statements are described in notes 4 and 5.

(3) Significant accounting policies

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

a) Foreign currency

Transactions in foreign currencies are translated to the functional currency of the Bank at the spot exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in foreign currency translated at the spot exchange rate at the end of the year. Foreign currency differences arising on retranslation are recognized in profit or loss. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

b) Gold

Gold is stated on the basis of the closing price in London gold market (USD 1,664 per ounce) as at 31 December 2012. The CBI maintains the gold as part of its foreign reserve management and does not have a present intent to dispose of it. The gains or losses on the revaluation of gold at market prices are recorded in the statement of comprehensive income. The cumulative gain on the gold revaluation is then transferred to a special reserve account and is disclosed in a separate component in equity.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) Significant accounting policies (continued)

c) Financial assets and liabilities

Recognition

The Bank initially recognizes loans, deposits and debt securities on the date that they are originated. All other financial assets and liabilities are initially recognized on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

Derecognition

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognized as a separate asset or liability in the statement of financial position. On derecognition of a financial asset, the difference between the carrying amount of the asset, and the sum of (1) the consideration received (including any new asset obtained less any new liability assumed) and (2) any cumulative gain or loss that had been recognized in other comprehensive income is recognized in profit or loss.

In transactions in which the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Bank retains obligation to service the transferred financial asset for a fee. The transferred asset is derecognized if it meets the derecognition criteria. An asset or liability is recognized for the servicing contract, depending on whether the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

The Bank derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

Offsetting

Financial assets and liabilities are offset and the net amount is presented in the statement of financial position when, and only when, the Bank has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activities.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) **Significant accounting policies (continued)**

c) **Financial assets and liabilities (continued)**

Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognized and the maturity amount, minus any reduction for impairment.

Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank establishes fair value using a valuation technique. Valuation techniques include using arm's length transactions between knowledgeable, willing parties (if reference), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analysis and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates related to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument.

The best evidence of the fair value of a financial instruments at initial recognition is the transaction price, i.e. the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instruments is initially measured at the transition price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in profit or loss on an appropriate basis over the life of the instrument but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Any difference between the fair value at initial recognition and the amount that would be determined at that date using a valuation technique in a situation in which the valuation is dependent on unobservable parameters is not recognised in profit or loss immediately but is recognised over the life of the instrument on an appropriate basis or when the instrument is redeemed, transferred or sold, or the fair value becomes observable.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) Significant accounting policies (continued)

c) Financial assets and liabilities (continued)

Identification and measurement of impairment

At each reporting date, the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A Financial asset or a group of financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows on the asset(s) that can be estimated reliably.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Impairment losses are recognized in profit or loss and reflected in an allowance account against loans and advances. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

d) Investment securities

Investment securities are initially measured at fair value plus, in case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as either held to maturity, fair value through profit or loss, or available for sale.

All the Bank's investment securities are classified as held to maturity.

Held-to-maturity

Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity, and which are not designated as at fair value through profit or loss or as available for sale.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) Significant accounting policies (continued)

d) Investment securities (continued)

Held-to-maturity(continued)

Held-to-maturity investments are carried at amortised cost using the effective interest method. A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available for sale, and would prevent the Bank from classifying investment securities as held to maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- Sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;
- Sales or reclassifications after the Bank has collected substantially all of the asset's original principal; and
- Sales or reclassifications attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

e) Loans and due from banks

Loans and due from banks are financial assets with fixed or determinable payments that are not quoted in an active market or classified as financial assets held for sale or for trading or financial assets designated at fair value through profit or loss. After initial measurement, loans and amounts due from banks are subsequently measured at amortised cost using the effective interest method, less allowance for impairment. The amortisation is included in 'Interest and similar income' in the income statement. The losses arising from impairment are recognized in the income statement as credit loss expenses.

f) Interest

Interest income and expense are recognized in the profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument.

Interest income and expense presented in the statement of the comprehensive income include:

- Interest on treasury bills and bonds,
- Interest on due from banks and due from Ministry of Finance,
- Interest on treasury bills issued.

g) Fees and commissions

Fees and commission income, including account servicing fees, investment management fees, sales commission, placement fees and other finance fees on loans are recognized as the related services are performed.

Fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) Significant accounting policies (continued)

h) Recognition of income

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured.

i) Local banks reserves and deposits

All local banks reserves and deposits are carried at cost less amounts repaid.

j) Due to foreign governments and banks

All due to foreign governments and banks balances are carried at cost less amounts repaid.

k) Cash and cash equivalents

Cash and cash equivalents include cash on hand and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

l) Property and equipment

Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Gains and losses on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognized net in profit or loss.

Subsequent costs

The cost of replacing a part of an item of property or equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in profit or loss as incurred.

Depreciation

Depreciation is based on the cost of an asset less its residual value. Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. Land is not depreciated.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) Significant accounting policies (continued)

l) Property and equipment (continued)

Depreciation (continued)

The estimated useful lives for the current and comparative years are as follows:

- Buildings 20 years
- Vehicles 5 years
- Furniture and other equipment 3 – 5 years

Depreciation methods, useful lives and residual values are reassessed at each financial year-end and adjusted if appropriate.

m) Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognized if the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of an asset is the greater of its value in use and its fair value less cost to sell. Impairment losses are recognized in profit or loss.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

n) Provisions

A provision is recognized if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by using management best estimates to the risk specific to the liability.

o) Fiduciary assets

Assets held in a fiduciary capacity are not reported in the financial statements, as they are not the assets of the Bank.

p) Issued currency

The liability of the CBI towards banknotes issued as a legal tender in Iraq under the CBI Law of year 2004 is stated at the face value. The issued banknotes that are returned to the CBI are reduced from the issued currency balance. Any un-issued and returned banknotes kept in the CBI vaults are not reflected in the financial statements. The cost of printing the banknotes is recorded in the income statement when incurred.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(3) Significant accounting policies (continued)

q) Taxes

According to Article 44 of the Central Bank Law of 2004, the CBI is exempted from taxes on income or profit and certain other taxes and customs as stated in the Law.

r) Treasury bills issued

Subsequent to initial recognition, treasury bills issued are measured at their amortized cost using the effective interest method.

s) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2012, and have not been applied in preparing these financial statements. None of these will have a significant effect on the financial statements of the Bank.

(i) IFRS 9 *Financial instruments* (2010) and IFRS 9 *Financial instruments* (2009)

IFRS 9 (2009) introduces new requirements for the classification and measurement of financial assets. IFRS 9 (2010) introduces additions relating to financial liabilities. The IASB currently has an active project to make limited amendments to the classification and measurement requirements of IFRS 9 and add new requirements to address the impairment of financial assets and hedge accounting.

The IFRS 9 (2009) requirements represent a significant change from the existing requirements in IAS 39 in respect of financial assets. The standard contains two primary measurement categories for financial assets: amortized cost and fair value. A financial asset would be measured at amortized cost if it is held within a business model whose objective is to hold assets in order to collect contractual cash flows, and the asset's contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding. All other financial assets would be measured at fair value. The standard eliminates the existing IAS 39 categories of held to maturity, available-for-sale and loans and receivables. For an investment in an equity instrument which is not held for trading, the standard permits an irrevocable election, on initial recognition, on an individual share-by-share basis, to present all fair value changes from the investment in other comprehensive income. No amount recognized in other comprehensive income would ever be reclassified to profit or loss at a later date. However, dividends on such investments are recognized in profit or loss, rather than other comprehensive income unless they clearly represent a partial recovery of the cost of the investment. Investments in equity instruments in respect of which an entity does not elect to present fair value changes in other comprehensive income would be measured at fair value with changes in fair value recognized in profit or loss.

IFRS 9 (2010) introduces a new requirement in respect of financial liabilities designated under the fair value option to generally present fair value changes that are attributable to the liability's credit risk in other comprehensive income rather than in profit or loss. Apart from this change, IFRS 9 (2010) largely carries forward without substantive amendment the guidance on classification and measurement of financial liabilities from IAS 39.

IFRS 9 is effective annual periods beginning on or after 1 January 2015 with early adoption permitted. The IASB decided to consider making limited amendments to IFRS 9 to address practice or other issues.

Central Bank of Iraq

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(3) Significant accounting policies (continued)

s) New standards and interpretations not yet adopted (continued)

(ii) Amendments to IFRS 7 and IAS 32 on offsetting financial assets and financial liabilities (2011)

Disclosures – Offsetting Financial Assets and Financial Liabilities (amendments to IFRS 7) introduces disclosures about the impact of netting arrangements on an entity's financial position. The amendments are effective for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods. Based on the new disclosure requirements the Bank will have to provide information about what amounts have been offset in the statement of financial position and the nature and extent of rights of set-off under master netting arrangements or similar arrangements.

Based on our initial assessment, the Bank is not expecting a significant impact from the adoption of the amendments to IAS 32. However, the adoption of the amendments to IFRS 7 requires more extensive disclosures about rights to off-set.

(iii) IFRS 13 *Fair Value Measurement* (2011)

IFRS 13 provides a single source of guidance on how fair value is measured, and replaces the fair value measurement guidance that is currently dispersed throughout IFRS. Subject to limited exceptions, IFRS 13 is applied when fair value measurements or disclosures are required or permitted by other IFRSs. Although many of the IFRS 13 disclosure requirements regarding financial assets and financial liabilities are already required, the adoption of IFRS 13 will require the Bank to provide additional disclosures. These include the fair value hierarchy disclosures for non-financial assets/liabilities and disclosures on fair value measurements that are categorised in Level 3. IFRS 13 is effective for annual periods beginning on or after 1 January 2013 with early adoption permitted.

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(4) Financial risk management

Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risks

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

Risk management framework

During the year 2011 the Bank established a risk management unit that manages the CBI's operational and financial risks which the CBI is to a certain extent exposed to. A detailed risk management program was developed. This program includes a general risk management framework which involves identifying, analyzing, measuring, evaluating and monitoring risk, evaluating performance, and monitoring the compliance with the limits and standards set for the risks. The Bank also has drafted procedures to deal with financial risks represented by investment guidelines issued by the board of directors which sets limits and standards for dealing with these risks and allows the management of these risks within the limits and levels set forth in these principle guidelines, as well as monitoring cases of exposure to risk to determine if that exposure extends beyond the acceptable limits. For the purpose of assessing the strengths and weaknesses in performances, the standards set by the risk management unit for dealing with operational and financial risks faced by the Bank, are reviewed on a regular basis according to the prevailing macroeconomic conditions and the possible effects of financial and macroeconomic shocks, and corrective measures are taken to mitigate these effects.

Central Bank of Iraq

Notes to the financial statements

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(4) Financial risk management (continued)

a) Credit risk

Credit risk is the risk that the Bank will incur a loss because any of the Bank's counterparties fail to discharge their contractual obligations. The maximum exposure to credit risk without taking into account any collateral or other credit enhancements is as per the schedule below:

In millions of IQD

		Gross maximum exposure	
		2012	2011
Balances with central banks	7	11,991,966	8,046,951
Balances with banks	8	10,469,338	11,955,411
Held to maturity investment securities	9	50,773,153	46,393,941
Due from Ministry of Finance	10	3,155,520	3,561,542
Foreign currencies investments at International Monetary Fund	11	4,140,272	4,161,675
Other assets	12	421,854	440,977
Total credit risk exposure		<u>80,952,103</u>	<u>74,560,497</u>

- Balances with foreign banks: the CBI is exposed to credit risk related to deposits with foreign banks including correspondent banks which are selected based on their credit ratings set by the credit rating agencies S&P or Moody's for investor services. The Board of Directors therefore sets limits as per the credit ratings that the Bank has exposure on, where deposits are not made with foreign banks with a credit rating below AA-. The ratings of these banks are monitored; and in any instance of deviation from the set limits, a report is submitted to the investment committee for corrective measures to be taken.

The schedule below presents the credit ratings of the central banks the CBI has credit exposure to according to Moody's or S&P credit rating agency:

Country	Credit rating as at 31 December 2012	
	Moody's	S&P
United States	Aaa	AA+
England	Aaa	AAA
Netherlands	Aaa	AAA
France	Aa1	AA+
Italy	Baa2	BBB+

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(4) Financial risk management (continued)

a) Credit risk (continued)

- Investment securities: the CBI relies on long term credit ratings from Standard and Poors and Moody's. According to risk management policy, the qualified party issuing securities to the CBI must fall above a credit rating of AA – given by these two institutions. The credit ratings are monitored on a daily basis by the risk management department to check that the Bank's investments are within the set criteria.

The credit ratings for the treasury securities that are held by the Bank for 2012 are as follows according to Moody's and S&P credit rating agency:

Country	<u>Credit rating as at 31 December 2012</u>	
	Moody's	S&P
United States	Aaa	AA+
Netherlands	Aaa	AAA
France	Aa1	AA+
Italy	Baa2	BBB+

- Local banks: the CBI provides 3 types of banking facilities to the local banks that are experiencing liquidity shortages, and they are the following:
 - Primary credit facilities
 - Secondary credit facilities
 - Last resort facilities
- In order to hedge the risk of defaulting on payment, the Bank imposes the following conditions to reduce the likelihood of this type of risk:
 - Submitting real estate or securities as collateral
 - The maximum loan period is 90 days
 - In case a bank requests the last resort loan, the Ministry of Finance needs to guarantee the payment in case the bank defaults.

Concentration arises when a number of counterparties which are engaged in similar business activities, or activities in the same geographic region, or when they have similar economic features and for which have an impact on their ability to meet contractual obligations in case they are faced by changes in economic, political or other conditions. Concentration indicates the relative sensitivity of the Bank's performance towards the developments affecting a particular industry or geographic location.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(4) Financial risk management (continued)

a) Credit risk (continued)

In order to avoid concentration risk, the CBI has diversified its risk by investing in several foreign banks as follows:

<i>In millions of IQD</i>	2012	2011
France	7,801,701	7,515,732
Italy	4,803,059	4,600,344
England	2,654,861	2,532,530
U.A.E	1,181	257
Netherlands	6,562,647	6,362,459
United States of America	40,941,670	33,429,570
Other countries	10,469,338	11,955,411
	<u>73,234,457</u>	<u>66,396,303</u>

Impaired loans and advances

Impaired loans are loans and advances for which the Bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan. Interest on the impaired loans is suspended and a provision for impairment loss is recognized in the income statement according to management best estimates taking into consideration collaterals if any.

Allowances for impairment

In order to reduce credit risk, the CBI establishes an allowance for impairment losses on its doubtful loans and frozen deposits, especially balances with local and foreign banks which suffer from liquidity problems. The CBI has fully provided for its impaired loans which amount to IQD 1,743,090 million in 2012 (2011: IQD 1,756,770 million).

Write-off policy

The Bank writes off a loan or an investment in a debt security balance and any related allowances for impairment losses, when the Bank determines that the loan or security is uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower's financial position such that the borrower can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

b) Liquidity risk

Liquidity risk is the risk that the CBI will be unable to meet its liabilities when they fall due. In extreme circumstances, lack of liquidity could result in reductions in the balance sheet and sales of assets, or potentially an inability to fulfill lending commitments. The risk that the Bank will be unable to do so is inherent in all banking operations and can be affected by a range of institution-specific and market-wide events including, but not limited to, credit events, merger and acquisition activity, systemic shocks and natural disasters.

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(4) Financial risk management (continued)

b) Liquidity risk (continued)

The CBI takes into consideration the following criteria to avoid those risks:

- The party issuing securities is rated AA- or above.
- The extent of the financial instruments to be easily liquidated without incurring loss on the investment.
- The term of the deposits does not exceed six months.
- The value of reserves invested in term deposits for each bank must not exceed USD 10 billion.

c) Market risk

Market risk is the risk that changes in market prices, such as interest rates, equity prices, foreign exchange rates will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. In order to avoid this risk, the CBI depends on diversifying its foreign currency reserves according to best international practices and standards in this field that define the limits and parameters for each currency reserve and the weight of each major currency in the global economy.

The risk management department and investment committee review these components and weights to measure deviations from the basic standards for currencies and take the required corrective measures to return to the basic standards. The Bank's weighted currency asset portfolio consists of the following:

Currency	Weight
Iraqi Dinar	4.37
US Dollar	61.68
Euro	22.49
Others	6.60
Special Drawing Rights	4.86

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(4) **Financial risk management (continued)**

c) **Market risk (continued)**

Currency risk (continued)

The Bank is exposed to risk of fluctuation in foreign exchange rates as shown in the following table:

31 December 2012

In millions of IQD

Assets

	IQD	USD	EUR	Others	SDR	Total
Gold reserve	–	1,860,236	–	–	–	1,860,236
Cash and balances with banks	33,197	17,833,811	1,279,609	5,624,809	–	24,771,426
Held to maturity investment securities	–	32,883,626	17,889,527	–	–	50,773,153
Due from Ministry of Finance	3,155,520	–	–	–	–	3,155,520
Foreign currencies investments at IMF	–	–	–	–	4,140,272	4,140,272
Property and equipment	119,746	–	–	–	–	119,746
Other assets	421,854	–	–	–	–	421,854
Total assets	3,730,317	52,577,673	19,169,136	5,624,809	4,140,272	85,242,207

Liabilities and equity

Currency issued	35,784,805	–	–	–	–	35,784,805
Treasury bills issued	745,471	–	–	–	–	745,471
Deposits of local and governmental banks	31,353,560	3,437,385	–	–	–	34,790,945
Due to foreign governments and banks	22,471	–	–	–	–	22,471
Due to International Monetary Fund	–	–	–	–	3,870,733	3,870,733
Balances due to governmental institutions	5,609,084	1,248,712	–	–	–	6,857,796
Other liabilities	36,762	–	–	–	–	36,762
Equity	3,133,224	–	–	–	–	3,133,224
Total liabilities and equity	76,685,377	4,686,097	–	–	3,870,733	85,242,207
Net	(72,955,060)	47,891,576	19,169,136	5,624,809	269,539	–

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(4) **Financial risk management (continued)**

c) **Market risk (continued)**

Currency risk (continued)

31 December 2011

In millions of IQD

Assets

	IQD	USD	EUR	Others	SDR	Total
Gold reserve	–	348,808	–	–	–	348,808
Cash and balances with banks	–	12,911,818	4,498,175	4,137,872	–	21,547,865
Held to maturity investment securities	–	28,077,310	18,316,631	–	–	46,393,941
Due from Ministry of Finance	3,561,542	–	–	–	–	3,561,542
Foreign currencies investments at IMF	–	–	–	–	4,161,675	4,161,675
Property and equipment	86,489	–	–	–	–	86,489
Other assets	59,309	375,240	5,807	621	–	440,977
Total assets	3,707,340	41,713,176	22,820,613	4,138,493	4,161,675	76,541,297

Liabilities and equity

Currency issued	32,157,444	–	–	–	–	32,157,444
Treasury bills issued	496,092	–	–	–	–	496,092
Deposits of local and governmental banks	29,155,071	3,329,309	–	–	–	32,484,380
Due to foreign governments and banks	4,183	11,221	–	61,898	–	77,302
Due to International Monetary Fund	–	–	–	–	3,959,098	3,959,098
Balances due to governmental institutions	5,843,003	443,751	–	–	–	6,286,754
Other liabilities	32,737	4,938	–	–	619	38,294
Equity	1,041,933	–	–	–	–	1,041,933
Total liabilities and equity	68,730,463	3,789,219	–	61,898	3,959,717	76,541,297
Net	(65,023,123)	37,923,957	22,820,613	4,076,595	201,958	–

Central Bank of Iraq

Notes to the financial statements

31 December 2012

(4) Financial risk management (continued)

c) Market risk (continued)

Interest rate risk

Following are the interest rate gaps as at 31 December 2012:

In millions of IQD

	Less than month	1 month to 3 months	3 months to 6 months	6 months to 1 year	More than 1 year	Non interest items	Total
Assets							
Gold reserve	–	–	–	–	–	1,860,236	1,860,236
Cash and balances with central banks	11,991,966	–	–	–	–	2,310,122	14,302,088
Balances with banks	10,469,338	–	–	–	–	–	10,469,338
Held to maturity investment securities	–	–	32,883,626	–	17,889,527	–	50,773,153
Due from Ministry of Finance	–	100,000	100,000	100,000	2,855,520	–	3,155,520
Foreign currencies investments at IMF	–	–	–	–	4,140,272	–	4,140,272
Property and equipment	–	–	–	–	–	119,746	119,746
Other assets	–	–	–	–	–	421,854	421,854
Total Assets	22,461,304	100,000	32,983,626	100,000	24,885,319	4,711,958	85,242,207
Liabilities							
Currency issued	–	–	–	–	–	35,784,805	35,784,805
Treasury bills issued	–	745,471	–	–	–	–	745,471
Deposits of local and governmental banks	3,114,670	–	–	–	–	31,676,275	34,790,945
Due to foreign governments and banks	–	–	–	–	–	22,471	22,471
Due to International Monetary Fund	–	1,832,271	–	–	–	2,038,462	3,870,733
Balances due to governmental institutions	–	–	–	–	–	6,857,796	6,857,796
Other liabilities	–	–	–	–	–	36,762	36,762
Total liabilities	3,114,670	2,577,742	–	–	–	76,416,571	82,108,983
Total equity	–	–	–	–	–	3,133,224	3,133,224
Total liabilities and equity	3,114,670	2,577,742	–	–	–	79,549,795	85,242,207
Interest rate sensitivity gap	19,346,634	(2,477,742)	32,983,626	100,000	24,885,319	(74,837,837)	–
Cumulative gap	19,346,634	16,868,892	49,852,518	49,952,518	74,837,837	–	–

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Notes to the financial statements

31 December 2012

(4) Financial risk management (continued)

c) Market risk (continued)

Interest rate risk (continued)

Following are the interest rate gaps as at 31 December 2011:

<i>In millions of IQD</i>	Less than month	1 month to 3 months	3 months to 6 months	6 months to 1 year	More than 1 year	Non interest items	Total
Assets							
Gold reserve	–	–	–	–	–	348,808	348,808
Cash and balances with central banks	8,046,951	–	–	–	–	1,545,503	9,592,454
Balances with banks	11,955,411	–	–	–	–	–	11,955,411
Held to maturity investment securities	–	–	28,086,090	1,543,185	16,764,666	–	46,393,941
Due from Ministry of Finance	–	100,000	100,000	100,000	3,255,519	6,023	3,561,542
Foreign currencies investments at IMF	–	–	–	–	2,340,130	1,821,545	4,161,675
Property and equipment	–	–	–	–	–	86,489	86,489
Other assets	–	–	–	–	–	440,977	440,977
Total Assets	20,002,362	100,000	28,186,090	1,643,185	22,360,315	4,249,345	76,541,297
Liabilities							
Currency issued	–	–	–	–	–	32,157,444	32,157,444
Treasury bills issued	–	496,092	–	–	–	–	496,092
Deposits of local and governmental banks	2,469,850	–	–	–	–	30,014,530	32,484,380
Due to foreign governments and banks	–	–	–	–	–	77,302	77,302
Due to International Monetary Fund	–	1,649,552	–	–	–	2,309,546	3,959,098
Balances due to governmental institutions	–	–	–	–	–	6,286,754	6,286,754
Other liabilities	–	–	–	–	–	38,294	38,294
Total liabilities	2,469,850	2,145,644	–	–	–	70,883,870	75,499,364
Total equity	–	–	–	–	–	1,041,933	1,041,933
Total liabilities and equity	2,469,850	2,145,644	–	–	–	71,925,803	76,541,297
Interest rate sensitivity gap	17,532,512	(2,045,644)	28,186,090	1,643,185	22,360,315	(67,676,458)	–
Cumulative gap	17,532,512	15,486,868	43,672,958	45,316,143	67,676,458	–	–

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Notes to the financial statements

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(4) Financial risk management (continued)

Market risk (continued)

Interest rate risk (continued)

The main objective behind managing interest rate risk is limiting the potential adverse effects on net interest revenue, future cash flows, and fair values of financial instruments resulting from fluctuations in market interest rates. The principal risk to which non-trading portfolios are exposed to is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates. Interest rate risk is managed by the risk management department principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands.

(5) Use of estimates and judgments

Management is responsible for the development, selection and disclosure of the Bank's critical accounting policies and estimates, and the application of these policies and estimates.

These disclosures supplement the commentary on financial risk management (see note 4).

Key sources of estimating uncertainty

Allowance for credit losses

Assets accounted for at amortised cost are evaluated for impairment on the basis described in accounting policy 3(c).

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of amounts considered recoverable

(6) Gold reserve

In millions of IQD

	2012	2011
Gold reserve in CBI vault	266,588	253,115
Gold reserve at the Bank for International Settlements	1,591,598	94,316
Gold coins at CBI vault	2,050	1,377
	<u>1,860,236</u>	<u>348,808</u>

During 2012, the CBI purchased 769,118 Ounces amounting to EUR 995,989,999 from the Bank for International Settlements and 309 Ounces amounting to IQD 641 million from the Ministry of Interior Affairs.

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(7) Cash and balances with central banks

<i>In millions of IQD</i>		2012	2011
Cash on hand		2,310,122	1,545,503
Current account with Federal Reserve Bank of New York		(1,584,516)	(1,322)
Time deposits with Federal Reserve Bank of New York		9,642,560	5,353,582
Current account with Central Bank of United Arab Emirates		1,181	257
Current account with Banque De France		6,723	9,083
Current account with Banca D'Italia		1,553	3,144
Time deposits with Bank of England		2,654,861	2,532,530
Time deposits with Banca D'Italia		1,113,926	–
Current account with De Nederlandsche Bank N.V.		155,678	149,677
		<u>14,302,088</u>	<u>9,592,454</u>

(8) Balances with banks

<i>In millions of IQD</i>	Note	2012	2011
Current accounts with local banks		33,198	–
Due from governmental banks	26	6,616	6,491
Current accounts with foreign banks		70,018	71,592
Time deposits with foreign banks		10,366,122	11,883,819
Frozen deposits with foreign banks		1,736,474	1,750,279
		<u>12,212,428</u>	<u>13,712,181</u>
Allowance for impairment losses of due from governmental banks	26	(6,616)	(6,491)
Allowance for impairment losses of frozen deposits with foreign banks		(1,736,474)	(1,750,279)
		<u>10,469,338</u>	<u>11,955,411</u>

The United Nations Security Council (UNSC) decided in its Resolution number 1483 (2003), that all member states in which there are funds or other financial assets or economic resources for the previous Government of Iraq or its state bodies, corporations, or agencies, located outside Iraq as of 22 May 2003 shall freeze those funds or other financial assets or economic resources and immediately cause their transfer to the Development Fund for Iraq (DFI), unless those funds are themselves subject of a prior judicial, administrative, or arbitral lien or judgment,.

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(8) Balances with banks (continued)

On November 22, 2005, the Iraqi Council of Ministers requested the Ministry of Finance (MOF) to make the necessary arrangements to refund all CBI balances at foreign banks that have been transferred to the DFI as required by UNSC Resolution number 1483 (2003). As of the date the financial statements were authorized for issuance, the MOF has not confirmed the amounts of IQD 401,310 million, equivalent to US Dollar 343 million (2011: IQD 401,310 million, equivalent to US Dollar 343 million) that may be refunded from the DFI to the CBI.

Due to the absence of the details, the CBI did not prepare reconciliations of certain frozen and old outstanding deposits at foreign banks as at 31 December 2012.

(9) Held to maturity investment securities

<i>In millions of IQD</i>	2012	2011
The Federal Reserve Bank of New York	32,895,075	28,080,000
Unamortized discount	(11,449)	(2,690)
	<u>32,883,626</u>	<u>28,077,310</u>
Banque De France - Bills and bonds	7,794,978	7,506,649
Banca D'Italia - Bonds	3,687,580	4,597,200
De Nederlandsche Bank N.V. - Bonds	6,406,969	6,212,782
	<u>50,773,153</u>	<u>46,393,941</u>

(10) Due from Ministry of Finance

<i>In millions of IQD</i>	Note	2012	2011
Due from Ministry of Finance		3,155,520	3,555,519
Accrued interest		–	6,023
	26	<u>3,155,520</u>	<u>3,561,542</u>

On 21 February 2006, a restructuring agreement was signed between the CBI and the MOF for the settlement of the total balance of IQD 5,393,890 million due to the CBI as of December 31, 2005. The balance should be settled over 7.5 years starting on 31 March 2006, through 30 equal quarterly installments of IQD 179,796 million each. An annual interest rate of 5% will be charged on the outstanding balance.

The MOF shall finance the quarterly repayments by issuing one year Treasury bills every quarter bearing an annual interest rate of 5%, which CBI could then auction to local banks.

The MOF did not settle installments related to the year 2008 that should be settled and paid to the CBI in 2009 amounting to IQD 719,184 million. On 24 December 2009, the CBI and the MOF agreed to reschedule the remaining balance due to the CBI, amounting to IQD 3,955,519 and to start making payments to the CBI from 1 March 2011, through equal quarterly installments of IQD 100,000 million each. During the years 2011 and 2012, eight installments were paid amounting to IQD 800,000 million.

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(11) Foreign currencies investments at International Monetary Fund

	2012		2011	
	SDR	IQD Million	SDR	IQD Million
International Monetary Fund Quota Subscription	1,184,000,000	2,129,671	1,184,000,000	2,127,911
Special Drawing Rights				
Holdings with IMF	1,135,820,667	2,010,601	1,135,820,667	2,033,764
	<u>2,319,820,667</u>	<u>4,140,272</u>	<u>2,319,820,667</u>	<u>4,161,675</u>

(12) Other assets

<i>In millions of IQD</i>	2012	2011
Interest receivable	348,395	381,668
Loans to employees	73,241	59,061
Others	218	248
	<u>421,854</u>	<u>440,977</u>

(13) Currency issued

<i>In millions of IQD</i>	2012	2011
Banknotes	<u>35,784,805</u>	<u>32,157,444</u>

(14) Treasury bills issued

<i>In millions of IQD</i>	2012	2011
Face value	750,040	500,020
Unamortized discount	(4,569)	(3,928)
	<u>745,471</u>	<u>496,092</u>

The discounted treasury bills are auctioned off to local banks with interest rates that range between 4.5% and 6% (2011: interest rates range between 5% and 7.5%) in accordance with the instructions issued by CBI.

Treasury bills are issued with original maturity of three months. Total treasury bills issued during the year 2012 amounted to IQD 3,900,330 million (2011: IQD 2,300,120 million).

The purpose of issuing these Treasury bills is to ensure that proper control over market liquidity is maintained.

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Notes to the financial statements

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(15) Property and equipment

In millions of IQD

	Land	Buildings	Fixtures and fittings	Vehicles	Building Under construction	Total
Cost						
Balance at 1 January 2011	76,013	2,789	7,861	3,924	1,381	91,968
Additions	20	–	1,779	2,839	646	5,284
Disposals	(40)	(18)	(894)	(2,662)	(6)	(3,620)
Balance at 31 December 2011	75,993	2,771	8,746	4,101	2,021	93,632
Balance at 1 January 2012	75,993	2,771	8,746	4,101	2,021	93,632
Additions	–	–	13,527	139	22,051	35,717
Balance at 31 December 2012	75,993	2,771	22,273	4,240	24,072	129,349
Depreciation						
Balance at 1 January 2011	–	(276)	(3,706)	(1,760)	–	(5,742)
Depreciation for the year	–	(256)	(1,126)	(687)	–	(2,069)
Disposals	–	–	668	–	–	668
Balance at 31 December 2011	–	(532)	(4,164)	(2,447)	–	(7,143)
Balance at 1 January 2012	–	(532)	(4,164)	(2,447)	–	(7,143)
Depreciation for the year	–	(139)	(1,670)	(651)	–	(2,460)
Balance at 31 December 2012	–	(671)	(5,834)	(3,098)	–	(9,603)
Carrying amounts						
At 1 January 2011	76,013	2,513	4,155	2,164	1,381	86,226
At 31 December 2011	75,993	2,239	4,582	1,654	2,021	86,489
At 1 January 2012	75,993	2,239	4,582	1,654	2,021	86,489
At 31 December 2012	75,993	2,100	16,439	1,142	24,072	119,746

(16) Deposits of local and governmental banks

In millions of IQD

	2012	2011
Current accounts	31,652,644	29,990,899
Time deposits	3,114,670	2,469,850
Others	23,631	23,631
	34,790,945	32,484,380

According to the CBI regulations, all banks operating in Iraq should maintain a compulsory reserve at the CBI equivalent to 10% of total customers' deposits in Iraqi Dinar and 15% of total customers' deposits in foreign currencies and to keep cash in their books equivalent to 5% of total customers' deposits in Iraqi Dinar. Compulsory reserve represents a non-interest bearing liability.

The deposits of local banks as at 31 December 2012 includes compulsory reserve deposited in the CBI amounted to IQD 4,623,497 million (2011: IQD 4,302,310 million) and a balance in USD amounted to USD 1,427,467,760 equivalent to IQD 1,664,427 million (2011: balance in USD amounted to USD 1,163,577,000 equivalent to IQD 1,361,386 million).

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(17) Due to foreign governments and banks

<i>In millions of IQD</i>	2012	2011
Due to foreign governments and financial institutions *	9	9
Overdraft accounts *	18,216	73,119
Balances for international institutions	4,246	4,174
	<u>22,471</u>	<u>77,302</u>

* During years 2007 to 2012 the CBI resolved to derecognize certain old outstanding balances due to foreign governments and banks in its records. In 2012, the CBI has recognized revenue amounting to IQD 54,858 million (2011: IQD 168,954 million) as a result of derecognition. The CBI believes that these balances are the liability of the Ministry of Finance as part of the Iraqi sovereign debt and the Ministry of Finance confirmed the relief of the CBI from all these liabilities.

(18) Due to International Monetary Fund

	2012		2011	
	SDR	IQD Million	SDR	IQD Million
SDR allocations	1,134,495,508	2,033,072	1,134,495,508	2,031,391
IMF securities	1,014,329,000	1,832,271	1,014,329,000	1,922,053
Currency Holdings:				
IMF no. 1 account including currency valuation adjustments	2,971,000	5,367	2,971,000	5,630
IMF no. 2 account including currency valuation adjustments	12,580	23	12,580	24
	<u>2,151,808,088</u>	<u>3,870,733</u>	<u>2,151,808,088</u>	<u>3,959,098</u>

The balance of Special Drawing Rights (SDR) 1,134,495,508 represents an allocation of SDRs by the International Monetary Fund (IMF) to Iraq. SDRs are allocated by the IMF to members that are participants in the IMF's SDR Department at the time of allocation in proportion to their quotas in the IMF.

(19) Balances due to governmental institutions

<i>In millions of IQD</i>	Note	2012	2011
Due to Ministry of Finance		5,262,158	4,452,223
Due to other governmental institutions		1,516,141	1,496,482
Due to Sulaimaniyah and Erbil branches		25,445	283,811
Others		54,052	54,238
	26	<u>6,857,796</u>	<u>6,286,754</u>

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Notes to the financial statements

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(20) Other liabilities

<i>In millions of IQD</i>	2012	2011
Interest payable	8,293	6,932
Accounts payable	2,881	6,371
Suspense balances *	8,006	8,000
Others	17,582	16,991
	<u>36,762</u>	<u>38,294</u>

* These balances represent liability balances that have not been reconciled as at 31 December 2012. The effects of the reconciliation of these balances on the financial statements have not been determined as at 31 December 2012.

(21) Equity

<i>In millions of IQD</i>	2012	2011
Capital (a)	100,000	100,000
General reserve (b)	474,511	–
Emergency reserve (b)	118,628	–
Gold revaluation reserve (c)	446,794	348,793
Retained earnings (d)	1,993,291	593,140
	<u>3,133,224</u>	<u>1,041,933</u>

a) Capital

According to Article 5 of the Central Bank of Iraq Law of 2004, the authorized capital of the CBI shall be IQD 100,000 million and shall be fully paid by the Republic of Iraq in exchange for 100% of the CBI's capital stock. The authorized capital stock of the CBI shall be held solely by the Republic of Iraq and shall not pay any dividend and shall not be transferable nor be subject to any encumbrances.

b) Reserves

According to Article 5 of the Central Bank of Iraq Law of 2004, the CBI shall hold a general reserve account, an unrealized profit reserve account and other reserves as may be appropriate under international accounting standards.

c) Gold revaluation reserve

The CBI has a gold revaluation reserve in the amount of IQD 446,794 million which represents the following:

<i>In millions of IQD</i>	2012	2011
Gold revaluation reserve, beginning of year	348,793	311,596
Gold revaluation gain for the year	98,001	37,197
Gold revaluation reserve, end of year	<u>446,794</u>	<u>348,793</u>

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(21) Equity (continued)

d) Retained earnings

Within three months after the end of each financial year, the CBI shall determine its net profits available for distribution or its net losses. If the CBI incurs a net operating loss for any financial year, that loss shall first be charged to the general reserve and subsequently to Capital.

In a period of three months after the end of each financial year, the Board shall distribute the net profits available for distribution as follows:

- 80 percent of any profits available for distribution shall be transferred to the general reserve account until this reserve reaches a sum equal to 10% of the total assets of the CBI;
- Any remaining net profits available for distribution shall be transferred to emergency reserve.

On 18 June 2012, the CBI's Board of directors decided to allocate the retained earnings of year 2011 amounting to IQD 593,140 million to the general reserve and emergency reserves accounts.

(22) Interest income

<i>In millions of IQD</i>	Note	2012	2011
Treasury bills and bonds		312,935	248,724
Due from banks		55,312	80,206
Due from Ministry of Finance	26	172,196	190,228
Overnight deposits		8,296	2,265
Others		3,381	10,198
		<u>552,120</u>	<u>531,621</u>

(23) Interest expense

<i>In millions of IQD</i>	Note	2012	2011
Local and governmental banks deposits	26	107,965	63,043
Treasury bills issued		47,783	41,566
Others		28,720	39,535
		<u>184,468</u>	<u>144,144</u>

(24) Net fee and commission income

<i>In millions of IQD</i>	2012	2011
Fee and commission income	1,306,436	1,106,379
Fee and commission expense	(2,477)	(2,585)
	<u>1,303,959</u>	<u>1,103,794</u>

Fee and commission income for the year 2012 includes the commission income of IQD 652,960 million (2011: IQD 584,985 million) earned from the transfers transactions ordered by the Ministry of Finance from the Development Fund of Iraq account. The CBI buys the dollars from the Ministry of Finance with a commission equivalent to 1% of the exchange rate applied to translate the amounts ordered into Iraqi Dinar.

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31 December 2012

(25) Cash and cash equivalents

In millions of IQD

	2012	2011
Cash and balances with central banks	14,302,088	9,592,454
Current accounts with foreign banks	70,018	71,592
Current accounts with local banks	33,198	–
Time deposits with foreign banks	10,366,122	11,883,819
	24,771,426	21,547,865

(26) Related party transactions

The CBI is a governmental entity and enters into transactions with governmental banks, ministries and other governmental institutions in the ordinary course of business at commercial interest and commission rates. Transactions with related parties included in the statement of financial position and income statement are as follows:

In millions of IQD

	Note	2012	2011
(A) Assets			
Due from Ministry of Finance	10	3,155,520	3,561,542
Due from governmental banks	8	6,616	6,491
Allowance for impairment losses of due from governmental banks	8	(6,616)	(6,491)
		3,155,520	3,561,542
(B) Liabilities			
Deposits of governmental banks	16	29,760,382	29,427,596
Balances due to governmental institutions	19	6,857,796	6,286,754
		36,618,178	35,714,350
(C) Related party transactions			
Interest income from Ministry of Finance	22	172,196	190,228
Interest expenses on governmental banks deposits	23	77,593	44,303

(27) Accounts managed on behalf of the MOF

The CBI maintains the cash payments and receipts records of the Development Fund for Iraq (DFI), which was established during May 2003 and recognized by the United Nations Security Council Resolution (UNSCR) 1483 (2003). The DFI's bank accounts are managed by the CBI on behalf of the Ministry of Finance (MOF). As at 31 December 2007 the DFI accounts have been excluded from the CBI's financial statements, which resulted in un-reconciled debit difference of IQD 11,823 million between the DFI assets balances and the related liability balances in the CBI records. This difference has been provided for in the CBI's financial statements as at 31 December 2007.

During 2007, CBI has excluded the DFI's accounts together with the provision taken as at 31 December 2007 from the CBI's records and financial statements.

During 2009, un-reconciled excess of assets over liabilities in the DFI balances amounted to IQD 5,418 million.

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31 December 2012

(28) Commitments and contingent liabilities

There are lawsuits in different countries against the CBI for the settlement of past due debt of the CBI, Iraqi ministries and other governmental institutions for the amount of IQD 859,955 million as at 31 December 2012 (2011: IQD 837,591 million).

Many of the lawsuits may relate to debts reconciled or settled under the Government of Iraq's External Debt Reconciliation Project. However, to the financial statements issuance date, there are no sufficient information regarding the balances that have been reconciled /settled or exempted as at 31 December 2012, and the balances that will be reconciled and settled subsequent to year end.

Due to the unavailability of sufficient information, the final outcome of these lawsuits and its effect on the CBI's financial statements, if any, is uncertain and could not be quantified and provided for as at 31 December 2012.

(29) Off-balance sheet

The Central Bank of Iraq, in its role as the banker of the Ministry of Finance and the fiscal agent of the Government of Iraq, as stipulated in the Central Bank Law of Iraq (Article 4, section 1.d), holds promissory notes in its off balance sheet amounting to IQD 1,932,040 million, which represent the International Monetary Fund financing to Iraq for budget support and therefore for the use of the Ministry of Finance.

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(30) Financial assets and liabilities

The table below sets out the carrying amounts and fair values of the Bank's financial assets and liabilities.

31 December 2012

In millions of IQD

	Held-to-maturity	Loans and receivables	Other amortised cost	Total carrying amount	Fair value
Cash and balances with central banks	–	14,302,088	–	14,302,088	14,302,088
Balances with banks	–	10,469,338	–	10,469,338	10,469,338
Held to maturity investment securities	50,773,153	–	–	50,773,153	51,070,480
Due from Ministry of Finance	–	3,155,520	–	3,155,520	3,155,520
Foreign currencies investments at IMF	–	4,140,272	–	4,140,272	4,140,272
Other assets	–	421,854	–	421,854	421,854
	50,773,153	32,489,072	–	83,262,225	83,559,552
Currency issued	–	–	35,784,805	35,784,805	35,784,805
Treasury bills issued	–	–	745,471	745,471	745,471
Deposits of local and governmental banks	–	–	34,790,945	34,790,945	34,790,945
Due to foreign governments and banks	–	–	22,471	22,471	22,471
Due to International Monetary Fund	–	–	3,870,733	3,870,733	3,870,733
Balances due to governmental institutions	–	–	6,857,796	6,857,796	6,857,796
Other liabilities	–	–	36,762	36,762	36,762
	–	–	82,108,983	82,108,983	82,108,983

31 December 2011

In millions of IQD

	Held-to-maturity	Loans and receivables	Other amortised cost	Total carrying amount	Fair value
Cash and balances with central banks	–	9,592,454	–	9,592,454	9,592,454
Balances with banks	–	11,955,411	–	11,955,411	11,955,411
Held to maturity investment securities	46,393,941	–	–	46,393,941	47,614,315
Due from Ministry of Finance	–	3,561,542	–	3,561,542	3,561,542
Foreign currencies investments at IMF	–	4,161,675	–	4,161,675	4,161,675
Other assets	–	440,977	–	440,977	440,977
	46,393,941	29,712,059	–	76,106,000	77,326,374
Currency issued	–	–	32,157,444	32,157,444	32,157,444
Treasury bills issued	–	–	496,092	496,092	496,092
Deposits of local and governmental banks	–	–	32,484,380	32,484,380	32,484,380
Due to foreign governments and banks	–	–	77,302	77,302	77,302
Due to International Monetary Fund	–	–	3,959,098	3,959,098	3,959,098
Balances due to governmental institutions	–	–	6,286,754	6,286,754	6,286,754
Other liabilities	–	–	38,294	38,294	38,294
	–	–	75,499,364	75,499,364	75,499,364

Glossary

CBI: Central Bank of Iraq

MOF: Ministry of Finance

IMF: International Monetary Fund

KRG: Kurdistan Regional Government

IQD: Iraqi Dinar

DFI: Development Fund for Iraq

SDR: Special Drawing Rights

MOU: Memorandum of Understanding