NOTES TO THE FINANCIAL STATEMENTS

1. Significant accounting policies

a. General

The financial statements are prepared in accordance with generally accepted accounting principles in Israel (Israeli GAAP), adapted for the special activity of a central bank and consistent with the practice of other central banks. The main items presented in accordance with generally accepted accounting principles of central banks are:

1) Revaluation accounts - as detailed in Section m below.
2) Statements of cash flows - as detailed in Section t below.

b. Definitions

In these financial statements:

1) **"The Bank"**—the Bank of Israel.
2) **"CPI"**—the Consumer Price Index as published by the Central Bureau of Statistics.
3) "**Adjusted amount**"—the historical nominal amount adjusted to the CPI in respect of December 2003, in accordance with the provisions of Opinions 23 and 36 of the Institute of Certified Public Accountants in Israel.
4) **"Reported amount"**—the adjusted amount at the transition date (December 31, 2003), with additional amounts in nominal values that were added after the transition date, less amounts subtracted after the transition date.
5) **"Nominal financial reporting"**—financial reporting based on reported amounts.
6) **"Fair value"**—the amount for which an asset can be acquired or sold (a liability assumed or settled) in a current transaction between independent willing parties.

c. Financial statements in reported amounts

1) In October 2001, the Israel Accounting Standards Board published Accounting Standard No. 12, "Discontinuance of Adjustment of Financial Statements". Pursuant to this Standard, and in accordance with Accounting Standard No. 17, which was published in December 2002, the adjustment of financial statements for the effect of inflation was discontinued as of January 1, 2004.
2) In the past, the Bank prepared its financial statements on the basis of historical cost, with no adjustment for changes in the purchasing power of the Israeli currency. In

the financial statements for 2005, comparative figures for the year ended December 31, 2003 were recalculated on a historical-cost basis, adjusted for changes in the CPI as required by Accounting Standard No. 12, for purposes of the transition to nominal financial reporting.

The adjusted amounts at December 31, 2003 served as a starting point for nominal financial reporting as of January 1, 2004. Any additions and disposals made during the period were included at their nominal values.

3) Amounts of nonfinancial assets do not necessarily reflect their realizable value or current economic value, but only the reported amounts of those assets.

4) The term "cost" in these financial statements denotes the reported amount of cost.

d. Reporting principles

1) Balance Sheet:
   a. Nonfinancial items (fixed assets and investments shown at cost) are stated in reported amounts.
   b. Financial items are stated in the Balance Sheet at their nominal values at the Balance Sheet date.
   c. The Balance Sheet is presented in the format generally accepted by central banks worldwide.

2) Statement of Operations:
   a. Income and expenses originating from nonfinancial items (such as depreciation, prepaid expenses and deferred income) or from provisions included in the Balance Sheet, are derived from the movement between the reported amount of the opening balance and the reported amount of the closing balance.
   b. All other items of the Statement of Operations (such as interest income and interest expenses) are stated at their nominal values.

3) Statement of Changes in Equity:

   In accordance with Section 76 of the Bank of Israel Law, 5770–2010, within three months from the end of each year the Bank will transfer its profits to the Government according to the following provisions:
   a. If the equity amounts to 2.5 percent or more of total assets, the Government will receive an amount equal to the net income, less any accumulated losses.
   b. If the equity amounts to more than 1 percent of total assets but less than 2.5 percent of total assets, the Government will receive 50 percent of the net income, less any accumulated losses.
   c. If the equity amounts to 1 percent or less of total assets, the Government will not receive any profits.

The Bank is permitted to record capital funds arising from accounting principles, provided that the balance of net income not transferred to the Government as aforementioned is added to retained earnings and not recognized as another capital item, unless agreed upon otherwise between the Governor and the Minister of Finance.

In accordance with these provisions, as of December 31, 2015 there is no obligation to transfer funds to the Government.

e. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the Bank's management to make estimates and assumptions regarding transactions or matters whose final effect on the financial statements cannot be determined with precision at the time the statements are prepared. Even though the estimates and assumptions are based on management's best judgment, the final effect of such transactions or matters may be different from the estimates and assumptions made in their respect.

f. Revenue recognition

Income and expenditures are charged to the Statement of Operations on an accrual basis.

Realized gains or losses from foreign currency and securities in local and foreign currency are transferred to the Statement of Operations. These gains or losses are calculated on the basis of average cost of the balances of that asset.

Unrealized gains are not transferred to the Statement of Operations but rather are charged to the "Revaluation accounts" line item in the Balance Sheet.

Unrealized losses are transferred to the Statement of Operations after offsetting unrealized gains of the same asset. These losses derive from the difference between the average cost of an asset and its fair value.

Unrealized losses from foreign currency securities, from local currency securities, or a specific foreign currency are not offset against unrealized gains from other securities or foreign currencies.

Losses recognized in the Statement of Operations are not offset against unrealized gains that will accrue in the future.

g. Securities

1) Foreign currency securities

Tradable foreign currency securities are stated in the Balance Sheet at their fair value as of the Balance Sheet date. The fair value of quoted securities is based on market prices. Unquoted securities are revalued on the basis of data obtained from outside sources.

The adjusted cost of securities is their par value plus the interest, indexation differentials and the balance of the premium or discount not yet amortized. The premium or discount is amortized over the period from the date of purchase until the date of redemption.

The difference between the original cost of the securities and their par value plus interest and the unamortized balance of the premium or discount in respect of each security is charged to the Statement of Operations.

Unrealized differentials from indexation to an index published abroad which accrued on the principal and the difference between the fair value of the securities and their adjusted cost in respect of each security are charged to the ″Revaluation accounts″ line item in the Balance Sheet.

Interest income and amortization of the premium or discount are charged to the Statement of Operations on an accrual basis, and are stated in the ″Interest income from assets in foreign currency abroad″ line item.

Income from the realization of securities is stated in ″Other financial income (expenses)—Securities and derivative financial instruments″.

The balance of unrealized loss, which is calculated separately in respect of each security, is charged to the Statement of Operations at the end of the year and stated under ″Other financial income (expenses)—Securities and derivative financial instruments″.

2) Local currency securities

Tradable government securities in local currency are stated in the Balance Sheet at their fair value as of the Balance Sheet date. The difference between the original cost of securities and their par value, plus interest and the unamortized balance of the premium or discount is charged to the Statement of Operations.

Unrealized indexation differentials accrued on the principal as well as the difference between the fair value of the securities and their adjusted cost are charged to the "Revaluation accounts" line item in the Balance Sheet.

Interest income and amortization of the premium or discount are stated in the "Interest income from the Government" line item.

The balance of unrealized loss, which is calculated separately in respect of each security, is charged to the Statement of Operations at the end of the year and stated under "Other financial income (expenses) - securities and derivative financial instruments".

h. International financial institutions

1) The International Monetary Fund (IMF)

The International Monetary Fund (IMF) balances are managed in Special Drawing Rights (hereinafter, "SDR") and presented in New Shekels using the representative exchange rates published by the Bank of Israel as of the Balance Sheet date (see Notes 3 and 12 below).

2) Balances in respect of international financial institutions

The Bank of Israel's participation in other international financial institutions is presented under assets in the "International financial institutions" line item according to the cost in the currency in which the participation was paid, translated according to the exchange rate on the transaction date with the necessary reporting adjustments to reported amounts pursuant to Accounting Standard No. 12, “Halting adjustment of financial statements”. Liabilities to international financial institutions are presented under liabilities in the "The International Monetary Fund and others" line item.

i. Fixed assets

1) Fixed assets are stated at cost less accumulated depreciation. Cost includes expenses directly attributable to the purchase of the asset.
2) Improvements and enhancements are charged to the cost of the assets and depreciated over their useful lives, whereas maintenance and repair expenses are charged to the Statement of Operations as incurred.
3) Depreciation is calculated by the straight-line method on the basis of the estimated useful life of the asset:
   Buildings - 50–67 years;
   Motor vehicles - 6.5 years;
   Computers - 4 years;
   Equipment - 10 years.
4) Software that is not an integral part of the related hardware is shown under fixed assets at cost and depreciated by the straight-line method over four years.

j. Banknotes and coins in circulation

Banknotes and coins in circulation that were issued by the Bank reflect the Bank’s liability to their holders. This liability is shown in the Bank’s Balance Sheet at face value.

k. Short-term loan

The balance of short-term loans (called makam, their Hebrew acronym) in the Balance Sheet reflects the redemption price of the loan held by the public, less the balance of unamortized discount. Makam sold by the Government to the Bank of Israel but not yet sold to the public is not included in this balance.

Makam are issued for a period of up to one year. The discount is the difference between the redemption price of the makam and the proceeds from their sale to the public.

The discount is amortized over the period from the date of issuance of the makam to its date of redemption.

Expenses for amortization of the discount on the balance of the makam held by the public are shown in the Statement of Operations in "Interest expenses to banks and the public".

l. Liabilities in respect of employee rights

All liabilities in respect of employer-employee relations have corresponding reserves in accordance with the law, relevant agreements, common practice and management's expectations.

Liabilities in respect of employee pensions and severance pay are calculated by an expert actuary using the method of estimation of cumulative benefits with probabilities taken into account on the basis of past experience. The discount rate applicable to the reserves is set in accordance with a discount rate which is based on the yield curve of government bonds in Israel, and the rate of future salary increases is estimated by management and based on past experience.

The provision for vacation pay is computed on the basis of the accrued vacation and the effective salary for vacation redemption days at October 31. The difference in the liability that derives from the accrual of vacation days between October 31 and December 31 is immaterial (see Note 14).

Employee benefits liabilities are stated under "Other liabilities" in local currency.

m. Revaluation accounts

The following are the types of revaluation accounts:

1) Revaluation accounts that include unrealized profits from exchange rate differentials on balances denominated in foreign currency and unrealized profits from indexation and the revaluation of tradable securities in local currency and foreign currency to their fair value.

   These revaluation accounts are maintained separately for each item (currency, security) and are recognized in the Statement of Operations when the item is fully or partially realized. No offsetting among different types of items is performed. Revaluation accounts in respect of certain externally managed portfolios are managed at the individual portfolio level.

Accumulated loss in the revaluation accounts relating to each item (currency, security) that originates from indexation differentials and price differentials in securities in local currency and foreign currency and exchange rate differentials on foreign exchange reserves is charged to the Statement of Operations at the end of the year (see also Section f above).

2) Revaluation accounts that consist of unrealized gains or losses deriving from changes in actuarial assumptions underlying the computation of pension accruals. Accordingly, any accumulated unrealized losses at year end will result in a negative account balance.

n. Foreign currency

Assets and liabilities denominated in or indexed to foreign currency are shown in New shekels according to the representative exchange rates published by the Bank of Israel at the Balance Sheet date.

Income and expenses in foreign currency are included in the Statement of Operations at the representative exchange rates in effect on the date of each transaction.

Exchange rate differentials arising from the adjustment of assets and liabilities due to changes in the exchange rate include realized and unrealized exchange rate differentials.

Realized gains or losses from exchange rate differentials are carried to the Statement of Operations. Unrealized exchange rate differentials are charged to revaluation accounts separately for each foreign currency.

A loss balance in the revaluation accounts at the end of the year is carried to the Statement of Operations and is not offset against future unrealized gains. Unrealized losses in one currency are not offset against unrealized gains in another currency.

Following are data on the shekel exchange rates against other key currencies:

	December 31			Rate of Change	
	2016	2015	2014	2016	2015
		(NIS)		(Percent)	
US Dollar	3.8450	3.9020	3.8890	(1.5)	0.3
Euro	4.0438	4.2468	4.7246	(4.8)	(10.1)
Pound Sterling	4.7252	5.7840	6.0636	(18.3)	(4.6)
Special Drawing Rights (SDRs)[a]	5.1689	5.4071	5.6344	(4.4)	(4.0)

[a] The SDR rate published by the IMF is determined according to a weighted basket of four currencies - the US dollar, euro, Japanese yen, and pound sterling.

o. Indexation

Assets and liabilities linked to the CPI are shown in accordance with the indexation terms determined for each balance.

Following are data on the CPI (based on the 2002 average):

		December 31			Rate of change	
		2016	2015	2014	2016	2015
			(Points)		(Percent)	
CPI	For November	122.8	123.2	124.3	(0.3)	(0.9)
	For December	122.8	123.1	124.3	(0.2)	(1.0)

p. Interest rates

Some of the local currency interest on the Government's and the banks' balances, which are collected or paid by the Bank of Israel, are based on the Bank of Israel interest rate or the prime interest rate.

Following are data on the interest rates:

	December 31			Rate of change	
	2016	2015	2014	2016	2015
			(Percent)		
Bank of Israel interest	0.10	0.10	0.25	-	(60.0)
Prime interest	1.60	1.60	1.75	-	(8.6)

q. Financial instruments

The Bank uses derivatives in its monetary policy and foreign exchange activities, both in Israel and abroad.

1) Activity in financial instruments in Israel

NIS/USD forwards

These transactions are shown net in the Balance Sheet under "Other assets" or "Other liabilities": future receipt of US dollars less future remittance of shekels. In the Statement of Operations, the results of the transactions are shown under "Interest income from assets in foreign currency abroad".

2) Activity in financial instruments abroad

a. Repurchase (Repo) and Reverse-Repurchase (R. Repo) Agreements

The Bank carries out reverse repurchase (R. Repo) agreements. These transactions are treated as a secured debt, and are included in the "Reverse repurchase agreements" item. Securities purchased within the framework of these agreements do not appear in the Balance Sheet. In the Statement of Operations, the results of these transactions are shown in the "Interest income from assets in foreign currency abroad" item.

The Bank also carries out repurchase (Repo) agreements. Such transactions are composed of the sale of securities under an agreement to purchase them in the future. The transactions are treated as a secured debt and accordingly the securities sold under its terms are not subtracted from the Bank's assets. The liability to purchase the securities is included in the "Repurchase agreements" item. In the Statement of Operations, the results of these transactions are shown in the "Interest income from assets in foreign currency abroad" item.

b. Foreign currency swaps and forwards

These transactions are included on the Balance Sheet as the sum of the differences between the foreign currency received and the foreign currency to be remitted in the future, with the addition of the balance of unamortized premium, and are shown in the "Derivative financial instruments" item. In the Statement of Operations, the results of these transactions are included in the "Interest income from assets in foreign currency abroad" item.

c. Futures

The balance of futures contracts at fair value on the date of the financial statements is shown in Note 17 - "Commitments, financial instruments and contingent liabilities". In the Statement of Operations, the change in the value of the contracts is recorded under "Other financial income (expenses)—securities and derivative financial instruments".

r. Offsetting financial balances

Financial assets and liabilities are presented on the Balance Sheet in net amount only when the Bank has a legal and enforceable offsetting right, and when it is intended to settle the asset or liability on a net basis or to realize the asset and settle the liability simultaneously.

s. Impairment of assets

The Bank applies Accounting Standard No. 15 (Revised), "Impairment of Assets" (hereinafter, "the Standard"), which establishes procedures that the Bank must apply to ensure that its assets in the Balance Sheet (to which the Standard applies) are not stated at an amount greater than the recoverable amount, i.e., the net selling price or value in use (the present value of the estimated future cash flows expected to derive from the use and realization of the asset), whichever is higher.

The Standard applies to all Balance Sheet assets, except for financial assets. The Standard also establishes presentation and disclosure rules for assets that have been impaired. Where the value of the asset in the Balance Sheet exceeds its recoverable amount, the Bank recognizes an impairment loss in the amount of the difference between the asset's book value and recoverable amount. A loss recognized in this manner is reversed only if changes occur in the estimates that were used to determine the recoverable amount of the asset from the date on which the last impairment loss was recognized.

t. Statements of cash flows

These financial statements do not include a statement of cash flows because such statement provides no significant information beyond that presented in the financial statements; this practice corresponds with the general practice among some of the central banks worldwide.

u. Taxes

According to the Bank of Israel Law, 5770–2010, regarding the payment of taxes, municipal taxes, levies and other mandatory payments, the Bank has the same status as the State of Israel.

2. Foreign currency assets and liabilities abroad

Foreign exchange reserves

As presented in the explanatory remarks, the economic analysis refers to foreign exchange reserves which consist of the balance of the ”Foreign currency assets abroad” item less the balance of the ”Foreign currency liabilities abroad” item.
The Bank’s investment policy relates to these balances.

The following is the composition of the foreign exchange reserves:

	December 31		December 31	
	2016	2015	2016	2015
	(NIS million)		(USD million)	
Foreign currency assets abroad	384,483	357,249	99,996	91,555
Less: Foreign currency liabilities abroad	(5,955)	(3,826)	(1,549)	(980)
Total foreign exchange reserves[a]	**378,528**	**353,423**	**98,447**	**90,575**

[a] Foreign exchange reserves include balances in respect of collaterals on futures presented on the assets side under "Other assets" in "Foreign currency assets abroad" and on the liabilities side under "Other liabilities" in "Foreign currency liabilities abroad".

In the comparative figures for 2015, an amount of approximately NIS 3,315 million was reclassified from "Reverse repurchase agreements" to "Demand deposits". These items are presented in the Balance Sheet under "Foreign currency assets abroad".

3. The International Monetary Fund (IMF)[a]

	December 31		December 31	
	2016	2015	2016	2015
	(NIS million)		(SDR million)	
IMF quota	9,929	5,738	1,921	1,061
Less: Liability for the quota	(9,763)	(4,218)	(1,889)	(780)
Reserve tranche	**166**	**1,520**	**32**	**281**
NAB loans	**305**	**261**	**59**	**48**
Special Drawing Rights (SDRs)	**4,034**	**4,591**	**780**	**849**
Total IMF balance	**4,505**	**6,372**	**871**	**1,178**

[a] The balances bear interest pursuant to the IMF's terms.

a. Bank of Israel participation in the IMF

Each member country of the IMF has a quota for its participation in the Fund's capital, a quota which is denominated in the SDR currency. The part of the quota that is paid in cash (the reserve tranche) is transferred to the IMF in foreign currency and may be withdrawn by the country, whereas the rest is deposited with the country's central bank in deposits and notes indexed to SDR.

In 2011, a reform was carried out in the quotas and in the IMF's voting rights. In the first stage, which came into effect in March 2011, Israel's quota was increased by about SDR 133 million to approximately SDR 1,061 million; in February 2016, the second stage was completed, in the context of which Israel's IMF quota was increased by about SDR 860 million, to about SDR 1,921 million.

Since 1999, Israel has been part of the IMF's Financial Transaction Plan. This plan is a mechanism through which an IMF member country may exchange SDRs or foreign currency against its local currency and another country is asked to perform a counter exchange. Executing transactions in the context of the Financial Transaction Plan modifies the quota composition between the Reserve Tranche and the other tranche which consists of deposits and notes placed in the central bank (liabilities for the quota).

b. NAB loans

In 2010, Israel joined the IMF's arrangement known as NAB (New Arrangements to Borrow).

In accordance with this arrangement, countries, including Israel, provide a credit line to the IMF, in the context of which loans are extended with maturities of ten years. However, the loans may be repaid to Israel at an earlier date at its request, should it need the money.

As of December 31, 2016, the Bank has provided loans that bear interest at the IMF's terms in an aggregate of NIS 305 million (SDR 59 million).

Simultaneously with the increase in Israel's IMF quota effective from February 2016, the maximum credit line that the Bank provides the IMF was reduced from SDR 500 million (NIS 2,704 million) on December 31, 2015 to SDR 340 million (NIS 1,757 million) on December 31, 2016.

c. Special Drawing Rights (SDRs)

The balance includes SDRs allocated by the IMF to Israel. Against these allocations the Bank has a liability towards the IMF with no repayment date, which is shown in liabilities under the item of "The International Monetary Fund and others". The State is not required to hold all the SDRs allocated to it.

At the end of 2009, Israel joined another IMF plan, "Voluntary Arrangement for the Purchase and Sale of SDRs". Within the framework of this plan, the State of Israel may be asked to buy or sell some SDRs from other IMF members, as instructed by the IMF. These transactions are recorded in the balance of "Special Drawing Rights (SDRs)".

Under this Arrangement, Israel’s SDR holdings may range from 50 percent up to a maximum of 145 percent of total SDRs allocated by the IMF to Israel (the IMF allocated a total of SDR 884 million). The IMF has undertaken to consult with Israel before making any purchase or sale of SDRs in the context of the plan.

4. Credit to the government

The item includes credit on account of binational foundations that was extended to the Government of Israel for investment, in conjunction with the United States government, in binational foundations involved in research, industrial development and science. The foundations deposited these sums with the Bank of Israel and they are shown in foreign currency on the Balance Sheet on the liabilities side under the item of "Other liabilities—the International Monetary Fund and others ". Both the credit and the fund deposits earn either fixed interest of 4–4.125 percent or interest on the basis of LIBOR.

5. Tradable securities in local currency

This item consists of tradable government securities in local currency, indexed to the last CPI level known on the Balance Sheet date, as well as unindexed securities. The securities are shown at fair value.

6. Other assets

	December 31	
	2016	2015
	(NIS million)	
Loans to employees	72	74
Other receivables	4	5
Total other assets	**76**	**79**

7. International financial institutions

	December 31	
	2016	2015
	(NIS million)	
Investment in BIS shares	282	282
Balance of other international financial institutions[a]	-	659
Total	**282**	**941**

[a] The balances are in respect of the following institutions:
i) The World Bank Group:
1. IBRD—International Bank for Reconstruction and Development
2. IDA—International Development Association
3. MIGA—Multilateral Investment Guarantee Agency
4. IFC—International Finance Corporation
ii) EBRD—European Bank for Reconstruction and Development
iii) IDB—Inter-American Development Bank
IIC—Inter-American Investment Corporation

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In December 2016, an agreement was signed between the Bank of Israel and the Government of Israel for assigning the State's representation from the Bank of Israel to the Government in the following international institutions: the World Bank Group, the Inter-American Development Bank Group and the European Bank for Reconstruction and Development. As part of the agreement, the Government paid the Bank the fair value of the shares that had been purchased by the Bank in these institutions. The Government also undertook to bear all the payments and obligations in connection with the State's membership in these institutions, including any borne or undertaken by the Bank of Israel.

When investing in international financial institutions, the Bank is generally required to assume additional undertakings toward these institutions beyond the actual callable capital, which may be exercised by the institutions only in times of need, a scenario which is relatively unlikely.

The balance of the above undertakings as of December 31, 2016 was NIS 4,342 million (December 31, 2015 - NIS 4,346 million).

As of the date of publication of these financial statements, the assignment of the liability for the additional obligations to the financial institutions discussed above has not yet been settled and the Bank and the Government are taking steps towards its settlement.

8. Fixed assets

	Land and buildings[a]	Equipment and furniture, computers, software and vehicles	Total
		(NIS million)	
Cost			
Balance as of January 1, 2016	281	365	646
Additions	24	36	60
Disposals	-	(1)	(1)
Balance as of December 31, 2016	**305**	**400**	**705**
Accumulated depreciation			
Balance as of January 1, 2016	56	204	260
Additions	12	41	53
Disposals[b]	-	(1)	(1)
Balance as of December 31, 2016	**68**	**244**	**312**
Depreciated balance as of December 31, 2016	**237**	**156**	**393**
Depreciated balance as of December 31, 2015	**225**	**161**	**386**

[a] The Bank's property in Jerusalem, the cost of which, including the depreciated cost of the structures thereon, amounts to approximately NIS 211 million as of December 31, 2016 (approximately NIS 192 million as of December 31, 2015), is leased from the Israel Land Authority (ILA) through June 30, 2016. As of the date of publication of the financial statements, the Bank is negotiating the extension of the lease agreement with the ILA.

9. Banknotes and coins in circulation

	December 31, 2016		December 31, 2015	
	Quantity	NIS	Quantity	NIS
	(million)		(million)	
Banknotes and coins in circulation				
NIS 20	39.54	791	37.28	746
NIS 50	60.62	3,031	59.72	2,986
NIS 100	168.59	16,859	164.89	16,489
NIS 200	265.60	53,120	255.94	51,189
Coins in circulation		2,188		2,070
Other[a]		2		2
Commemorative banknotes and coins		5		5
Total		**75,996**		**73,487**

[a] The balance consists mainly of special coin items in circulation.

10. Government deposits

Government balances consist of balances in local currency and balances in foreign currency. All the government balances in the Bank of Israel (excluding several extraordinary balances) can be offset against each other.

	December 31		December 31	
	2016	2015	2016	2015
	(NIS million)		(USD million)	
In foreign currency[a]				
Current deposits	8,506	9,040	2,212	2,317
Other deposits	776	735	202	188
Total deposits in foreign currency	**9,282**	**9,775**	**2,414**	**2,505**
In local currency[b]				
Current deposits	15,134	12,766		
Total government deposits	**24,416**	**22,541**		

[a] **Government deposits in foreign currency**
The current deposits are used for financing budgetary activity. Some foreign currency government deposits bear interest at the rate paid on US Treasury bills with an average of six months to maturity. The average interest rate in 2016 was 0.42 percent (2015—0.14 percent).

[b] **Government deposits in local currency**
The current deposits and the balances used for bond lending are designated for financing budgetary activity. Local currency current deposits bear (when in debit) or are paid (when in credit) interest at the Prime rate. The average Prime rate in 2016 was 1.6 percent (in 2015—1.62 percent), other than on the government balances used for bond lending and other government balances for which a different interest rate is collected.

11. Deposits of banking corporations

	December 31		December 31	
	2016	2015	2016	2015
	(NIS million)		(USD million)	
Deposits in foreign currency[a] (*Pamach*)	**772**	**1,136**	**201**	**291**
Deposits in local currency[b]				
Time deposits	172,001	144,000		
Demand deposits	34,502	26,224		
Total deposits in local currency	**206,503**	**170,224**		
Total deposits of banking corporations	**207,275**	**171,360**		

[a] **Deposits in foreign currency**
Foreign currency demand deposits (known by their Hebrew acronym, Pamach) serve as a liquid asset against nonresidents' foreign currency deposits. The reserve requirement ranges from 0 to 6 percent, depending on the term of the deposit.

[b] **Deposits in local currency**

1. The Bank of Israel receives time deposits in New Shekels from the banking corporations. The deposits are allocated by auction for terms of one day, one week and one month. The deposits are not considered liquid assets with regard to the banking corporations' reserve requirements. In addition, deposits are received at the (overnight) deposit window available to the banking corporations at an interest rate of 0.1 percentage points below the Bank of Israel interest rate.
   The interest rate for deposits at the window on December 31, 2016 was 0 percent (on December 31, 2015 - 0 percent).
   The average interest rate for deposits at the window in 2016 was 0 percent (in 2015 - 0 percent).
   The average interest rate for time deposits by auction on December 31, 2016 was 0.10 percent (on December 31, 2015 - 0.1 percent).
   The average interest rate for time deposits by auction in 2016 was 0.1 percent (in 2015 - 0.12 percent).
   The average interest rate for time deposits by auction in 2015 was 0.12 percent (in 2014 - 0.59 percent).
2. The banking corporations' local currency demand deposits serve as a liquid asset against deposits in Israeli currency and Israeli residents' deposits in foreign currency. The reserve requirement ranges from 0–6 percent, depending on the term of the deposit.

12. The International Monetary Fund and others

	December 31	
	2016	2015
	(NIS million)	
Allocated Special Drawing Rights[a]	4,568	4,777
Other[b]	129	*) 137
Total	**4,697**	**4,914**

[a] Special Drawing Rights (SDRs) are sums of money that member countries in the IMF undertook to purchase from the Fund. No repayment date has been set for this liability and it bears interest according to the IMF's terms. The IMF allocates SDRs to its constituent countries commensurate with the size of their quotas.
As of December 31, 2016, Israel has been allocated approximately SDR 884 million.

[b] The item mainly includes liabilities to binational foundations.

*) Reclassified.

13. *Makam*

	December 31	
	2016	2015
	(NIS million)	
Redemption value of short-term loans sold to the public	104,999	116,000
Less: Discount at time of sale to the public	(138)	(161)
Proceeds from sale of *makam* to the public	**104,861**	**115,839**
Plus amortization of discount difference for the period through the Balance Sheet date	73	95
Total balance of *makam*	**104,934**	**115,934**

The Short-Term Loan Law, 5744–1984, authorizes the government to issue short-term bills to be sold only to the Bank of Israel, with the Bank selling them to, and buying them from, the public in order to carry out its functions. The government must deposit all proceeds from sales of these bills with the Bank of Israel and may not use them for any purpose other than repayment of the loan taken under said Law, or payment of the yield thereon. The purchase of bills from the government by the Bank of Israel and the deposit of the proceeds from this purchase with the Bank of Israel are not reflected in the Bank's Balance Sheet.

The balance of *makam* shown in the Balance Sheet reflects the redemption value of bills held by the public, less the balance of the unamortized discount.

14. Other liabilities

	December 31	
	2016	2015
	(NIS million)	
Pension and severance pay liabilities	6,040	5,982
Liability for employees' and other rights	181	187
Other payables[a]	430	74
Total other liabilities	**6,651**	**6,243**

[a] The balance mainly comprises accounts of statutory bodies that are managed at the Bank of Israel.

a. Pension and severance pay liabilities

The pension liability is calculated according to the pension agreements with the Bank's employees and pensioners who commenced their employment before September 2002 and their survivors (on December 31, 2016 - 248 employees and 854 pensioners and survivors; on December 31, 2015 - 271 employees and 842 pensioners and survivors). The pension liability includes future payment of benefits for Bank employees, former Bank employees whose pensions have been frozen, retirees, and survivors. It also includes obligations on account of the cash value of unused sick leave upon retirement and retirement grants.

The Bank's liability is calculated on the basis of salary and pension data for December 2016 and actuarial calculations. The calculation was performed using a method of estimating benefits which are accrued under various parameters: early retirement rates, pension rates for surviving spouses and orphans, employees' seniority and grade, relevant tax rates, etc.

The actuarial calculation is based on foreseen changes in white-collar mortality rates as well as other demographic tables, in accordance with pension circular 2013-3-1 published by the Capital Market, Insurance, and Savings Division of the Ministry of Finance regarding the preparation of actuarial calculations. The calculation assumes a real annual employee salary increase of 1.5 percent or 3 percent based on the employee's age.

For Bank employees who commenced their employment after September 2002, the Bank's liability for pension and severance pay is covered by regular deposits to a recognized pension and severance pay fund on behalf of the individual employee. Since sums deposited in said manner are neither controlled nor managed by the Bank, neither they nor the liabilities against which they were deposited are recorded in the Balance Sheet.

b. Liability for employees' and other rights

This item includes a liability for employees' vacation pay of approximately NIS 116 million (in 2015—approximately NIS 111 million). The liability at December 31 is calculated on the basis of the accrued vacation days due and the effective salary for vacation redemption at October 31. The difference in the liability that derives from the accrual of vacation days between October 31 and December 31 is immaterial.

15. Revaluation accounts

Revaluation accounts include unrealized profits from the revaluation of the following items (see Notes 1g, 1m and 1n above):

	December 31	
	2016	2015
	(NIS million)	
Balances denominated in foreign currency	19,559	23,025
Tradable securities in foreign currency	7,127	4,393
Tradable securities in local currency	949	1,231
Changes in actuarial assumptions for computing pension accruals	(2,071)	(1,939)
Total revaluation accounts	**25,564**	**26,710**

16. Share capital and general reserve in historical nominal values

Data on the Bank's share capital and general reserve appear in the financial statements in reported amounts (see Note 1c above).

The data in historical nominal values are: NIS 60 million in share capital and NIS 260 million in the general reserve at December 31, 2016 and 2015.

The general reserve served in the past to increase the Bank's capital in accordance with Section 6 of the Bank of Israel Law, 5714-1954.

17. Commitments, financial instruments and contingent liabilities

	December 31	
	2016	2015
	(NIS million)	
a. Commitments (off-Balance Sheet)		
Guarantees for government exports	-	4
Documentary credit	41	42
b. Financial instruments		
Currency swaps and forwards:		
Fair value	3,283	730
Future receipts of foreign currency	90,230	86,043
Future payments of foreign currency	86,501	84,950
Stock index futures - fair value:		
Purchase obligation in dollars	-	4
Purchase obligation in euros	-	35
Sale obligation in dollars	9	-
Sale obligation in euros	(13)	-
Interest rate futures - fair value:		
Sale obligation in dollars	-	24
Bond futures - fair value:		
Sale obligation in dollars	16	-
Purchase obligation in dollars	(8)	-
c. Contingent liabilities		

There are several claims pending against the Bank of Israel. However, no provision has been recorded in the Bank's books in respect of these claims as it is the Bank's opinion, based on the opinion of its Legal Department, that the probability of these claims being upheld is low, or that the sums involved are not significant.

18. Interest income (expenses) from assets in foreign currency abroad

	For the year ended December 31	
	2016	2015
	(NIS million)	
Demand deposits	(24)	5
Short-term deposits	(33)	2
Tradable securities	1,816	1,279
Securities purchased under R.Repo agreements	(21)	(3)
Derivative financial instruments, net	682	253
The IMF	4	3
Total	**2,424**	**1,539**

19. Interest income from the government

	For the year ended December 31	
	2016	2015
	(NIS million)	
Binational foundations[a]	76	76
Securities in local currency	343	529
Total	**419**	**605**

[a] See Note 4 above.

20. Other interest income

This item consists of interest income from banks in respect of balances bearing the Bank of Israel interest rate.

21. Interest expenses to banks and the public

	For the year ended December 31	
	2016	2015
	(NIS million)	
Makam	144	362
Time deposits	144	148
Total	**288**	**510**

22. Interest expenses to the government

	For the year ended December 31	
	2016	2015
	(NIS million)	
Balances in local currency[a]	283	232
Balances in foreign currency	4	1
Total	**287**	**233**

23. Other interest expenses

This item consists mainly of interest expenses in respect of deposits of the US-Israel Binational Industrial Research and Development Foundation, a deposit of the US-Israel Binational Science Foundation and international financial institutions.

24. Other financial income (expenses)—securities and derivative financial instruments

	For the year ended December 31	
	2016	2015
	(NIS million)	
Securities in foreign currency[a]	1,153	1,319
Derivative financial instruments in foreign currency[b]	(531)	98
Total	**622**	**1,417**

[a] Dividend income, gain (loss) from sale of securities and loss from net impairment of securities at the end of the year.
[b] Including financial income (expenses) from the realization of derivative financial instruments.

25. Other financial income (expenses)—exchange rate differentials

This item consists of exchange rate differentials in respect of balances denominated in foreign currency (see Notes 1f, 1m and 1n).

26. Other financial income (expenses)—miscellaneous

	For the year ended December 31	
	2016	2015
	(NIS million)	
In local currency	4	-
In foreign currency	(27)	(29)
Total[a]	**(23)**	**(29)**

[a] This item includes income (expenses) from commissions from the Bank's financial activities, from international financial institutions and from loans to employees.

27. General and administrative expenses

	For the year ended December 31	
	2016	2015
	(NIS million)	
Salaries and employees' rights[a]	316	302
Pension and severance pay[b]	207	242
General expenses	152	129
Total	**675**	**673**

[a] In respect of salaries and provision for employees' vacation (753 employee posts on December 31, 2016 and 754 employee posts on December 31, 2015).
[b] In respect of defined benefit pension payments to retirees and an update of the Bank's liability for pension payments (see Note 14 above).

28. Other expenses

In 2016, this item mainly includes a capital loss from the assignment of the State's representation in international financial institutions from the Bank of Israel to the Government (see Note 7 above). In 2015, this item mainly included capital losses from the disposal of fixed assets.