HEARTLAND BANK

Disclosure Statement

For the year ended 30 June 2018

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GENERAL INFORMATION

This Disclosure Statement has been issued by Heartland Bank Limited (the Bank) and its subsidiaries (the Banking Group) for the year ended 30 June 2018 in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the Order). The financial statements of the Bank for the year ended 30 June 2018 form part of, and should be read in conjunction with, this Disclosure Statement.

Words and phrases defined by the Order have the same meanings when used in this Disclosure Statement.

Name and address for service

The name of the Registered Bank is Heartland Bank Limited.

The Bank's address for service is Level 3, Heartland House, 35 Teed Street, Newmarket, Auckland.

Details of incorporation

The Bank was incorporated under the Companies Act 1993 on 30 September 2010.

Interests in 5% or more of voting securities of the Bank

Name	Percentage held
Harrogate Trustee Limited	9.63%

No person has the ability to directly or indirectly appoint 25% or more of the board of directors (the Board) (or other persons exercising powers of management) of the Bank.

PRIORITY OF CREDITORS' CLAIMS

In the event of the Bank becoming insolvent or ceasing business, certain claims set out in legislation are paid in priority to others. These claims include secured creditors, taxes, certain payments to employees and any liquidator’s costs. After payment of those creditors, the claims of all other creditors are unsecured and would rank equally, with the exception of holders of subordinated bonds and notes which rank below all other claims.

The loans sold to Heartland ABCP Trust 1 (ABCP Trust) are set aside for the benefit of investors in ABCP Trust. Loans held as receivables within Seniors Warehouse Trust (SW Trust) and ASF Settlement Trust (ASF Trust) are also set aside for the benefit of funders in these Trusts. See Note 25 - Structured entities for further details.

GUARANTEE ARRANGEMENTS

As at the date this Disclosure Statement was signed, no material obligations of the Bank were guaranteed.

DIRECTORS

All Directors of the Bank reside in New Zealand with the exception of Ellen Comerford who resides in Australia. Communications to the Directors can be sent to Heartland Bank Limited, 35 Teed Street, Newmarket, Auckland. The Directors of the Bank and their details at the time this Disclosure Statement was signed were:

Name: Geoffrey Thomas Ricketts CNZM
Chairman - Board of Directors
Type of director: Independent Non-Executive Director
Qualifications: LLB (Hons), LLD *(honoris causa),* CF Inst D
Occupation: Company Director
External Directorships:
Asteron Life Limited, Highground Trust Limited, Janmac Capital Limited, Maisemore Enterprises Limited, MCF 1 Limited, MCF 2 Message4U Limited, MCF 2 Nexus Limited, MCF 3 Limited (in liquidation), MCF 5 Limited (in liquidation), MCF 7 Limited, MCF 8 Limited, MCF 9 Limited, MCF 10 Limited, MCF2 (Fund 1) Limited, MCF2A General Partner Limited, MCF2 GP Limited, MC Medical Properties Limited, Mercury Capital No.1 Fund Limited, Mercury Capital No. 1 Trustee Limited, Mercury Pharmacy Holdings Limited, Mercury Medical Holdings Limited, New Zealand Catholic Education Office Limited, NZCEO Finance Limited, O & E Group Services Limited, Oceania and Eastern Finance Limited, Oceania and Eastern Group Funds Limited, Oceania and Eastern Holdings Limited, Oceania and Eastern Limited, Oceania and Eastern Securities Limited, Oceania Securities Limited, Quartet Equities Limited, Suncorp Group Holdings (NZ) Limited, Suncorp New Zealand Limited, Suncorp Group Services NZ Limited, The Centre for Independent Studies Limited, The Todd Corporation Limited, Todd Management Services Limited, Todd Offshore Limited, Vero Insurance New Zealand Limited, Vero Liability Insurance Limited.

Name: Ellen Frances Comerford
Type of director: Independent Non-Executive Director
Qualifications: BEc
Occupation: Company Director
External Directorships:
Cash Converters International Limited, Comerford Gohl Holdings Pty Limited, Hollard Holdings Australia Pty Limited, The Hollard Insurance Company Pty Limited.

Name: Edward John Harvey
Type of director: Independent Non-Executive Director
Qualifications: BCom, CA, CF Inst D
Occupation: Company Director
External Directorships:
Investore Property Limited, Kathmandu Holdings Limited, New Zealand Opera Limited, Pomare Investments Limited, Stride Holdings Limited, Stride Investment Management Limited, Stride Property Limited.

Name: Bruce Robertson Irvine
Type of director: Independent Non-Executive Director
Qualifications: BCom, LLB, FCA, CF Inst D, FNZIM
Occupation: Company Director
External Directorships:
Air Rarotonga Limited, Amaia Day Spa (Tonga) Limited, Amaia Luxury Spa Limited, B R Irvine Limited, Blackbyre Horticulture Limited, Bowdens Mart Limited, Bray Frampton Limited, Britten Motorcycle Company Limited, Chambers @151 Limited, Clipper Investments (2002) Limited, Cockerill and Campbell (2007) Limited, Cowes Bay Holdings (NZ) Limited, Embassy Hotels Limited, GZ Capital Limited, GZ NZ Limited, GZ RES Limited, Hansons Lane International Holdings Limited, Hawling Holding Limited, House of Travel ESP Trustee Limited, House of Travel Holdings Limited, Janes Ventures Limited, J.S. Ewers Limited, Lake Angelus Holdings Limited, Lamanna Bananas (NZ) Limited, Lamanna Limited, Lamanna Premier Group Pty Limited, Limeloader Irrigation Limited, Market Fresh Wholesale Limited, Market Gardeners Limited, Market Gardeners Orders (Christchurch) Limited, Market Gardeners Orders Wellington Limited, MG Group Holdings Limited, MG Marketing Limited, MG New Zealand Limited, Monarch Hotels Limited, Noblesse Oblige Limited, PGG Wrightson Limited, Phimai Holdings Limited, Quitachi Limited, Rakon ESOP Trustee Limited, Rakon Limited, Rakon PPS Trustee Limited, Scenic Circle Convention Services Limited, Scenic Circle MLC Cafe & Bar Limited, Scenic Circle (Napier) Limited, Scenic Hotels (Ashburton) Limited, Scenic Hotel Group Limited, Scenic Hotels (Hamilton) Limited, Scenic Hotels (International) Limited, Scenic Hotels (Karapiro) Limited, Skope Industries Limited, Southland Produce Markets Limited, USC Investments Limited, Wavell Resources Limited.

Name: Graham Russell Kennedy MNZM J.P.
Type of director: Independent Non-Executive Director
Qualifications: BCom, FCA, ACIS, ACIM, CF Inst D
Occupation: Company Director
External Directorships:
Ashburton Aquatic Park Limited, Ashburton Central Limited, Avon Properties (2008) Limited, BK&P Trustees Limited, BK Riversdale Trustees Limited, Black Gnat Properties Limited, Black Quill Investments Limited, Bradford Group Holdings Limited, Cates Grain & Seed Limited, Concurrent Properties Limited, Crescent Custodians Limited, E & S Tekapo Limited, Earth & Sky GP Limited, Eastfield Health Limited, Eastfield Investments Limited, Hornby Consortium Limited, Lake Extension Trust Limited, Norman Spencer Nominees Limited, Timaru Central Limited, Wareing Group Limited.

Name: Sir Christopher Robert Mace KNZM
Type of director: Independent Non-Executive Director
Qualifications: CM Inst D
Occupation: Company Director
External Directorships:
Akitu Equities Limited, Akitu Capital Limited, Akitu Health Services Limited, Akitu Investments Limited, Goldburn Resources Limited, Helicopter Enterprises Limited, Janik Equities Limited, Janmac Capital Limited, J N S Capital Limited, Mace Capital Limited, Mace Construction Limited, Mace Developments Limited, Mace Enterprises Limited, Mace Investments Limited, Maisemore Enterprises Limited, Nuffield Forestry Limited, Oceania and Eastern Finance Limited, Oceania and Eastern Group Funds Limited, Oceania and Eastern Holdings Limited, Oceania and Eastern Limited, Oceania and Eastern Securities Limited, O & E Group Services Limited, Paroa Bay Station Limited, PPT Trustee (NZ) Limited, Quartet Equities Limited, Ryburn Lagoon Trust Limited, St. Just Enterprises Limited, Te Pūia Tāpapa Fund, The New Zealand Initiative Limited.

DIRECTORS (CONTINUED)

Name: Vanessa Cynthia May Stoddart
Qualifications: BCom/LLB (Hons), PG Dip in Prof Ethics
Type of director: Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Alliance Group Limited, New Zealand Global Women Limited, The New Zealand Refinery Company Limited.

Name: Gregory Raymond Tomlinson
Qualifications: AME
Type of director: Non-Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Alta Cable Holdings Limited, Argenta Limited, Chippies Vineyard Limited, Forte Health Group Limited, Forte Health Limited, Impact Capital Management Limited, Impact Capital Limited, Indevin Group Limited, Little Ngakuta Trust Company Limited, Mountbatten Trustee Limited, Nearco Stud Limited, Ngakuta Trust Company Limited, Oceania Healthcare Limited, Oceania Healthcare Holdings Limited, Pelorus Finance Limited, St Leonards Limited, The Icehouse Limited, Tomlinson Group Investments Limited, Tomlinson Group NZ Limited, Tomlinson Holdings Limited.

Name: Jeffrey Kenneth Greenslade
Qualifications: LLB
Type of director: Non-Independent Executive Director
Occupation: Chief Executive Officer of the Bank
External Directorships:
Brew Greenslade & Company Limited.

Conflicts of interest policy

All Directors are required to disclose to the Board any actual or potential conflict of interest which may exist or is thought to exist upon appointment and are required to keep these disclosures up to date. The details of each disclosure made by a Director to the Board must be entered in the Interests Register.

Directors are required to take any necessary and reasonable measures to try to resolve the conflict and comply with the Companies Act 1993 on disclosing interests and restrictions on voting. Any Director with a material personal, professional or business interest in a matter being considered by the Board must declare their interest and, unless the Board resolves otherwise, may not be present during the boardroom discussions or vote on the relevant matter.

Interested transactions

There have been no transactions between the Bank or any member of the Banking Group and any Director or immediate relative or close business associate of any Director which either has been entered into on terms other than those which would in the ordinary course of business of the Bank or any member of the Banking Group be given to any other person of like circumstances or means, or could be reasonably likely to influence materially the exercise of the Directors' duties.

Audit committee composition

Members of the Bank's Audit Committee as at the date of this Disclosure Statement are as follows:

Bruce Robertson Irvine (Chairperson)	Independent Non-Executive Director
Edward John Harvey	Independent Non-Executive Director
Graham Russell Kennedy	Independent Non-Executive Director
Geoffrey Thomas Ricketts	Independent Non-Executive Director

AUDITOR

KPMG
KPMG Centre
18 Viaduct Harbour Avenue
Auckland

AMENDMENTS TO CONDITIONS OF REGISTRATION

The conditions of registration applying to the Bank were amended on 1 January 2018 to refer to revised versions of the RBNZ Banking Supervision Handbook documents:

- Liquidity Policy (BS13) which includes changes to the calculation of liquidity ratios as a consequence of the removal of off-quarter disclosure statements; and
- Framework for Restrictions on High-LVR Residential Mortgage Lending (BS19) which includes changes to the High-LVR restrictions.

CONDITIONS OF REGISTRATION

These conditions apply on and after 1 January 2018.

The registration of Heartland Bank Limited ("the Bank") as a registered Bank is subject to the following conditions:

1. That—

(a) the Total capital ratio of the Banking Group is not less than 8%;

(b) the Tier 1 capital ratio of the Banking Group is not less than 6%;

(c) the Common Equity Tier 1 capital ratio of the Banking Group is not less than 4.5%;

(d) the Total capital of the Banking Group is not less than $30 million;

(e) the Bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued after 1 January 2013 in the calculation of its capital ratios unless it has received a notice of non-objection to the instrument from the Reserve Bank; and

(f) the Bank meets the requirements of Part 3 of the Reserve Bank of New Zealand document "Application requirements for capital recognition or repayment and notification requirements in respect of capital" (BS16) dated November 2015 in respect of regulatory capital instruments.

For the purposes of this condition of registration, -

the Total capital ratio, the Tier 1 capital ratio, the Common Equity Tier 1 capital ratio and Total capital must be calculated in accordance with the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

an Additional Tier 1 capital instrument is an instrument that meets the requirements of subsection 8(2)(a) or (c) of the Reserve Bank of New Zealand document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

a Tier 2 capital instrument is an instrument that meets the requirements of subsection 9(2)(a) or (c) of the Reserve Bank of New Zealand document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

1A. That—

(a) the Bank has an internal capital adequacy assessment process ("ICAAP") that accords with the requirements set out in the document "Guidelines on a Bank's internal capital adequacy assessment process ('ICAAP')" (BS12) dated December 2007;

(b) under its ICAAP the Bank identifies and measures its "other material risks" defined as all material risks of the Banking Group that are not explicitly captured in the calculation of the Common Equity Tier 1 capital ratio, the Tier 1 capital ratio and the Total capital ratio under the requirements set out in the document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015; and

(c) the Bank determines an internal capital allocation for each identified and measured "other material risk".

1B. That, if the buffer ratio of the Banking Group is 2.5% or less, the Bank must:

(a) according to the following table, limit the aggregate distributions of the Bank's earnings to the percentage limit to distributions that corresponds to the Banking Group's buffer ratio:

Banking Group's buffer ratio	Percentage limit to distributions of the Banks' earnings
0% - 0.625%	0%
>0.625% - 1.25%	20%
>1.25% - 1.875%	40%
>1.875% - 2.5%	60%

(b) prepare a capital plan to restore the Banking Group's buffer ratio to above 2.5% within any timeframe determined by the Reserve Bank for restoring the buffer ratio; and

(c) have the capital plan approved by the Reserve Bank.

For the purposes of this condition of registration, -

"buffer ratio", "distributions", and "earnings" have the same meaning as in Part 3 of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

2. That the Banking Group does not conduct any non-financial activities that in aggregate are material relative to its total activities.

In this condition of registration, the meaning of "material" is based on generally accepted accounting practice.

3. That the Banking Group's insurance business is not greater than 1% of its total consolidated assets.

For the purposes of this condition of registration, the Banking Group's insurance business is the sum of the following amounts for entities in the Banking Group:

(a) if the business of an entity predominantly consists of insurance business and the entity is not a subsidiary of another entity in the Banking Group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total consolidated assets of the group headed by the entity; and

(b) if the entity conducts insurance business and its business does not predominantly consist of insurance business and the entity is not a subsidiary of another entity in the Banking Group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total liabilities relating to the entity's insurance business plus the equity retained by the entity to meet the solvency or financial soundness needs of its insurance business.

In determining the total amount of the Banking Group's insurance business—

(a) all amounts must relate to on balance sheet items only, and must comply with generally accepted accounting practice; and

(b) if products or assets of which an insurance business is comprised also contain a non-insurance component, the whole of such products or assets must be considered part of the insurance business.

For the purposes of this condition of registration,—

"insurance business" means the undertaking or assumption of liability as an insurer under a contract of insurance:

"insurer" and "contract of insurance" have the same meaning as provided in sections 6 and 7 of the Insurance (Prudential Supervision) Act 2010.

4. That aggregate credit exposures (of a non-capital nature and net of any allowances for impairment) of the Banking Group to all connected persons do not exceed the rating-contingent limit outlined in the following matrix:

Credit rating of the Bank[1]	Connected exposure limit (% of the Banking Group's Tier 1 capital)
AA/Aa2 and above	75
AA-/Aa3	70
A+/A1	60
A/A2	40
A-/A3	30
BBB+/Baa1 and below	15

Within the rating-contingent limit, credit exposures (of a non-capital nature and net of any allowances for impairment) to non-bank connected persons shall not exceed 15% of the Banking Group's Tier 1 capital.

For the purposes of this condition of registration, compliance with the rating-contingent connected exposure limit is determined in accordance with the Reserve Bank of New Zealand document entitled "Connected exposures policy" (BS8) dated November 2015.

5. That exposures to connected persons are not on more favourable terms (e.g. as relates to such matters as credit assessment, tenor, interest rates, amortisation schedules and requirement for collateral) than corresponding exposures to non-connected persons.

6. That the Bank complies with the following corporate governance requirements:

(a) the board of the Bank must have at least five directors;

(b) the majority of the board members must be non-executive directors;

(c) at least half of the board members must be independent directors;

(d) an alternate director,—

(i) for a non-executive director must be non-executive; and

(ii) for an independent director must be independent;

(e) at least half of the independent directors of the Bank must be ordinarily resident in New Zealand;

(f) the chairperson of the board of the Bank must be independent; and

(g) the Bank's constitution must not include any provision permitting a director, when exercising powers or performing duties as a director, to act other than in what he or she believes is the best interests of the company (i.e. the Bank).

For the purposes of this condition of registration,—

"independent,"—

(a) in relation to a person other than a person to whom paragraph (b) applies, has the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014; and

(b) in relation to a person who is the chairperson of the board of the Bank, means a person who—

(i) meets the criteria for independence set out in section 10 except for those in paragraph 10(1)(a) in BS14; and

(ii) does not raise any grounds of concern in relation to the person's independence that are communicated in writing to the Bank by the Reserve Bank of New Zealand:

1 This table uses the rating scales of Standard & Poor's, Fitch Ratings and Moody's Investor Service. (Fitch Ratings' scale is identical to Standard & Poor's.)

"non-executive" has the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014.

7. That no appointment of any director, chief executive officer, or executive who reports or is accountable directly to the chief executive officer, is made in respect of the Bank unless:

    (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and

    (b) the Reserve Bank has advised that it has no objection to that appointment.

8. That a person must not be appointed as chairperson of the board of the Bank unless:

    (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and

    (b) the Reserve Bank has advised that it has no objection to that appointment.

9. That the Bank has a board audit committee, or other separate board committee covering audit matters, that meets the following requirements:

    (a) the mandate of the committee must include: ensuring the integrity of the Bank's financial controls, reporting systems and internal audit standards;

    (b) the committee must have at least three members;

    (c) every member of the committee must be a non-executive director of the Bank;

    (d) the majority of the members of the committee must be independent; and

    (e) the chairperson of the committee must be independent and must not be the chairperson of the Bank.

    For the purposes of this condition of registration, "independent" and "non-executive" have the same meanings as in condition of registration 6.

10. That a substantial proportion of the Bank's business is conducted in and from New Zealand.

11. That the Banking Group complies with the following quantitative requirements for liquidity-risk management:

    (a) the one-week mismatch ratio of the Banking Group is not less than zero percent at the end of each business day;

    (b) the one-month mismatch ratio of the Banking Group is not less than zero percent at the end of each business day; and

    (c) the one-year core funding ratio of the Banking Group is not less than 75 percent at the end of each business day.

    For the purposes of this condition of registration, the ratios identified must be calculated in accordance with the Reserve Bank of New Zealand documents entitled "Liquidity Policy" (BS13) dated January 2018 and "Liquidity Policy Annex: Liquid Assets" (BS13A) dated December 2011.

12. That the Bank has an internal framework for liquidity risk management that is adequate in the Bank's view for managing the Bank's liquidity risk at a prudent level, and that, in particular:

    (a) is clearly documented and communicated to all those in the organisation with responsibility for managing liquidity and liquidity risk;

    (b) identifies responsibility for approval, oversight and implementation of the framework and policies for liquidity risk management;

    (c) identifies the principal methods that the Bank will use for measuring, monitoring and controlling liquidity risk; and

    (d) considers the material sources of stress that the Bank might face, and prepares the Bank to manage stress through a contingency funding plan.

13. That no more than 10% of total assets may be beneficially owned by a SPV.

    For the purposes of this condition,—

    "total assets" means all assets of the Banking Group plus any assets held by any SPV that are not included in the Banking Group's assets:

    "SPV" means a person—

    (a) to whom any member of the Banking Group has sold, assigned, or otherwise transferred any asset;

    (b) who has granted, or may grant, a security interest in its assets for the benefit of any holder of any covered bond; and

    (c) who carries on no other business except for that necessary or incidental to guarantee the obligations of any member of the Banking Group under a covered bond:

    "covered bond" means a debt security issued by any member of the Banking Group, for which repayment to holders is guaranteed by a SPV, and investors retain an unsecured claim on the issuer.

CONDITIONS OF REGISTRATION (CONTINUED)

14. That—

  (a) no member of the Banking Group may give effect to a qualifying acquisition or business combination that meets the notification threshold, and does not meet the non-objection threshold, unless:

    (i) the Bank has notified the Reserve Bank in writing of the intended acquisition or business combination and at least 10 working days have passed; and

    (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the Bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document “Significant Acquisitions Policy” (BS15) dated December 2011; and

  (b) no member of the Banking Group may give effect to a qualifying acquisition or business combination that meets the non-objection threshold unless:

    (i) the Bank has notified the Reserve Bank in writing of the intended acquisition or business combination;

    (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the Bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document “Significant Acquisitions Policy” (BS15) dated December 2011; and

    (iii) the Reserve Bank has given the Bank a notice of non-objection to the significant acquisition or business combination.

  For the purposes of this condition of registration, “qualifying acquisition or business combination”, “notification threshold” and “non-objection threshold” have the same meaning as in the Reserve Bank of New Zealand Banking Supervision Handbook document “Significant Acquisitions Policy” (BS15) dated December 2011.

15. That the Bank is pre-positioned for Open Bank Resolution and in accordance with a direction from the Reserve Bank, the Bank can—

  (a) close promptly at any time of the day and on any day of the week and that effective upon the appointment of the statutory manager—

    (i) all liabilities are frozen in full; and

    (ii) no further access by customers and counterparties to their accounts (deposits, liabilities or other obligations) is possible;

  (b) apply a *de minimis* to relevant customer liability accounts;

  (c) apply a partial freeze to the customer liability account balances;

  (d) reopen by no later than 9am the next business day following the appointment of a statutory manager and provide customers access to their unfrozen funds;

  (e) maintain a full freeze on liabilities not pre-positioned for open bank resolution; and

  (f) reinstate customers' access to some or all of their residual frozen funds.

  For the purposes of this condition of registration, “*de minimis*”, “partial freeze”, “customer liability account”, and “frozen and unfrozen funds” have the same meaning as in the Reserve Bank of New Zealand document “Open Bank Resolution (OBR) Pre-positioning Requirements Policy” (BS17) dated September 2013.

16. That the Bank has an Implementation Plan that—

  (a) is up-to-date; and

  (b) demonstrates that the Bank's prepositioning for Open Bank Resolution meets the requirements set out in the Reserve Bank document: "Open Bank Resolution Pre-positioning Requirements Policy" (BS 17) dated September 2013.

  For the purposes of this condition of registration, “Implementation Plan” has the same meaning as in the Reserve Bank of New Zealand document “Open Bank Resolution (OBR) Pre-positioning Requirements Policy” (BS17) dated September 2013.

17. That the Bank has a compendium of liabilities that—

  (a) at the product-class level lists all liabilities, indicating which are—

    (i) pre-positioned for Open Bank Resolution; and

    (ii) not pre-positioned for Open Bank Resolution;

  (b) is agreed to by the Reserve Bank; and

  (c) if the Reserve Bank's agreement is conditional, meets the Reserve Bank's conditions.

  For the purposes of this condition of registration, “compendium of liabilities”, and “pre-positioned and non pre-positioned liabilities” have the same meaning as in the Reserve Bank of New Zealand document “Open Bank Resolution (OBR) Pre-positioning Requirements Policy” (BS17) dated September 2013.

CONDITIONS OF REGISTRATION (CONTINUED)

18. That on an annual basis the Bank tests all the component parts of its Open Bank Resolution solution that demonstrates the Bank's prepositioning for Open Bank Resolution as specified in the Bank's Implementation Plan.

    For the purposes of this condition of registration, “Implementation Plan” has the same meaning as in the Reserve Bank of New Zealand document “Open Bank Resolution (OBR) Pre-positioning Requirements Policy” (BS17) dated September 2013.

19. That, for a loan-to-valuation measurement period, the total of the Bank’s qualifying new mortgage lending amount in respect of property-investment residential mortgage loans with a loan-to-valuation ratio of more than 65%, must not exceed 5% of the total of the qualifying new mortgage lending amount in respect of property-investment residential mortgage loans arising in the loan-to-valuation measurement period.

20. That, for a loan-to-valuation measurement period, the total of the Bank’s qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans with a loan-to-valuation ratio of more than 80%, must not exceed 15% of the total of the qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans arising in the loan-to-valuation measurement period.

21. That the Bank must not make a residential mortgage loan unless the terms and conditions of the loan contract or the terms and conditions for an associated mortgage require that a borrower obtain the registered Bank’s agreement before the borrower can grant to another person a charge over the residential property used as security for the loan.

In these conditions of registration,—

“Banking Group” means Heartland Bank Limited (as reporting entity) and all other entities included in the group as defined in section 6(1) of the Financial Markets Conduct Act 2013 for the purposes of Part 7 of that Act.

"generally accepted accounting practice" has the same meaning as in section 8 of the Financial Reporting Act 2013.

In conditions of registration 19 to 21,—

“loan-to-valuation ratio”, “non property-investment residential mortgage loan”, “property-investment residential mortgage loan”, “qualifying new mortgage lending amount in respect of property-investment residential mortgage loans”, “qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans”, and “residential mortgage loan” have the same meaning as in the Reserve Bank of New Zealand document entitled “Framework for Restrictions on High-LVR Residential Mortgage Lending” (BS19) dated January 2018:

“loan-to-valuation measurement period” means a period of six calendar months ending on the last day of the sixth calendar month, the first of which ends on the last day of June 2018.

PENDING PROCEEDINGS OR ARBITRATION

There are no pending legal proceedings or arbitrations concerning any member of the Banking Group at the date of this Disclosure Statement that may have a material adverse effect on the Bank or the Banking Group.

CREDIT RATINGS

As at the date of signing this Disclosure Statement, the Bank's credit rating issued by Fitch Australia Pty Ltd (Fitch Ratings) was BBB stable. This BBB credit rating was issued on 14 October 2015 and is applicable to long term unsecured obligations payable in New Zealand, in New Zealand dollars. This BBB stable credit rating was affirmed by Fitch Ratings on 3 October 2017.

The following is a summary of the descriptions of the ratings categories for rating agencies for the rating of long-term senior unsecured obligations:

Fitch Ratings	Standard & Poor's	Moody's Investors Service	Description of Grade
AAA	AAA	Aaa	Ability to repay principal and interest is extremely strong. This is the highest investment category.
AA	AA	Aa	Very strong ability to repay principal and interest in a timely manner.
A	A	A	Strong ability to repay principal and interest although somewhat susceptible to adverse changes in economic, business or financial conditions.
BBB	BBB	Baa	Adequate ability to repay principal and interest. More vulnerable to adverse changes.
BB	BB	Ba	Significant uncertainties exist which could affect the payment of principal and interest on a timely basis.
B	B	B	Greater vulnerability and therefore greater likelihood of default.
CCC	CCC	Caa	Likelihood of default considered high. Timely repayment of principal and interest is dependent on favourable financial conditions.
CC - C	CC - C	Ca - C	Highest risk of default.
RD to D	D	-	Obligations currently in default.

Credit ratings from Fitch Ratings and Standard & Poor’s may be modified by the addition of a plus or minus sign to show relative status within the major rating categories. Moody’s Investors Service apply numerical modifiers 1, 2, and 3 to show relative standing within the major rating categories, with 1 indicating the higher end and 3 the lower end of the rating category.

OTHER MATERIAL MATTERS

There are no material matters relating to the business or affairs of the Bank or the Banking Group that are not contained elsewhere in this Disclosure Statement which would, if disclosed in this Disclosure Statement, materially affect the decision of a person to subscribe for debt securities of which the Bank or any member of the Banking Group is the issuer.

GROUP RESTRUCTURE

As announced on the NZX Main Board on 1 August 2018, Heartland Bank is intending to conduct a corporate restructure and seek a Foreign Exempt Listing on the Australian Securities Exchange (ASX).

If approved, the restructure will result in the Bank becoming a wholly owned subsidiary of a new listed holding company (New Listed Company). Existing shareholders' shares in the Bank will be exchanged with new shares in the New Listed Company on a 1-for-1 basis, and the Australian group companies will be transferred from the Bank to the New Listed Company (so that they become "sister" companies of the Bank, rather than subsidiaries). The Bank will remain a registered bank in New Zealand and will continue to operate its New Zealand business in the same way as it does now.

The restructure will be undertaken by way of a scheme of arrangement that must be approved by shareholders and the High Court of New Zealand. The Bank will be asking shareholders to consider and vote on the restructure at its Annual Shareholder Meeting on Wednesday 19 September 2018.

DIRECTORS' STATEMENTS

Each Director of the Bank states that he or she believes, after due enquiry, that:

1. As at the date on which this Disclosure Statement is signed:
   (a) the Disclosure Statement contains all the information that is required by the Order; and
   (b) the Disclosure Statement is not false or misleading.
2. During the year ended 30 June 2018:
   (a) the Bank complied with all Conditions of Registration;
   (b) credit exposures to connected persons were not contrary to the interests of the Banking Group; and
   (c) the Bank had systems in place to monitor and control adequately material risks of the Banking Group, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk and other business risks, and that those systems were being properly applied.

This Disclosure Statement is dated 15 August 2018 and has been signed by all the Directors.

G. T. Ricketts (Chair - Board of Directors)

G. R. Kennedy

J. K. Greenslade

C. R. Mace

E. F. Comerford

V. C. M. Stoddart

E. J. Harvey

G. R. Tomlinson

B. R. Irvine

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 30 June 2018

	NOTE	Jun 2018 $000	Jun 2017 $000
Interest income	2	309,284	278,279
Interest expense	2	125,483	115,169
Net interest income		**183,801**	**163,110**
Operating lease income	3	5,675	6,989
Operating lease expenses	3	4,005	5,195
Net operating lease income		**1,670**	**1,794**
Lending and credit fee income		2,351	3,005
Other income	4	8,972	3,343
Net operating income		**196,794**	**171,252**
Selling and administration expenses	5	80,433	71,684
Profit before impaired asset expense and income tax		**116,361**	**99,568**
Impaired asset expense	6	22,067	15,015
Profit before income tax		**94,294**	**84,553**
Income tax expense	7	26,781	23,745
Profit for the year		**67,513**	**60,808**
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss:			
Effective portion of changes in fair value of cash flow hedges, net of income tax		72	1,108
Movement in available for sale reserve, net of income tax		981	(353)
Movement in foreign currency translation reserve, net of income tax		2,315	761
Items that will not be reclassified to profit or loss:			
Movement in defined benefit reserve, net of income tax		340	(84)
Other comprehensive income / (loss) for the year, net of income tax		**3,708**	**1,432**
Total comprehensive income for the year		**71,221**	**62,240**
Earnings per share from continuing operations			
Basic earnings per share	8	13c	12c
Diluted earnings per share	8	13c	12c

Total comprehensive income for the year is attributable to owners of the Bank.

The notes on pages 16 to 54 are an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

For the year ended 30 June 2018

		Year ended Jun 2018				Year ended Jun 2017			
		Share capital	Reserves	Retained Earnings	Total Equity	Share capital	Reserves	Retained Earnings	Total Equity
	NOTE	$000	$000	$000	$000	$000	$000	$000	$000
Balance at beginning of the year		**470,516**	**1,437**	**97,642**	**569,595**	**418,765**	**765**	**78,811**	**498,341**
Total comprehensive income for the year									
Profit for the year	15	-	-	67,513	67,513	-	-	60,808	60,808
Other comprehensive, net of income tax	15	-	3,708	-	3,708	-	1,432	-	1,432
Total comprehensive income for the year		**-**	**3,708**	**67,513**	**71,221**	**-**	**1,432**	**60,808**	**62,240**
Contributions by and distributions to owners									
Dividends paid	14	-	-	(47,895)	(47,895)	-	-	(41,977)	(41,977)
Dividend reinvestment plan	14	12,745	-	-	12,745	10,590	-	-	10,590
Issue of share capital	14	59,225	-	-	59,225	40,003	-	-	40,003
Capital raising transaction costs		(910)	-	-	(910)	(655)	-	-	(655)
Share based payments	26	-	666	-	666	-	1,053	-	1,053
Shares vested	26	739	(1,226)	-	(487)	1,813	(1,813)	-	-
Total transactions with owners		**71,799**	**(560)**	**(47,895)**	**23,344**	**51,751**	**(760)**	**(41,977)**	**9,014**
Balance at end of the year		**542,315**	**4,585**	**117,260**	**664,160**	**470,516**	**1,437**	**97,642**	**569,595**

The notes on pages 16 to 54 are an integral part of these financial statements.

STATEMENT OF FINANCIAL POSITION
As at 30 June 2018

	NOTE	Jun 2018 $000	Jun 2017 $000
Assets			
Cash and cash equivalents		49,588	57,040
Investments	9	340,546	318,698
Investment properties	10	9,196	4,909
Finance receivables	11	3,984,941	3,545,897
Operating lease vehicles	12	17,524	19,038
Other assets	16(a)	14,411	10,000
Intangible assets	16(b)	74,401	71,237
Deferred tax asset	7(c)	5,319	7,852
Total assets		**4,495,926**	**4,034,671**
Liabilities			
Borrowings	13	3,796,058	3,429,741
Current tax liabilities		11,459	9,856
Trade and other payables	16(c)	24,249	25,479
Total liabilities		**3,831,766**	**3,465,076**
Equity			
Share capital	14	542,315	470,516
Retained earnings and other reserves	15	121,845	99,079
Total equity		**664,160**	**569,595**
Total equity and liabilities		**4,495,926**	**4,034,671**

Total interest earning and discount bearing assets	4,361,014	3,909,711
Total interest and discount bearing liabilities	3,789,144	3,425,685

The notes on pages 16 to 54 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS
For the year ended 30 June 2018

	Note	Jun 2018 $000	Jun 2017 $000
Cash flows from operating activities			
Interest received		280,471	261,339
Operating lease income received		4,941	6,974
Lending, credit fees and other income received		10,398	6,325
Operating inflows		**295,810**	**274,638**
Payments to suppliers and employees		73,672	68,017
Interest paid		123,783	118,616
Taxation paid		23,818	21,695
Operating outflows		**221,273**	**208,328**
Net cash flows from operating activities before changes in operating assets and liabilities		**74,537**	**66,310**
Proceeds from sale of operating lease vehicles		5,577	7,678
Purchase of operating lease vehicles	12	(7,163)	(6,236)
Net movement in finance receivables		(431,863)	(441,400)
Net movement in deposits		307,733	285,551
Total cash applied to operating activities		**(51,179)**	**(88,097)**
Cash flows from investing activities			
Net proceeds from sale of investment properties	10	3,185	3,498
Total cash provided from investing activities		**3,185**	**3,498**
Purchase of office fit-out, equipment and intangible assets		8,837	15,180
Net increase in investments		23,107	82,616
Purchase of investment properties	10	7,472	-
Total cash applied to investing activities		**39,116**	**97,796**
Net cash flows applied to investing activities		**(35,931)**	**(94,298)**
Cash flows from financing activities			
Net increase in wholesale funding		-	147,320
Proceeds from issue of Unsubordinated Notes		150,000	-
Increase in share capital		58,315	39,348
Total cash provided from financing activities		**208,315**	**186,668**
Dividends paid	14	35,150	31,387
Net decrease in wholesale funding		93,507	-
Total cash applied to financing activities		**128,657**	**31,387**
Net cash flows from financing activities		**79,658**	**155,281**
Net decrease increase in cash held		**(7,452)**	**(27,114)**
Opening cash and cash equivalents		57,040	84,154
Closing cash and cash equivalents		**49,588**	**57,040**

The notes on pages 16 to 54 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS
For the year ended 30 June 2018

Reconciliation of profit after tax to net cash flows from operating activities

		Jun 2018 $000	Jun 2017 $000
Profit for the year		**67,513**	**60,808**
Add / (less) non-cash items:			
Depreciation and amortisation expense		4,638	2,376
Depreciation on lease vehicles		3,771	4,701
Capitalised net interest income		(26,373)	(25,815)
Impaired asset expense	6	22,067	15,015
Total non-cash items		**4,103**	**(3,723)**
Add / (less) movements in operating assets and liabilities:			
Finance receivables		(431,863)	(441,400)
Operating lease vehicles		(2,257)	818
Other assets		(635)	5,938
Current tax		1,603	3,102
Derivative financial instruments revaluation		(1,638)	(1,261)
Deferred tax		2,533	(784)
Deposits		307,733	285,551
Other liabilities		1,729	2,854
Total movements in operating assets and liabilities		**(122,795)**	**(145,182)**
Net cash flows applied to operating activities		**(51,179)**	**(88,097)**

The notes on pages 16 to 54 are an integral part of these financial statements.

Basis of reporting

Reporting entity

The financial statements presented are the consolidated financial statements comprising Heartland Bank Limited (the Bank) and its subsidiaries (the Banking Group). Refer to Note 24 - Significant subsidiaries for further details.

As at 30 June 2018 Heartland Bank Limited is a listed public company incorporated in New Zealand under the Companies Act 1993, a registered Bank under the Reserve Bank of New Zealand Act 1989 and a FMC reporting entity for the purposes of the Financial Markets Conduct Act 2013 and the Financial Reporting Act 2013.

Basis of preparation

The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP) and with the requirements of the Financial Markets Conduct Act 2013. The financial statements comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards as appropriate for profit-oriented entities, and the Registered Bank Disclosure Statement (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the Order). The financial statements also comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

The financial statements are presented in New Zealand dollars which is the Bank's functional and the Banking Group's presentation currency. Unless otherwise indicated, amounts are rounded to the nearest thousand.

The accounting policies adopted have been applied consistently throughout the periods presented in these financial statements. Certain comparative information has been restated to comply with the current year presentation.

The financial statements have been prepared on the basis of historical cost, except for certain financial instruments, land and buildings and investment property, which are measured at their fair values as identified in the accounting policies set out in the accompanying notes.

The financial statements have been prepared on a going concern basis after considering the Banking Group's funding and liquidity position.

Principles of consolidation

The consolidated financial statements of the Banking Group incorporate the assets, liabilities and results of all controlled entities. Controlled entities are all entities in which the Bank is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Intercompany transactions, balances and any unrealised income and expense (except for foreign currency transaction gains or losses) between controlled entities are eliminated.

The assets and liabilities of entities whose functional currency is not the New Zealand dollar, are translated at the exchange rates ruling at balance date. Revenue and expense items are translated at the spot rate at the transaction date or a rate approximating that rate. Exchange differences are taken to the foreign currency translation reserve.

Estimates and judgements

The preparation of the Banking Group's financial statements requires the use of estimates and judgement. This note provides an overview of the areas that involve a higher degree of judgement or complexity. Detailed information about each of these estimates and judgements is included in the relevant notes together with the basis of calculation for each affected item in the financial statements.

- **Provisions for impairment** - The effect of credit risk is quantified based on management's best estimate of future cash repayments and proceeds from any security held or by reference to risk profile groupings and historical loss data. Refer to Note 20(e) for further details.
- **Goodwill** - Determining the fair value of assets and liabilities of acquired businesses requires the exercise of management judgement. The carrying value of goodwill is tested annually for impairment, refer to Note 16(b).

The estimates and judgements used in the preparation of the Banking Group's financial statements are continually evaluated. They are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity.

Application of new and revised accounting standards

There were no new standards applied during the year ended 30 June 2018. However, the Banking Group has adopted a number of interpretations and amendments to standards which had an insignificant effect on the consolidated financial statements of the Banking Group. The following new standards relevant to the Banking Group have been issued that are not mandatory for the 30 June 2018 reporting period and have not been early adopted by the Banking Group.

NZ IFRS 9 'Financial Instruments'

The complete version of NZ IFRS 9 'Financial Instruments' was issued in 2014, which is the comprehensive standard to replace NZ IAS 39 'Financial Instruments: Recognition and Measurement', and includes requirements for classification and measurement of financial assets and liabilities, impairment of financial assets and hedge accounting.

Transitional impact
The requirements of NZ IFRS 9 'Financial Instruments' will be adopted from 1 July 2018. NZ IFRS 9 includes an accounting policy choice to continue NZ IAS 39 hedge accounting, which the Banking Group is intending to exercise, although it will implement the revised hedge accounting disclosures required by the related amendments to NZ IFRS 7 'Financial Instruments: Disclosures'. The classification, measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirement to restate comparative periods. The Banking Group does not intend to restate comparatives.

Based on assessments undertaken to date, the total estimated reduction of the Banking Group's equity and assets on the adoption of NZ IFRS 9 at 1 July 2018 is approximately $14 million to $18 million, representing:
- a reduction of approximately $20 million to $25 million related to an increase in the provision for impairment
- a increase of approximately $6 million to $7 million related to deferred tax assets

Application of new and revised accounting standards (continued)

NZ IFRS 9 'Financial Instruments' (continued)

Transitional impact (continued)

The Banking Group estimates that the adoption of IFRS 9 will reduce the Common Equity Tier 1 capital ratio by 0.40% to 0.50% points as at 1 July 2018.

The above assessment is preliminary because not all transition work has been finalised. The actual impact of adopting NZ IFRS 9 on 1 July 2018 may change because:
- the Banking Group is refining and finalising its models for expected credit loss calculations; and
- the new accounting policies, assumptions, judgements and estimation techniques employed are subject to changes until the Banking Group finalises its first financial statements that include the date of initial application.

Impairment of financial assets

The biggest impact will be on the how the Banking Group accounts for credit impairment on its Finance Receivables. NZ IFRS 9 replaces the "incurred loss" model in NZ IAS 39 with a forward-looking expected credit loss (ECL) model.

At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for ECLs resulting from default events that are possible within the next 12 months (12-month ECL). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument (lifetime ECL). Financial assets where 12-month ECL is recognised are in 'stage 1'; financial assets that are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment, so are considered to be in default or otherwise credit impaired, are in 'stage 3'.

The assessment of credit risk and the estimation of ECL are required to be unbiased and probability-weighted, and should incorporate all available information relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money. As a result, the recognition and measurement of impairment is intended to be more forward-looking than under NZ IAS 39. NZ IFRS 9 may also result in an increase in the total level of impairment allowances, since all financial assets will be assessed for at least 12-month ECL and the population of financial assets to which lifetime ECL applies is likely to be larger than the population for which there is objective evidence of impairment in accordance with NZ IAS 39.

Classification and measurement

NZ IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics. These factors determine whether the financial assets are measured at amortised cost ('amortised cost'), fair value through other comprehensive income ('FVOCI') or fair value through profit or loss ('FVPL').

The combined effect of the application of the business model and the contractual cash flow characteristics tests may result in some differences in the group of financial assets measured at amortised cost or fair value compared with NZ IAS 39. In addition, on transition to NZ IFRS 9 entities are required to revoke previous designations of financial assets and financial liabilities measured at fair value through profit or loss where the accounting mismatch no longer exists and are permitted to revoke such designations where accounting mismatches continue to exist.

Under NZ IFRS 9, derivatives embedded in contracts where the host is a financial assets in the scope of NZ IFRS 9 are not separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

NZ IFRS 9 doesn't change the basic accounting model for financial liabilities under NZ IAS 39. Two measurement categories continue to exist: FVPL and amortised cost. Financial liabilities held for trading are measured at FVPL, and all other financial liabilities are measured at amortised cost unless the fair value option is applied.

Impact analysis of classification and measurement requirements

No material impact is expected from the adoption of NZ IFRS 9 in respect of the classification and measurement of financial assets. The classification and measurement of financial assets held as at 1 July 2018 is as follows:
- Derivative assets held for risk management, which are classified as held for trading at fair value through profit or loss under NZ IAS 39, will be measured at FVTPL under NZ IFRS 9.
- Loans and receivables to banks and to customers that are classified as loans and receivables measured at amortised cost under NZ IAS 39 will in general also be measured at amortised cost under NZ IFRS 9. However, the Banking Group will measure the reverse mortgage loan portfolio at fair value through profit and loss.
- Investment securities including local authority stock, bank securities and other bonds that are classified as available for sale under NZ IAS 39 will be measured at FVOCI under NZ IFRS 9.
- Funds with financial institutions that are classified as available for sale under NZ IAS 39 will be measured at amortised cost under NZ IFRS 9.
- Equity investment securities classified at fair value through profit or loss under NZ IAS 39 will be designated at FVOCI as at 1 July 2018 as these investments are held for long term strategic purposes.

Application of new and revised accounting standards (continued)

NZ IFRS 9 'Financial Instruments' (continued)

Hedge accounting

NZ IFRS 9 relaxes the requirements for hedge effectiveness by removing the 80% to 125% hedge effectiveness threshold. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as that used by management for risk management purposes. The Banking Group's preliminary assessment indicates that the hedge accounting relationships currently designated will be capable of meeting the requirements of IFRS 9 and will be easier to designate within a hedge relationship under NZ IFRS 9. Expanded disclosures on hedge accounting introduced by NZ IFRS 9's amendments will be provided in future financial statements.

NZ IFRS 15 'Revenue from Contracts with Customers'

NZ IFRS 15 'Revenue from Contracts with Customers' is effective for annual periods beginning on or after 1 January 2018. NZ IFRS 15 provides a principles-based approach for revenue recognition, and introduces the concept of recognising revenue for performance obligations as they are satisfied. The Banking Group will adopt the standard on its mandatory effective date, and the standard will be applied on a retrospective basis, recognising the cumulative effect, if any, of initially applying the standard as an adjustment to the opening balance of retained earnings. The Banking Group has assessed the impact of NZ IFRS 15 and expects that the standard will have no significant effect, when applied, on the financial statements of the Banking Group.

Other standards and interpretations not yet adopted are set out in the table below.

Standard and description	*Effective for annual years beginning on or after:*	*Expected to be initially applied in year ending:*
NZ IFRS 16 Leases, contains guidance on identification, recognition, measurement, presentation, and disclosure of leases by lessees and lessors.	1 Jan 2019	30 Jun 2020
NZ IFRS 17 Insurance contracts, establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts.	1 Jan 2021	30 Jun 2022

The Banking Group is currently assessing the impact of NZ IFRS 16 and NZ IFRS 17, and it is not practicable to quantify the effect at the date of the publication of these financial statements

Financial assets and liabilities

The Banking Group initially recognises finance receivables and borrowings on the date that they are originated. All other financial assets and liabilities (including assets and liabilities designated at fair value through profit or loss) are initially recognised on the trade date at which the Banking Group becomes a party to the contractual provisions of the instrument.

The Banking Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Banking Group is recognised as a separate asset or liability.

The Banking Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

The Banking Group enters into transactions whereby it transfers assets recognised on its Statement of Financial Position, but retains either all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the Statement of Financial Position. Transfers of assets with the retention of all or substantially all risks and rewards include, for example, securitised assets and repurchase transactions.

Offsetting financial instruments

The Banking Group offsets financial assets and financial liabilities and reports the net balance in the balance sheet where there is currently a legally enforceable right to set off and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

Performance

1 Segmental analysis

Segment information is presented in respect of the Banking Group's operating segments which are those used for the Banking Group's management and internal reporting structure.

All income received is from external sources. Certain selling and administration expenses, such as premises, IT and support centre costs are not allocated to operating segments and are included in Administration and Support (Admin & Support).

Operating segments

The Banking Group operates predominantly within New Zealand and Australia and comprises the following main operating segments:

Households Providing both a comprehensive range of financial services to New Zealand families - including term, transactional and savings based deposit accounts together with mortgage lending (residential and reverse mortgage), motor vehicle finance and consumer finance - as well as reverse mortgage lending and other financial services to Australian families.

Business Providing term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium sized businesses.

Rural Providing specialist financial services to the farming sector primarily offering livestock finance, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers.

The Banking Group's operating segments are different from the industry categories detailed in Note 20 - Asset quality. The operating segments are primarily categorised by sales channel, whereas Note 20 - Asset quality categorises exposures based on credit risk concentrations.

	Households $000	Business $000	Rural $000	Admin & Support $000	Total $000
Jun 2018					
Net interest income	99,504	52,086	32,122	89	183,801
Net other income	5,291	1,113	165	6,424	12,993
Net operating income	**104,795**	**53,199**	**32,287**	**6,513**	**196,794**
Selling and administration expenses	14,339	8,130	4,351	53,613	80,433
Profit / (loss) before impaired asset expense and income tax	**90,456**	**45,069**	**27,936**	**(47,100)**	**116,361**
Impaired asset expense	13,048	7,862	1,157	-	22,067
Profit / (loss) before income tax	**77,408**	**37,207**	**26,779**	**(47,100)**	**94,294**
Income tax expense	-	-	-	26,781	26,781
Profit / (loss) for the year	**77,408**	**37,207**	**26,779**	**(73,881)**	**67,513**
Total assets	2,280,876	1,074,607	656,178	484,265	**4,495,926**
Total liabilities					**3,831,766**

	Households $000	Business $000	Rural $000	Admin & Support $000	Total $000
Jun 2017					
Net interest income	88,346	45,431	29,087	246	163,110
Net other income	4,514	1,629	139	1,860	8,142
Net operating income	**92,860**	**47,060**	**29,226**	**2,106**	**171,252**
Selling and administration expenses	13,980	8,195	4,356	45,153	71,684
Profit / (loss) before impaired asset expense and income tax	**78,880**	**38,865**	**24,870**	**(43,047)**	**99,568**
Impaired asset expense	10,321	4,377	317	-	15,015
Profit / (loss) before income tax	**68,559**	**34,488**	**24,553**	**(43,047)**	**84,553**
Income tax expense	-	-	-	23,745	23,745
Profit / (loss) for the year	**68,559**	**34,488**	**24,553**	**(66,792)**	**60,808**
Total assets	1,894,514	999,891	675,439	464,827	**4,034,671**
Total liabilities					**3,465,076**

The Households segment includes Finance Receivables of $702.7 million which are located in Australia (2017: $517.5 million) and has derived net operating income of $16.0 million from customers in Australia (2017: $11.0 million). The Business segment includes Finance Receivables of $18.6 million which are located in Australia (2017: $3.1 million) and has derived net operating income of $0.5 million from customers in Australia (2017: $0.08 million). All other assets and income have been derived from New Zealand.

Included within Households segment are reverse mortgages of $1,130.0 million (2017: $920.8 million) of which $453.1 million are located in New Zealand (2017: $403.3 million) and $676.9 million are located in Australia (2017: $517.5 million). Reverse mortgage loans are a form of mortgage lending targeted toward the seniors market. These loans differ to conventional mortgages in that they typically are not repaid until the borrower ceases to reside in the property. Further, interest is not required to be paid, it is capitalised with the loan balance and is repayable on termination of the loan. The Banking Group offers a no negative equity guarantee to customers, which means that they can reside in their property for 'as long as they wish' and repayment of their loan is limited to the net sale proceeds of their property. For further details refer to Note 19 - Credit Risk.

2 Net interest income

Interest income and expense is recognised in profit or loss using the effective interest method. The effective interest rate is established on initial recognition of the financial assets and liabilities and is not revised subsequently. The calculation of the effective interest rate includes all yield related fees and commissions paid or received that are an integral part of the effective interest rate.

Interest on the effective portion of a derivative designated as a cash flow hedge is initially recognised in the hedging reserve. It is released to profit or loss at the same time as the hedged item or when the hedge relationship is subsequently deemed to be ineffective, should this occur.

	NOTE	Jun 2018 $000	Jun 2017 $000
Interest income			
Cash and cash equivalents		842	825
Investments		9,515	8,966
Finance receivables		298,927	268,488
Total interest income		**309,284**	**278,279**
Interest expense			
Retail deposits		90,880	86,692
Subordinated Notes	13	1,368	326
Unsubordinated Notes	13	5,228	-
Bank and securitised borrowings		25,380	25,714
Net interest expense on derivative financial instruments		2,627	2,437
Total interest expense		**125,483**	**115,169**
Net interest income		**183,801**	**163,110**

3 Net operating lease income

Leases where the Banking Group retains substantially all the risks and rewards of ownership of an asset are classified as operating leases. Rental income and expense from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term. Profits on the sale of operating lease assets are included as part of operating lease income. Current year depreciation and losses on the sale of operating lease assets are included as part of operating lease expenses. The leased assets are depreciated over their useful lives on a basis consistent with similar assets.

	Jun 2018 $000	Jun 2017 $000
Operating lease income		
Lease income	5,004	6,365
Gain on disposal of lease assets	671	624
Total operating lease income	**5,675**	**6,989**
Operating lease expense		
Depreciation on lease assets	3,771	4,701
Direct lease costs	234	494
Total operating lease expenses	**4,005**	**5,195**
Net operating lease income	**1,670**	**1,794**

4 Other income

Rental income from investment properties is recognised on a straight-line basis over the term of the relevant lease. Other items of income are recognised at the fair value of the consideration received or receivable, net of the amount of goods and services tax (GST) levied.

	Jun 2018 $000	Jun 2017 $000
Rental income from investment properties	739	887
Insurance income	2,238	1,783
Gain on sale of investments	156	628
Other income[1]	5,839	45
Total other income	**8,972**	**3,343**

[1] Other income includes:
- a $0.6 million gain on the sale of the Bank's invoice finance business.
- a $4.8 million gain in relation to the sale of property pertaining to a loan previously written off for which the bank had entered into a profit share arrangement with third parties.

5 Selling and administration expenses

	Jun 2018 $000	Jun 2017 $000
Personnel expenses	45,539	40,766
Directors' fees	972	769
Superannuation	921	781
Audit and review of financial statements[1]	433	454
Other assurance services paid to auditor[2]	36	44
Other fees paid to auditor[3]	171	143
Depreciation - property, plant and equipment	1,386	1,361
Amortisation - intangible assets	3,252	1,015
Operating lease expense as a lessee	2,033	2,102
Legal and professional fees	2,267	1,698
Other operating expenses	23,423	22,551
Total selling and administration expenses	**80,433**	**71,684**

[1] Audit and review of financial statements includes fees paid for both the audit of annual financial statements and review of interim financial statements.

[2] Other assurance services paid to the auditor comprise review of regulatory assurance services, agreed upon procedures engagements and supervisor reporting.

[3] Other fees paid to the auditor include professional fees in connection with health and safety advisory services, and tax, regulatory and accounting advisory services.

6 Impaired asset expense

	NOTE	Jun 2018 $000	Jun 2017 $000
Non-securitised			
Individually impaired asset expense		5,190	4,505
Collectively impaired asset expense		16,889	9,199
Total non-securitised impaired asset expense		**22,079**	**13,704**
Securitised			
Collectively impaired asset (benefit) / expense		(12)	1,311
Total securitised impaired asset expense		**(12)**	**1,311**
Total			
Individually impaired asset expense	20(e)	5,190	4,505
Collectively impaired asset expense	20(e)	16,877	10,510
Total impaired asset expense		**22,067**	**15,015**

7 Taxation

(a) Income tax expense

Income tax expense for the year comprises current tax and movements in deferred tax balances. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in equity or other comprehensive income.

	Jun 2018 $000	Jun 2017 $000
Income tax recognised in profit or loss		
Current tax		
Current year	24,861	25,025
Adjustments for prior year	(332)	(29)
Deferred tax		
Current year	1,898	(953)
Adjustments for prior year	354	(298)
Income tax expense recognised in profit or loss	**26,781**	**23,745**

7 Taxation (continued)

(a) Income tax expense (continued)

	Jun 2018 $000	Jun 2017 $000
Income tax recognised in other comprehensive income		
Current tax		
Fair value movements of available for sale investments and derivatives	(261)	205
Deferred tax		
Defined benefit plan	(132)	33
Fair value movements of cash flow hedges	(149)	(500)
Income tax benefit recognised in other comprehensive income	**(542)**	**(262)**

	Jun 2018 $000	Jun 2017 $000
Reconciliation of effective tax rate		
Profit before income tax	94,294	84,553
Prima facie tax at 28%	26,402	23,675
Higher tax rate for overseas jurisdiction	299	212
Plus tax effect of items not taxable / deductible	58	185
Adjustments for prior year	22	(327)
Total income tax expense	**26,781**	**23,745**

(b) Current tax

Current tax is the expected tax receivable or payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to the tax receivable or payable in respect of previous years. Current tax for current and prior years is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

(c) Deferred tax

The Banking Group has recognised deferred tax assets, including those relating to the tax effects of income tax losses and credits available to be carried forward, to the extent that there are sufficient taxable temporary differences (deferred tax liabilities) relating to the same taxation authority and the same subsidiary against which the unused tax losses can be utilised.

Deferred tax assets comprise the following temporary differences:

	Jun 2018 $000	Jun 2017 $000
Employee entitlements	1,240	1,323
Provision for impairment	8,427	7,601
Investment properties	546	1,044
Intangibles and property, plant and equipment	(2,100)	(342)
Deferred acquisition costs	(1,476)	(1,369)
Operating lease vehicles	(850)	(905)
Other temporary differences	(468)	500
Total deferred tax assets	**5,319**	**7,852**

	Jun 2018 $000	Jun 2017 $000
Opening balance of deferred tax assets	**7,852**	**7,068**
Movement recognised in profit or loss	(2,252)	1,251
Movement recognised in other comprehensive income	(281)	(467)
Closing balance of deferred tax assets	**5,319**	**7,852**

(d) Goods and services tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST. As the Banking Group is predominantly involved in providing financial services, only a proportion of GST paid on inputs is recoverable. The non-recoverable proportion of GST is treated as part of the cost of acquisition of the asset or is expensed.

(e) Imputation credit account

	Jun 2018 $000	Jun 2017 $000
Imputation credit account	6,717	5,799

8 Earnings per share

	Jun 2018			Jun 2017		
	Earnings per share	Net profit after tax	Weighted average no. of shares	Earnings per share	Net profit after tax	Weighted average no. of shares
	cents	$000	000	cents	$000	000
Basic earnings	13	67,513	538,594	12	60,808	493,177
Diluted earnings	13	67,513	538,594	12	60,808	496,725

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of fully paid shares less treasury shares.

Financial Position

9 Investments

The Banking Group holds investments in bank deposits, bank bonds and floating rate notes, local authority stock, public securities, corporate bonds and equity investments. Equity investments are classified as being fair valued through profit or loss and the fair value is based on unobservable inputs. All other investments held are classified as being available for sale and are stated at fair value less impairment, if any. The fair values are derived by reference to published price quotations in an active market or modelled using observable market inputs.

	Jun 2018	Jun 2017
	$000	$000
Bank deposits, bank bonds and floating rate notes	230,754	237,416
Public sector securities and corporate bonds	57,818	16,055
Local authority stock	42,280	53,436
Equity investments	9,694	11,791
Total investments	**340,546**	**318,698**

10 Investment properties

Investment properties have been acquired through the enforcement of security over finance receivables and are held to earn rental income or for capital appreciation (or both).

Investment properties are initially recorded at their fair value, with subsequent changes in fair value recognised in profit or loss. Fair values are determined by qualified independent valuers or other similar external evidence, adjusted for changes in market conditions and the time since the last valuation.

	Jun 2018	Jun 2017
	$000	$000
Opening balance	4,909	8,384
Acquisition	7,472	-
Sales	(3,185)	(3,475)
Closing balance	**9,196**	**4,909**

11 Finance receivables

Finance receivables are initially recognised at fair value plus incremental direct transaction costs and are subsequently measured at amortised cost using the effective interest method, less any impairment loss.

Fees and direct costs relating to loan origination, financing and loan commitments are deferred and amortised to interest income over the life of the loan using the effective interest method. Lending fees not directly related to the origination of a loan are recognised over the period of service.

Past due but not impaired assets are any assets which have not been operated by the counterparty within their key terms but are not considered to be impaired by the Banking Group.

Individually impaired assets are those loans for which the Banking Group has evidence that it will incur a loss, and will be unable to collect all principal and interest due according to the contractual terms of the loan.

Credit impairment provisions are made where events have occurred leading to an expectation of reduced future cash flows from certain receivables. These provisions are made in some cases against an individual loan and in other cases on a collective basis. When it becomes clear that there is little likelihood or recovery the loan is written off against the related provision for impairment. In most cases this will be following the realisation of tangible security.

11 Finance receivables (continued)

	NOTE	Jun 2018 $000	Jun 2017 $000
Non-securitised			
Neither at least 90 days past due nor impaired[1]		3,863,764	3,282,405
At least 90 days past due		27,893	33,047
Individually impaired[1]		45,186	32,084
Gross finance receivables		**3,936,843**	**3,347,536**
Less provision for impairment		(29,367)	(24,762)
Less fair value adjustment for present value of future losses[2]		(2,824)	(3,851)
Total non-securitised finance receivables		**3,904,652**	**3,318,923**
Securitised			
Neither at least 90 days past due nor impaired		79,809	225,495
At least 90 days past due		784	2,582
Gross finance receivables		**80,593**	**228,077**
Less provision for impairment		(304)	(1,103)
Total securitised finance receivables		**80,289**	**226,974**
Total			
Neither at least 90 days past due nor impaired		3,943,573	3,507,900
At least 90 days past due	20(b)	28,677	35,629
Individually impaired	20(c)	45,186	32,084
Gross finance receivables		**4,017,436**	**3,575,613**
Less provision for impairment	20(e)	(29,671)	(25,865)
Less fair value adjustment for present value of future losses[2]	20(a)	(2,824)	(3,851)
Total finance receivables		**3,984,941**	**3,545,897**

Refer to Note 20 - Asset quality for further analysis of finance receivables by credit risk concentration.

[1] A $3.5m reclassification of restructured loans from 'Neither at least 90 days past due nor impaired' to 'Individually impaired' has been made in respect of the year ended 30 June 2017.

[2] A fair value adjustment of $8m for the present value of future losses was recognised on acquisition of New Sentinel Limited and Australian Seniors Finance Pty Limited. This fair value adjustment is being amortised over the estimated lifetime of the finance receivables acquired.

Finance lease receivables

Included in finance receivables are finance leases. Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. Amounts due from finance leases are recognised as finance receivables at the amount of the Banking Group's net investment in the leases. The difference between the gross finance receivable and the present value of the receivable is treated as unearned finance income. Lease income is recognised over the lease term so as to produce a constant periodic rate of return on the net investment in the finance lease. The table below provides an analysis of finance lease receivables for leases of certain property and equipment in which the Banking Group is the lessor.

	Jun 2018 $000	Jun 2017 $000
Finance lease receivables included in finance receivables		
Gross finance lease receivables included		
Less than 1 year	25,438	23,628
Between 1 and 5 years	42,664	38,748
More than 5 years	1	-
Total gross finance lease receivables	**68,103**	**62,376**
Less unearned finance income	(10,124)	(9,465)
Less provision for impairment	(199)	(156)
Net finance lease receivables	**57,780**	**52,755**

12 Operating lease vehicles

Operating lease vehicles are stated at cost less accumulated depreciation.

Operating lease vehicles are depreciated on a straight line basis over their expected life after allowing for any residual values. The estimated lives of these vehicles vary up to five years. Vehicles held for sale are not depreciated but are tested for impairment.

	Jun 2018 $000	Jun 2017 $000
Cost		
Opening balance	28,137	35,728
Additions	7,163	6,236
Disposals	(10,597)	(13,827)
Closing balance	**24,703**	**28,137**
Accumulated depreciation		
Opening balance	9,099	11,171
Depreciation charge for the year	3,771	4,701
Disposals	(5,691)	(6,773)
Closing balance	**7,179**	**9,099**
Opening net book value	19,038	24,557
Closing net book value	**17,524**	**19,038**

The future minimum lease payments receivable under non-cancellable operating leases not later than one year is $4.380 million (2017: $5.022 million), within one to five years is $3.897 million (2017: $3.644 million) and over five years is nil (2017: nil).

13 Borrowings

Bank borrowings and deposits are initially recognised at fair value including incremental direct transaction costs. They are subsequently measured at amortised cost using the effective interest method.

	Note	Jun 2018 $000	Jun 2017 $000
Deposits		2,881,805	2,573,980
Subordinated Bonds		3,378	3,378
Subordinated Notes		22,172	21,180
Unsubordinated Notes		151,853	-
Bank borrowings		689,346	616,838
Securitised borrowings		47,504	214,365
Total borrowings		**3,796,058**	**3,429,741**

On 21 September 2017, the Bank issued unsubordinated fixed rate notes (Unsubordinated Notes). These notes are paid a fixed rate of interest every 6 months and will mature on 21 September 2022.

The Subordinated Bonds and Subordinated Notes rank below all other general liabilities of the Banking Group. All other liabilities including Deposits and Unsubordinated notes rank equally and are unsecured.

Securitised borrowings held by investors in Heartland ABCP Trust 1 (ABCP Trust) rank equally with each other and are secured over the securitised assets of that trust. Securitised borrowings comprise notes issued by ABCP Trust and drawings under the ABCP Trust's bank facilities. The ABCP Trust has bank facilities of $100 million (2017: $300 million) which mature on 31 August 2018.

The Banking Group has an Australian Bank facility provided by Commonwealth Bank of Australia (CBA Bank facility) totalling AUD $600 million, with AUD $562 million drawn (2017: AUD $440 million). The CBA Bank facility is secured over the shares in Australian Seniors Finance Pty Limited (ASF) and the assets of the ASF Group (comprising ASF, the ASF Settlement Trust and the Seniors Warehouse Trust). The CBA Bank facility has a maturity date of 30 September 2019.

The banking agreements include covenants for the provision of information, attainment of minimum financial ratios and equity, compliance with specified procedures and certification of due performance by ASF Group.

14 Share capital and dividends

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

	Jun 2018 Number of shares 000	Jun 2017 Number of shares 000
Issued shares		
Opening balance	516,236	476,469
Shares issued during the year	37,224	32,860
Dividend reinvestment plan	7,128	6,907
Closing balance	**560,588**	**516,236**
Less treasury shares[1]	(2,299)	(2,299)
Net closing balance	**558,289**	**513,937**

[1] Included in the Bank's share capital are treasury shares of $2.6 million (2017: $2.6million)

On 14 December 2017, the Bank issued 34,838,414 new shares at $1.70 per share under a Pro Rata Rights Offer. Other shares issued during the period relate to staff share schemes.

Under dividend reinvestment plans, the Banking Group issued 4,163,008 new shares at $1.8004 per share on 21 September 2017 and 2,965,048 new shares at $1.7707 per share on 3 April 2018 (June 2017: 3,573,104 new shares at $1.4766 per share on 7 October 2016 and 3,334,049 new shares at $1.5939 per share on 7 April 2017).

The shares have equal voting rights, rights to dividends and distributions and do not have a par value.

Dividends paid

	Jun 2018 date declared	Jun 2018 cents per share	Jun 2018 $000	Jun 2017 date declared	Jun 2017 cents per share	Jun 2017 $000
Final dividend	14 Aug 2017	5.5	28,393	16 Aug 2016	5.0	24,041
Interim dividend	20 Feb 2018	3.5	19,502	21 Feb 2017	3.5	17,936
Total dividends paid		**9.0**	**47,895**		**8.5**	**41,977**

On 15 August 2018, the Board declared a final dividend for the 2018 financial year of 5.5 cents per Ordinary Share, payable on 21 September 2018 to registered shareholders at 7 September 2018. This final dividend has not been recognised within these financial statements.

15 Retained earnings and other reserves

	Retained Earnings $000	Employee Benefits Reserve $000	Foreign Currency Translation Reserve $000	Available for Sale Reserve $000	Defined Benefit Reserve $000	Hedging Reserve $000	Total $000
Balance 1 July 2017	97,642	3,118	(1,055)	609	(83)	(1,152)	99,079
Profit for the year	67,513	-	-	-	-	-	67,513
Other comprehensive income, net of income tax	-	-	2,315	981	340	72	3,708
Dividends paid	(47,895)	-	-	-	-	-	(47,895)
Share based payments	-	666	-	-	-	-	666
Shares vested	-	(1,226)	-	-	-	-	(1,226)
Balance 30 June 2018	**117,260**	**2,558**	**1,260**	**1,590**	**257**	**(1,080)**	**121,845**
Balance 1 July 2016	78,811	3,878	(1,816)	962	1	(2,260)	79,576
Profit for the year	60,808	-	-	-	-	-	60,808
Other comprehensive income (loss), net of income tax	-	-	761	(353)	(84)	1,108	1,432
Dividends paid	(41,977)	-	-	-	-	-	(41,977)
Share based payments	-	1,053	-	-	-	-	1,053
Shares vested	-	(1,813)	-	-	-	-	(1,813)
Balance 30 June 2017	**97,642**	**3,118**	**(1,055)**	**609**	**(83)**	**(1,152)**	**99,079**

16 Other balance sheet items

(a) Other assets

	Jun 2018 $000	Jun 2017 $000
Trade receivables	1,613	101
GST receivable	1,553	1,128
Prepayments	2,261	822
Property, plant and equipment	8,984	7,949
Total other assets	**14,411**	**10,000**

Property, plant and equipment are stated at cost less accumulated depreciation and impairment. Depreciation is calculated on a straight line basis to write off the net cost or other revalued amount of each asset over its expected useful life to its estimated residual value.

(b) Intangible assets

Intangible assets with finite useful lives
Software acquired or internally developed by the Banking Group is stated at cost less accumulated amortisation and any accumulated impairment losses. Subsequent expenditure on software assets is capitalised only when it increases the future economic value of that asset. Amortisation of software is on a straight line basis, at rates which will write off the cost over their estimated economic lives. All other expenditure is expensed immediately as incurred.

Goodwill
Goodwill arising on acquisition represents the excess of the cost of the acquisition over the Banking Group's interest in the fair value of the identifiable net assets of a controlled entity. Goodwill that has an indefinite useful life is not subject to amortisation and is tested for impairment annually. Goodwill is carried at cost less accumulated impairment losses.

	Jun 2018 $000	Jun 2017 $000
Computer software		
Cost	36,215	31,543
Accumulated amortisation	6,957	5,449
Net carrying amount of computer software	**29,258**	**26,094**
Net carrying amount of goodwill	**45,143**	**45,143**
Total intangible assets	**74,401**	**71,237**

A significant portion of the computer software costs relate to the core Banking system replacement which the Bank brought into use in May 2017. The expected useful life of the new core Banking system has been determined to be ten years.

Goodwill was tested for impairment as at 30 June 2018. In assessing impairment, an internal valuation model was developed to indicate the value of the business. This value was compared to the net assets of the Banking Group. There was no indication of impairment and no impairment losses have been recognised against the carrying amount of goodwill for the year ended 30 June 2018 (30 June 2017: nil).

The Banking Group has assessed that goodwill should be allocated to the Banking Group as a cash-generating unit (CGU), at which goodwill is assessed for impairment and to which any future economic benefit will arise.

Assumptions are used to determine the CGU's recoverable amount for goodwill, which is based on value-in-use calculations. Value-in-use refers to the present value of expected cash flows under its current use. The Banking Group discounts the projected cash flows by an assumed cost of equity.

(c) Trade and other payables

Derivative financial liabilities consist of interest rate swaps held to manage the Banking Group's exposure to interest rate repricing risk arising from fixed rate mortgage loans.

Annual leave entitlements are accrued at amounts expected to be paid. Long service leave is accrued by calculating the probable future value of entitlements and discounting back to present value. Obligations to defined contribution superannuation schemes are recognised as an expense when the contribution is paid.

	Jun 2018 $000	Jun 2017 $000
Derivative financial liabilities	1,639	3,349
Trade payables	10,406	10,697
Insurance liability	6,333	5,927
Employee benefits	5,871	5,506
Total trade and other payables	**24,249**	**25,479**

16 Other balance sheet items (continued)

(d) Related party transactions

Heartland Cash and Term PIE Fund and some key management personnel invested in the Bank's deposits. The investments of Heartland Cash and Term PIE Fund are detailed in Note 25 - Structured entities.

Transactions with key management personnel

Key management personnel (KMP), being directors of the Bank, the Chief Executive Officer (CEO), those executive staff reporting directly to the CEO, and their immediate relatives, have transacted with the Banking Group during the period as follows:

Loans made to KMPs are made in the ordinary course of business on normal commercial terms and conditions no more favourable than those given to other employees or customers, including the term of the loan, security required and the interest rate.

All other transactions with KMPs and their related entities are made on terms equivalent to those that prevail in arm's length transactions.

	Jun 2018 $000	Jun 2017 $000
Transactions with key management personnel		
Interest income	5	8
Interest expense	(128)	(691)
Key management personnel compensation:		
Short-term employee benefits	(6,194)	(5,020)
Share-based payment expense	(640)	(813)
Total transactions with key management personnel	**(6,957)**	**(6,516)**

Due (to) / from key management personnel		
Finance receivables	-	71
Borrowings - deposits	(2,412)	(9,153)
Total due (to) / from key management personnel	**(2,412)**	**(9,082)**

17 Fair value

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Banking Group determines fair value using other valuation techniques.

The Banking Group measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements.

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (derived from prices).
- Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Banking Group recognises transfers between levels of the fair value hierarchy as at the end of the reporting period during which the change has occurred.

(a) Financial instruments measured at fair value

The following methods and assumptions were used to estimate the fair value of each class of financial asset and liability measured at fair value on a recurring basis in the Statement of Financial Position.

Investments

Investments in public sector securities and corporate bonds are classified as being available for sale and are stated at fair value, with the fair value being based on quoted market prices (Level 1 under the fair value hierarchy) or modelled using observable market inputs (Level 2 under the fair value hierarchy). Refer to Note 9 - Investments for more details.

Investments valued under Level 2 of the fair value hierarchy are valued either based on quoted market prices or dealer quotes for similar instruments, or discounted cash flows analysis.

Investments in unlisted equity securities are classified as being fair valued through profit or loss and are valued under Level 3 of the fair value hierarchy, with the fair value being based on unobservable inputs.

Finance receivables

Fixed rate reverse mortgage loans classified as finance receivables are stated at fair value with the fair value being based on present value of future cash flows discounted using observable market interest rates (Level 2 under the fair value hierarchy).

17 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

Derivative items

Interest rate swaps are classified as held for trading and are recognised in the financial statements at fair value. Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are determined on the basis of discounted cash flow analysis using observable market prices and adjustments for counterparty credit spreads. (Level 2 under the fair value hierarchy).

The following table analyses financial instruments measured at fair value at the reporting date by the level in the fair value hierarchy into which each fair value measurement is categorised. The amounts are based on the values recognised in the Statement of Financial Position.

	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
Jun 2018				
Investments	140,282	190,570	9,694	340,546
Finance receivables	-	454	-	454
Total assets measured at fair value	**140,282**	**191,024**	**9,694**	**341,000**
Derivative liabilities held for risk management	-	1,639	-	1,639
Total liabilities measured at fair value	**-**	**1,639**	**-**	**1,639**
Jun 2017				
Investments	145,503	161,404	11,791	318,698
Finance receivables	-	11,211	-	11,211
Total assets measured at fair value	**306,907**	**11,211**	**11,791**	**329,909**
Derivative liabilities held for risk management	-	3,349	-	3,349
Total liabilities measured at fair value	**-**	**3,349**	**-**	**3,349**

(b) Financial instruments not measured at fair value

The following methods and assumptions were used to estimate the fair value of each class of financial assets and liabilities not recognised at fair value but for which fair value is calculated for disclosure purposes under Level 2 or 3 of the fair value hierarchy.

Cash and cash equivalents and other financial assets and liabilities

The fair value of all cash and cash equivalents and other financial assets and liabilities is considered equivalent to their carrying value due to their short term nature.

Finance receivables

The fair value of the Banking Group's finance receivables is calculated using a valuation technique which assumes the Banking Group's current weighted average lending rates for loans of a similar nature and term.

The current weighted average lending rate used to fair value finance receivables with a fixed interest rate was 8.12% (2017: 8.72%). Finance receivables with a floating interest rate are deemed to be at current market rates. The current amount of credit provisioning has been deducted from the fair value calculation of finance receivables as a proxy for future losses. Prepayment rates have not been factored into the fair value calculation as they are not deemed to be material.

Borrowings

The fair value of deposits, bank borrowings and other borrowings is the present value of future cash flows and is based on the current market interest rates payable by the Banking Group for debt of similar maturities. The current market rate used to fair value borrowings was 3.09% (2017: 3.19%).

Other financial assets and financial liabilities

The Banking Group has not disclosed the fair values for financial instruments such as short-term trade receivables and payables, because their carrying amounts are a reasonable approximation of fair values.

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorised.

17 Fair value (continued)

(b) Financial instruments not measured at fair value (continued)

	Level 1	Level 2	Level 3	Total Fair Value	Total Carrying Value
	$000	$000	$000	$000	$000
Jun 2018					
Cash and cash equivalents	49,588	-	-	49,588	49,588
Finance receivables	-	-	3,891,458	3,891,458	3,904,198
Finance receivables - securitised	-	-	80,614	80,614	80,289
Other financial assets	-	-	1,613	1,613	1,613
Total financial assets	**49,588**	**-**	**3,973,685**	**4,023,273**	**4,035,688**
Borrowings	-	3,744,634	-	3,744,634	3,748,554
Borrowings - securitised	-	47,504	-	47,504	47,504
Other financial liabilities	-	-	22,610	22,610	22,610
Total financial liabilities	**-**	**3,792,138**	**22,610**	**3,814,748**	**3,818,668**
Jun 2017					
Cash and cash equivalents	57,040	-	-	57,040	57,040
Finance receivables	-	-	3,300,325	3,300,325	3,307,712
Finance receivables - securitised	-	-	227,166	227,166	226,974
Other financial assets	-	-	101	101	101
Total financial assets	**57,040**	**-**	**3,527,592**	**3,584,632**	**3,591,827**
Borrowings	-	3,220,344	-	3,220,344	3,215,376
Borrowings - securitised	-	214,365	-	214,365	214,365
Other financial liabilities	-	-	22,130	22,130	22,130
Total financial liabilities	**-**	**3,434,709**	**22,130**	**3,456,839**	**3,451,871**

(c) Classification of financial instruments

The following tables summarise the categories of financial instruments and the carrying value and fair value of all financial instruments of the Banking Group:

	Held for trading	Fair value through profit or loss	Loans and receivables	Available for sale	Financial liabilities at amortised cost	Total Carrying Value	Total Fair Value
	$000	$000	$000	$000	$000	$000	$000
Jun 2018							
Cash and cash equivalents	-	-	49,588	-	-	49,588	49,588
Investments	-	9,694	-	330,852	-	340,546	340,546
Finance receivables	-	-	3,904,652	-	-	3,904,652	3,891,912
Finance receivables - securitised	-	-	80,289	-	-	80,289	80,614
Other financial assets	-	-	1,613	-	-	1,613	1,613
Total financial assets	**-**	**9,694**	**4,036,142**	**330,852**	**-**	**4,376,688**	**4,364,273**
Borrowings	-	-	-	-	3,748,554	3,748,554	3,744,634
Borrowings - securitised	-	-	-	-	47,504	47,504	47,504
Derivative financial liabilities	1,639	-	-	-	-	1,639	1,639
Other financial liabilities	-	-	-	-	22,610	22,610	22,610
Total financial liabilities	**1,639**	**-**	**-**	**-**	**3,818,668**	**3,820,307**	**3,816,387**
Jun 2017							
Cash and cash equivalents	-	-	57,040	-	-	57,040	57,040
Investments	-	11,791	-	306,907	-	318,698	318,698
Finance receivables	-	-	3,318,923	-	-	3,318,923	3,311,536
Finance receivables - securitised	-	-	226,974	-	-	226,974	227,166
Other financial assets	-	-	101	-	-	101	101
Total financial assets	**-**	**11,791**	**3,603,038**	**306,907**	**-**	**3,921,736**	**3,914,541**
Borrowings	-	-	-	-	3,215,376	3,215,376	3,220,344
Borrowings - securitised	-	-	-	-	214,365	214,365	214,365
Derivative financial liabilities	3,349	-	-	-	-	3,349	3,349
Other financial liabilities	-	-	-	-	22,130	22,130	22,130
Total financial liabilities	**3,349**	**-**	**-**	**-**	**3,451,871**	**3,455,220**	**3,460,188**

Risk Management

18 Enterprise risk management program

The board of directors (the Board) sets and monitors the Banking Group's risk appetite across five primary risk domains; credit, liquidity, market (including interest rate), operational & compliance, and general business risk. Management are, in turn, responsible for ensuring appropriate structures, policies, procedures, and information systems are in place to actively manage these risk domains. Collectively, these processes are known as the Banking Group's Enterprise Risk Management Programme (RMP).

Role of the Board and the Board Risk Committee

The Board, through its Board Risk Committee (BRC) is responsible for oversight and governance of the development of the RMP. The role of the BRC is to assist the Board to formulate its risk appetite, and to monitor the effectiveness of the RMP. The BRC has the following specific responsibilities:

- To advise the Board on the formulation of the Board's Risk Appetite Statement at least annually.
- To review reports from management concerning the RMP in the context of the Risk Appetite Statement in order to assure the Board of the programme's effectiveness.
- To review reports from management concerning changes anticipated in the economic, business and regulatory environment (including consideration of emerging trends) and other factors considered relevant to the Risk Appetite Statement, in order to monitor them and advise the Board of any new risks or opportunities that could have a significant financial, regulatory or reputational impact.
- To review reports from management concerning the Bank's internal compliance policies in order to advise the Board of their effectiveness and recommend their approval or variation (or, where the BRC has been delegated authority to itself approve or vary them).
- To review the lending standards developed by the CRO at least annually.

The BRC consists of at least three non-executive directors, of which a majority must be independent. A member of the BRC sits on the Audit Committee. In addition the CRO, Deputy CEO and CFO (or their nominee, subject to the Chair's prior approval) attend the BRC meetings, and the CEO and directors who are not members of the BRC are entitled to attend meetings and to receive copies of the BRC papers. The BRC meets at least bi-monthly and reports directly to the Board.

Audit Committee and Internal Audit

The Banking Group has an internal audit function, the objective of which is to provide independent, objective assurance over the internal control environment. In certain circumstances, Internal audit will provide risk and control advice to Management provided the work does not impede the independence of the Internal Audit function. The function assists the Bank in accomplishing its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Internal audit is allowed full, free and unfettered access to any and all of the organisation's records, personnel and physical properties deemed necessary to accomplish its activities.

A regular cycle of review has been implemented to cover all areas of the business, focused on assessment, management and control of risks. The audit plan takes into account cyclical review of various business units and operational areas, as well as identified areas of higher identified risk. The audit methodology is designed to meet the International Standards for the Professional Practice of Internal Auditing of The Institute of Internal Auditors.

Each audit has specific audit procedures tailored to the area of business that is being reviewed. The audit procedures are updated during each audit to reflect any process changes. Audit work papers are completed to evidence the testing performed in accordance with the audit procedures.

Audit reports are addressed to the manager of the relevant area that is being audited in addition to other relevant stakeholders within the Bank. Management comments are obtained from the process owner(s) and are included in the report.

The internal audit function has a direct reporting line, and accountability to the Audit Committee of the Bank and administratively to the CFO. A schedule of all outstanding internal control issues is maintained and presented to the Audit Committee to assist the Audit Committee to track the resolution of previously identified issues. Any issues raised that are categorised as high risk are specifically reviewed by internal audit during a follow-up review once the issue is considered closed by management. The follow-up review is performed with a view to formally close out the issue.

The Audit Committee focuses on financial reporting and application of accounting policies as part of the internal control and risk assessment framework. The Audit Committee monitors the identification, evaluation and management of all significant risks through the Banking Group. This work is supported by internal audit, which provides an independent assessment of the design, adequacy and effectiveness of internal controls. The Audit Committee receives regular reports from internal audit.

18 Enterprise risk management program (continued)

Audit Committee and Internal Audit (continued)

Charters for both the BRC and the Audit Committee ensure suitable cross representation to allow effective communication pertaining to identified issues with oversight by the Board. The CRO has a direct reporting line to the Chairman of the BRC. The Head of Internal Audit has a direct reporting line to the Chairman of the Audit Committee.

Asset and Liability Committee (ALCO)

The ALCO comprises the CEO (Chair), Deputy CEO, CFO, CRO, Treasurer, Head of Business Advisory and Funding and the Management Reporting Manager. The ALCO has responsibility for overseeing aspects of the Banking Group's financial position risk management. The ALCO usually meet monthly, and provide reports to the BRC. ALCO's specific responsibilities include decision making and oversight of risk matters in relation to:

- Market risk (including non-traded interest rate risk and the investment of capital)
- Liquidity risk (including funding)
- Foreign exchange rate risk
- Balance sheet structure
- Capital management

Executive Risk Committee (ERC)

The ERC comprises the CEO (Chair), Deputy CEO, CFO, CRO, Internal Auditor and Group General Counsel. The ERC has responsibility for overseeing all risk aspects not considered by ALCO, including that the internal control environment is managed so that residual risk is consistent with the Banking Group's risk appetite. The ERC usually meets monthly, and provides its minutes to the BRC. ERC specific responsibilities include decision making and oversight of the following risk categories:

- Operational and compliance risk
- Credit risk
- Strategic risk
- Legal and governance risk

Operational & compliance risk

Operational & compliance risk is the risk arising from day to day operational activities in the execution of the Banking Group's strategy which may result in direct or indirect loss. Operational & compliance risk losses can occur as a result of fraud, human error, missing or inadequately designed processes, failed systems, damage to physical assets, improper behaviour or from external events. The losses range from direct financial losses, to reputational damage, unfavourable media attention, injury to or loss of staff or clients or as a breach of laws or banking regulations. Where appropriate, risks are mitigated by insurance.

To ensure appropriate responsibility is allocated for the management, reporting and escalation of operational & compliance risk, the Banking Group operates a “three lines of defence” model which outlines principles for the roles, responsibilities and accountabilities for operational & compliance risk management:

- The first line of defence is the business line management of the identification, management and mitigation of the risks associated with the products and processes of the business. This accountability includes regular testing and attestation of the adequacy and effectiveness of controls and compliance with the Banking Group’s policies.
- The second line of defence is the Risk & Compliance function, responsible for the design and ownership of the Operational Risk Management Framework. It incorporates key processes including Risk and Control Self-Assessment (RCSA), incident management, independent evaluation of the adequacy and effectiveness of the internal control framework, independent and the attestation process.
- The third line of defence is Internal Audit which is responsible for independently assessing how effectively the Banking Group is managing its risk according to stated risk appetite.

The Banking Group’s exposure to operational & compliance risk is governed by a risk appetite statement approved by the Board and is used to guide management activities by the ERC. This statement sets out the nature of risk which may be taken and aggregate risk limits, and the ERC must monitor adherence to this.

Market risk

Market risk is the possibility of experiencing losses or gains due to factors affecting the overall performance of financial markets in which the Banking Group is exposed. The primary market risk exposures for the Banking Group are Interest Rate risk and Foreign Exchange risk. The risk being that market interest rates or foreign exchange rates will change and adversely impact on the Banking Group’s earnings due to either adverse moves in foreign exchange market rates or in the case of interest rate risks mismatches between repricing dates of interest bearing assets and liabilities and/or differences between customer pricing and wholesale rates. Refer Note 22 - Interest rate risk for further details regarding interest rate risk.

Interest rate risk

Interest rate risk is principally generated through interest rate risk in the bank book. This risk arises from three key sources:

- Mismatches between the repricing dates of interest bearing assets and liabilities;
- Banking products repricing differently to changes in wholesale market rates (basis risk); and
- The investment of capital in interest bearing assets.

18 Enterprise risk management program (continued)

Foreign exchange rate risk

Foreign exchange risk is the risk that the Banking Group's earnings and shareholder equity position are adversely impacted from changes in foreign exchange rates. The Banking Group has exposure to foreign exchange translation risks through its Australian subsidiaries (which have a functional currency of AUD), in the forms of profit translation risk and balance sheet translation risk.

Profit translation risk is the risk that deviations in exchange rates have a significant impact on the reported profit. Balance sheet translation risk is the risk that whilst the foreign currency value of the net investment in a subsidiary may not have changed, when translated back to the New Zealand dollars (NZD), the NZD value has changed materially due to movements in the exchange rates. Foreign exchange revaluation gains and losses are booked to the Foreign Currency Translation Reserve. Foreign exchange rate movements in any given year may have an impact on other comprehensive income. The Banking Group manages this risk by setting and approving the foreign exchange rate for the upcoming financial year and entering into hedging contracts to manage the foreign exchange translation risks.

Counterparty Credit Risk

The Banking Group has on-going credit exposure associated with:

- Cash and cash equivalents
- Holding of investment securities
- Payments owed to the Banking Group from risk management instruments

Counterparty credit risk is managed against limits set in the Market Risk Policy including credit exposure on derivative contracts, bilateral set-off arrangements, cash and cash equivalents and investment securities.

19 Credit risk

Credit risk is the risk that a borrower will default on any type of debt by failing to make payments which it is obligated to make. The risk is primarily that of the lender and includes loss of principal and interest, disruption to cash flows and increased collection costs.

Credit risk is managed to achieve sustainable risk-reward performance whilst maintaining exposures within acceptable risk "appetite" parameters. This is achieved through the combination of governance, policies, systems and controls, underpinned by commercial judgement as described below.

To manage this risk the ERC oversees the formal credit risk management strategy. The ERC reviews the Banking Group's credit risk exposures typically on a monthly basis. The credit risk management strategies aim to ensure that:

- Credit origination meets agreed levels of credit quality at point of approval.
- Sector concentrations are monitored.
- Maximum total exposure to any one debtor is actively managed.
- Changes to credit risk are actively monitored with regular credit reviews.

The BRC also oversees the Banking Group's credit risk exposures to monitor overall risk metrics having regard to risk appetite set by the Board.

The Banking Group has adopted a detailed Credit Risk Framework. The Framework is the overarching Credit Risk document and is supported further by lending standards that provide criteria for finance products within each business sector.

The BRC has authority from the Board for approval of all credit exposures. Lending authority has been provided to the Banking Group's Credit Committees, and to the business units under a detailed Delegated Lending Authority framework. Application of credit discretions in the business operation are monitored through a defined review and hindsight structure as outlined in the Credit Risk Oversight Policy. Delegated Lending Authorities are provided to individual officers with due cognisance of their experience and ability. Larger and higher risk exposures require approval of senior management, the Credit Committees and ultimately through to the BRC.

The Banking Group employs a process of hindsighting loans to ensure that credit policies and the quality of credit processes are maintained.

Reverse mortgage loans and negative equity risk

Reverse mortgage loans are a form of mortgage lending targeted toward the seniors market. These loans differ to conventional mortgages in that they typically are not repaid until the borrower ceases to reside in the property. Further, interest is not required to be paid, it is capitalised with the loan balance and is repayable on termination of the loan. As such, there are no incoming cash flows and therefore no default risk to manage during the term of the loan. Credit risk becomes 'negative equity' risk through the promise by the Banking Group to customers that they can reside in their property for 'as long as they wish' and repayment of their loan is limited to the net sale proceeds of their property.

The Banking Group's exposure to negative equity risk is managed by the Credit Risk Oversight Policy in conjunction with associated lending standards specific for this product. In addition to usual criteria regarding the type, and location, of security property that Heartland will accept for reverse mortgage lending, a key aspect of Heartland's policy is that a borrower's age on origination of the reverse mortgage loan will dictate the loan-to-value ratio of the reserve mortgage on origination. Both New Zealand and Australia reverse mortgage operations are similarly aligned. The policy is managed and reviewed periodically to ensure appropriate consistency across locations.

19 Credit risk (continued)

(a) Maximum exposure to credit risk at the relevant reporting dates

The following table represents the maximum credit risk exposure, without taking account of any collateral held. The exposures set out below are based on net carrying amounts as reported in the Statement of Financial Position.

	Jun 2018 $000	Jun 2017 $000
Cash and cash equivalents	49,588	57,040
Investments	330,852	306,907
Finance receivables	3,984,941	3,545,897
Other financial assets	1,613	101
Total on balance sheet credit exposures	**4,366,994**	**3,909,945**

(b) Concentration of credit risk by geographic region

	Jun 2018 $000	Jun 2017 $000
Auckland	1,073,320	944,446
Wellington	250,782	217,921
Rest of North Island	1,121,983	1,037,873
Canterbury	483,296	485,844
Rest of South Island	595,071	571,251
Australia:		
Queensland	153,955	124,535
New South Wales	331,782	229,715
Victoria	162,214	113,674
Western Australia	35,672	23,602
South Australia	25,356	19,280
Rest of Australia	13,951	10,838
Rest of the world [1]	143,041	152,260
	4,390,423	**3,931,239**
Collective provision	(20,605)	(17,443)
Less acquisition fair value adjustment for present value of future losses	(2,824)	(3,851)
Total on balance sheet credit exposures	**4,366,994**	**3,909,945**

[1] These overseas assets are primarily NZD-denominated investments in AA+ and higher rated securities issued by offshore supranational agencies ("Kauri Bonds").

(c) Concentration of credit risk by industry sector

	Jun 2018 $000	Jun 2017 $000
Agriculture	740,798	757,004
Forestry and Fishing	87,654	79,973
Mining	19,222	19,006
Manufacturing	70,822	76,445
Finance & Insurance	337,241	331,518
Wholesale trade	33,195	38,146
Retail trade	204,869	150,795
Households	2,105,231	1,717,407
Property and Business services	399,973	347,776
Transport and storage	206,592	179,016
Other Services	184,826	234,153
	4,390,423	**3,931,239**
Collective provision	(20,605)	(17,443)
Less acquisition fair value adjustment for present value of future losses	(2,824)	(3,851)
Total on balance sheet credit exposures	**4,366,994**	**3,909,945**

19 Credit risk (continued)

(d) Commitments to extend credit

	Jun 2018 $000	Jun 2017 $000
Undrawn facilities available to customers	180,940	154,848
Conditional commitments to fund at future dates	94,239	119,266

As at 30 June 2018 there are $0.196 million of undrawn lending commitments available to counterparties for whom drawn balances are classified as individually impaired (2017: $0.219 million).

(e) Credit exposures to connected persons

The Banking Group does not have credit exposures to bank or non-back connected persons (2017: nil).

The Banking Group's methodology for calculating credit exposure concentrations is on the basis of actual credit exposures and calculated on a gross basis (net of individual credit impairment allowances and excluding advances of a capital nature) in accordance with the Bank's conditions of registration and the Reserve Bank's Connected Exposures Policy (BS8). Peak end-of-day credit exposures to non-bank connected persons are calculated using the Banking Group's Tier 1 capital at the end of the reporting period.

The rating-contingent limit is 15%, which is the same as the overall rating-contingent sub-limit. There have been no rating-contingent limit changes during the accounting period.

(f) Credit exposure to individual counterparties

The Banking Group measures its concentration of credit risk to individual counterparties at the reporting date based on actual exposures. Peak aggregate end-of-day credit exposure is determined by taking the maximum end-of-day aggregate amount of credit exposure over the period. The exposure is then divided by the Banking Group's Comment Equity Tier 1 Capital (CET1) as at the reporting date.

The exposure information in the table below excludes exposures to connected persons, the central government or central bank of any country with a long term credit rating of A- or A3 or above, or its equivalent and any supernational or quasi-sovereign agency with a long-term credit rating of A- or A3 or above, or its equivalent.

	As at 30 Jun 2018	Peak end-of-day over 6 months to 30 Jun 2018
Exposures to banks		
Total number of exposures to banks that are greater than 10% of CET1 capital	-	1
with a long term credit rating of A- or A3 or above, or its equivalent	-	1
10% to less than 15% of CET1 capital	-	1
with a credit rating of at least BBB- or Baa3, or its equivalent, and at the most BBB+ or Baa1 or its equivalent.	-	-
Exposures to non-banks		
Total number of exposures to non-banks that are greater than 10% of CET1 capital	-	-
with a long term credit rating of A- or A3 or above, or its equivalent	-	-
10% to less than 15% of CET1 capital	-	-
with a credit rating of at least BBB- or Baa3, or its equivalent, and at the most BBB+ or Baa1 or its equivalent.	-	-

20 Asset quality

The disclosures in this note are categorised by the following credit risk concentrations:

Rural	Lending to the farming sector primarily livestock, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers. Includes lending to individuals and small to medium enterprises.
Other Corporate	Business lending other than rural lending.
Residential	Lending secured by a first ranking mortgage over a residential property used primarily for residential purposes either by the mortgagor or a tenant of the mortgagor. This includes reverse mortgages.
All Other	This relates primarily to consumer lending to individuals.

(a) Finance receivables by credit risk concentration

	NOTE	Rural $000	Other Corporate $000	Residential $000	All Other $000	Total $000
Jun 2018						
Neither at least 90 days past due nor impaired		817,894	1,034,519	1,180,623	910,537	3,943,573
At least 90 days past due	20(b)	1,296	5,965	140	21,276	28,677
Individually impaired	20(c)	5,978	35,259	612	3,337	45,186
Fair value adjustment for present value of future losses	11	-	-	(2,824)	-	(2,824)
Provision for impairment	20(e)	(5,549)	(13,968)	(2,114)	(8,040)	(29,671)
Total net finance receivables		**819,619**	**1,061,775**	**1,176,437**	**927,110**	**3,984,941**
Jun 2017						
Neither at least 90 days past due nor impaired[1]		815,904	963,242	999,309	729,445	3,507,900
At least 90 days past due	20(b)	10,517	10,614	787	13,711	35,629
Individually impaired[1]	20(c)	2,361	24,709	2,358	2,656	32,084
Fair value adjustment for present value of future losses	11	-	-	(3,851)	-	(3,851)
Provision for impairment	20(e)	(4,147)	(12,976)	(2,482)	(6,260)	(25,865)
Total net finance receivables		**824,635**	**985,589**	**996,121**	**739,552**	**3,545,897**

[1] A $3.5m reclassification of restructured loans from 'Neither at least 90 days past due nor impaired' to 'Individually impaired' has been made in respect of the year ended 30 June 2017.

(b) Past due but not impaired

	NOTE	Rural $000	Other Corporate $000	Residential $000	All Other $000	Total $000
Jun 2018						
Less than 30 days past due		7,888	11,814	984	29,370	50,056
At least 30 and less than 60 days past due		1,460	3,541	152	12,261	17,414
At least 60 but less than 90 days past due		111	1,798	-	5,752	7,661
At least 90 days past due		1,296	5,965	140	21,276	28,677
Total past due but not impaired		**10,755**	**23,118**	**1,276**	**68,659**	**103,808**
Jun 2017						
Less than 30 days past due		34,287	36,270	2,656	23,796	97,009
At least 30 and less than 60 days past due		13,222	15,655	4,228	9,827	42,932
At least 60 but less than 90 days past due		6,836	5,131	628	4,138	16,733
At least 90 days past due		10,517	10,614	787	13,711	35,629
Total past due but not impaired		**64,862**	**67,670**	**8,299**	**51,472**	**192,303**

20 Asset quality (continued)

(c) Individually impaired assets

	Rural	Other Corporate	Residential	All Other	Total
	$000	$000	$000	$000	$000
Jun 2018					
Opening	2,361	24,709	2,358	2,656	32,084
Additions	11,477	28,309	209	3,312	43,307
Deletions	(6,973)	(14,219)	(1,836)	(2,631)	(25,659)
Write offs	(887)	(3,540)	(119)	-	(4,546)
Closing gross individually impaired assets	**5,978**	**35,259**	**612**	**3,337**	**45,186**
Less: provision for individually impaired assets	1,000	7,672	193	201	9,066
Total net impaired assets	**4,978**	**27,587**	**419**	**3,136**	**36,120**
Jun 2017					
Opening	22,667	11,097	-	-	33,764
Additions	5,657	27,809	2,358	2,656	38,480
Deletions	(25,405)	(12,615)	-	-	(38,020)
Write offs	(558)	(1,582)	-	-	(2,140)
Closing gross individually impaired assets	**2,361**	**24,709**	**2,358**	**2,656**	**32,084**
Less: provision for individually impaired assets	1,005	7,288	129	-	8,422
Total net impaired assets	**1,356**	**17,421**	**2,229**	**2,656**	**23,662**

(d) Credit risk grading

The Banking Group's receivables are monitored either by account behaviour or a regular assessment of their credit risk grade based on an objective review of defined risk characteristics. The portfolio risk is regularly refreshed based on current information.

The Banking Group classifies finance receivables as Behavioural or Judgemental.

The Behavioural portfolio consists of consumer, retail and reverse mortgage, and open for business receivables.

Consumer, open for business and retail loans are risk graded based on arrears status.

Consumer, open for business and retail loans are classified as either not in arrears, active, arrangement, non-performing / repossession or recovery, as described below:

- Active – loans for which the arrears category has reached 5 days overdue.
- Arrangement – overdue accounts for which arrangements have or are in the process of being made for arrears to be repaid.
- Non-performing / Repossession – residential mortgage loans that are greater than 90 days past due / other loans for which security has or is in the process of being repossessed.
- Recovery loans – loans for which security has been sold and shortfalls are being sought from the customer or where other recovery action is being taken.

The Banking Group also lends funds on its reverse mortgage product which is considered behavioural but has no arrears characteristics. These loans are assessed on origination against a pre-determined criteria supported by an actuarial assessment of future losses. The assumptions embedded in that assessment are reviewed annually against actual experience.

The Judgemental portfolio consists mainly of business and rural lending. Judgemental loans relate to loans where an on-going and detailed working relationship with the customer has been developed.

Judgemental loans are individually risk graded based on loan status, financial information, security and debt servicing ability. Exposures in the Judgemental portfolio are credit risk graded by an internal risk grading mechanism.

In the Judgemental portfolio, grade 1 is the strongest risk grade and grade 9 represents the weakest risk grade where a loss is probable. Grade 10 reflects loss accounts written off.

20 Asset quality (continued)

(d) Credit risk grading (continued)

	Rural	Other Corporate	Residential	All Other	Total
	$000	$000	$000	$000	$000
Jun 2018					
Judgemental portfolio					
Grade 1 - Very Strong	29	-	-	-	29
Grade 2 - Strong	1,868	7,534	770	-	10,172
Grade 3 - Sound	21,562	46,715	3,206	964	72,447
Grade 4 - Adequate	105,828	230,651	11,243	4,546	352,268
Grade 5 - Acceptable	464,055	206,840	15,096	1,183	687,174
Grade 6 - Monitor	114,838	28,787	575	1,506	145,706
Grade 7 - Substandard	11,384	11,574	-	-	22,958
Grade 8 - Doubtful	3,802	20,118	-	-	23,920
Grade 9 - At risk of loss	422	5,955	10	128	6,515
Total Judgemental portfolio	**723,788**	**558,174**	**30,900**	**8,327**	**1,321,189**
Behavioural portfolio					
Not in arrears	95,162	483,439	1,148,771	831,946	2,559,318
Active	4,463	18,881	878	45,753	69,975
Arrangement	298	4,603	633	41,194	46,728
Non-performing / Repossession	370	1,250	-	4,050	5,670
Recovery	87	1,724	-	3,679	5,490
Total Behavioural portfolio	**100,380**	**509,897**	**1,150,282**	**926,622**	**2,687,181**
Provision for collectively impaired assets	(4,549)	(6,296)	(1,921)	(7,839)	(20,605)
Fair value adjustment for present value of future losses	-	-	(2,824)	-	(2,824)
Total finance receivables	**819,619**	**1,061,775**	**1,176,437**	**927,110**	**3,984,941**
Jun 2017					
Judgemental portfolio					
Grade 1 - Very Strong	715	-	-	-	715
Grade 2 - Strong	2,871	22,720	968	-	26,559
Grade 3 - Sound	20,533	54,178	5,022	-	79,733
Grade 4 - Adequate	86,832	191,076	15,542	624	294,074
Grade 5 - Acceptable	466,989	231,065	28,799	1,683	728,536
Grade 6 - Monitor	129,717	35,171	1,267	-	166,155
Grade 7 - Substandard	13,871	13,798	-	-	27,669
Grade 8 - Doubtful	1,071	13,895	1,783	-	16,749
Grade 9 - At risk of loss	11	2,545	-	-	2,556
Total Judgemental portfolio	**722,610**	**564,448**	**53,381**	**2,307**	**1,342,746**
Behavioural portfolio					
Not in arrears	100,552	407,291	948,475	683,017	2,139,335
Active	3,766	15,645	362	36,848	56,621
Arrangement	647	2,288	107	15,590	18,632
Non-performing / Repossession	154	836	-	3,966	4,956
Recovery	48	769	-	4,084	4,901
Total Behavioural portfolio	**105,167**	**426,829**	**948,944**	**743,505**	**2,224,445**
Provision for collectively impaired assets	(3,142)	(5,688)	(2,353)	(6,260)	(17,443)
Fair value adjustment for present value of future losses	-	-	(3,851)	-	(3,851)
Total finance receivables	**824,635**	**985,589**	**996,121**	**739,552**	**3,545,897**

20 Asset quality (continued)

(e) Provision for impairment

Credit impairment provisions are made where events have occurred leading to an expectation of reduced future cash flows from certain receivables. These provisions are made in some cases against an individual loan and in other cases on a collective basis.

Bad debts provided for are written off against individual or collective provisions. Amounts required to bring the provisions to their assessed levels are recognised in profit or loss. Any future recoveries of amounts provided for are recognised in profit or loss.

Collective provisioning

The term collectively impaired asset refers to an asset where an event has occurred of which past history indicates that there is an increased possibility that the Banking Group will not collect all of its principal and interest as it falls due. No losses have yet been identified on these individual loans within the collectively impaired asset grouping, and history would indicate that only a small portion of these loans will eventually not be recovered. The Banking Group provides fully for its expected losses on collectively impaired assets.

Collective provisions are assessed with reference to risk profile groupings and historical loss data. Other judgemental factors including economic and credit cycle considerations are also taken into account in determining appropriate loss propensities to be applied. The future credit quality of these portfolios is subject to uncertainties that could cause actual credit losses to differ materially from reported loan impairment provisions. These uncertainties include the wider economic environment, interest rates and their effect on customer spending, unemployment levels, payment behaviour and bankruptcy rates.

No provisions are applied to loans that are newly written and loans that remain within their contractual terms, except where the Banking Group becomes aware of an event that might alter its view of the risk of a particular deal or group of deals.

Adequacy of the collective provision levels for each risk grouping is measured against historical loss experience at least annually. Adequacy of individual provisions is assessed in respect of each loan on a material development or at least quarterly.

Individual provisioning

Specific impairment provisions are made where events have occurred leading to an expectation of reduced future cash flows from certain receivables. For individually significant loans for which the assessed risk grade is considered a “potential loss”, an individual assessment is made of an appropriate provision for credit impairment.

Credit impairments are recognised as the difference between the carrying value of the loan and the discounted value of management’s best estimate of future cash repayments and proceeds from any security held (discounted at the loan’s original effective interest rate). All relevant considerations that have a bearing on the expected future cash flows are taken into account, including the business prospects for the customer, the likely realisable value of collateral, the Banking Group’s position relative to other claimants, the reliability of customer information and the likely cost and duration of the work-out process. Subjective judgements are made in this process. Furthermore, judgement can change with time as new information becomes available or as work-out strategies evolve, resulting in revisions to the impairment provision as individual decisions are taken. Changes in judgement could have a material impact on the financial statements.

For the Behavioural portfolio, excluding reverse mortgage loans, arrears drive provision outcomes. Each arrears classification carries a provision for potential loss based on historical experience for that classification in the same portfolio.

20 Asset quality (continued)

(e) Provision for impairment (continued)

	Rural $000	Other Corporate $000	Residential $000	All Other $000	Total $000
Jun 2018					
Provision for individually impaired assets					
Opening provision for individually impaired assets	1,005	7,288	129	-	8,422
Impairment loss for the year					
- charge for the year	882	3,924	183	201	5,190
- recoveries	-	-	-	-	-
- write offs	(887)	(3,540)	(119)	-	(4,546)
Closing provision for individually impaired assets	**1,000**	**7,672**	**193**	**201**	**9,066**
Provision for collectively impaired assets					
Opening provision for collectively impaired assets	3,142	5,688	2,353	6,260	17,443
Impairment loss for the year					
- charge / (credit) for the year	1,628	3,226	(490)	12,513	16,877
- effect of changes in foreign exchange rates	-	-	76	-	76
- recoveries	2	200	-	931	1,133
- write offs	(223)	(2,818)	(18)	(11,865)	(14,924)
Closing provision for collectively impaired assets	**4,549**	**6,296**	**1,921**	**7,839**	**20,605**
Total provision for impairment	**5,549**	**13,968**	**2,114**	**8,040**	**29,671**
Jun 2017					
Provision for individually impaired assets					
Opening provision for individually impaired assets	869	4,033	-	-	4,902
Impairment loss for the year					
- charge for the year	694	3,682	129	-	4,505
- recoveries	-	1,155	-	-	1,155
- write offs	(558)	(1,582)	-	-	(2,140)
Closing provision for individually impaired assets	**1,005**	**7,288**	**129**	**-**	**8,422**
Provision for collectively impaired assets					
Opening provision for collectively impaired assets	3,595	6,032	3,046	3,586	16,259
Impairment loss for the year					
- charge / (credit) for the year	(48)	1,474	(619)	9,703	10,510
- recoveries	23	119	-	63	205
- write offs	(428)	(1,937)	(74)	(7,092)	(9,531)
Closing provision for collectively impaired assets	**3,142**	**5,688**	**2,353**	**6,260**	**17,443**
Total provision for impairment	**4,147**	**12,976**	**2,482**	**6,260**	**25,865**

(f) Other assets under administration

Other assets under administration are any loans, not being individually impaired or 90 days or more past due, where the customer is in any form of voluntary or involuntary administration, including receivership, liquidation, bankruptcy or statutory management. As at 30 June 2018, the Banking Group had assets under administration of $1,188,000 (2017: $1,203,000).

21 Liquidity risk

Liquidity risk is the risk that the Banking Group is unable to meet its payment obligations as they fall due. The timing mismatch of cash flows and the related liquidity risk is inherent in all Banking operations and is closely monitored by the Banking Group.

Management of liquidity risk is designed to ensure that the Banking Group has the ability to generate or obtain sufficient cash in a timely manner and at a reasonable price to meet its financial commitments on a daily basis.

The Banking Group's exposure to liquidity risk is governed by a policy approved by the Board and managed by the ALCO. This policy sets out the nature of risk which may be taken and aggregate risk limits, and the ALCO must conform to this. The objective of the ALCO is to derive the most appropriate strategy for the Banking Group in terms of the mix of assets and liabilities given its expectations of future cash flows, liquidity constraints and capital adequacy. The Banking Group employs asset and liability cash flow modelling to determine appropriate liquidity and funding strategies.

The Banking Group holds the following financial assets for the purpose of managing liquidity risk:

	Jun 2018 $000	Jun 2017 $000
Cash and cash equivalents	49,588	57,040
Investments	330,852	306,907
Undrawn committed bank facilities	52,500	85,000
Total liquidity	**432,940**	**448,947**

Contractual liquidity profile of financial assets and liabilities

The following tables present the Banking Group's financial assets and liabilities by relevant maturity groupings based upon contractual maturity date. The amounts disclosed in the tables represent undiscounted future principal and interest cash flows. As a result, the amounts in the tables below may differ to the amounts reported on the balance sheet.

The contractual cash flows presented below may differ significantly from actual cash flows. This occurs as a result of future actions by the Banking Group and its counterparties, such as early repayments or refinancing of term loans and borrowings. Deposits and other public borrowings include customer savings deposits and transactional accounts, which are at call. History demonstrates that such accounts provide a stable source of long term funding for the Banking Group.

The Banking Group does not manage its liquidity risk on a contractual liquidity basis.

	On Demand $000	0-6 Months $000	6-12 Months $000	1-2 Years $000	2-5 Years $000	5+ Years $000	Total $000
Jun 2018							
Financial assets							
Cash and cash equivalents	49,588	-	-	-	-	-	49,588
Investments	-	53,474	85,376	134,654	71,592	9,694	354,790
Finance receivables	-	532,992	363,067	1,162,174	1,353,343	5,031,437	8,443,013
Finance receivables - securitised	-	21,189	21,189	42,378	3,531	-	88,287
Derivative financial assets	-	-	-	-	-	-	-
Other financial assets	-	1,613	-	-	-	-	1,613
Total financial assets	**49,588**	**609,268**	**469,632**	**1,339,206**	**1,428,466**	**5,041,131**	**8,937,291**
Financial liabilities							
Borrowings	924,072	1,273,453	572,731	786,835	251,694	-	3,808,786
Borrowings - securitised	-	47,614	-	-	-	-	47,614
Derivative financial liabilities	-	1,639	-	-	-	-	1,639
Other financial liabilities	-	22,610	-	-	-	-	22,610
Total financial liabilities	**924,072**	**1,345,316**	**572,731**	**786,835**	**251,694**	**-**	**3,880,649**
Net financial (liabilities) / assets	**(874,484)**	**(736,048)**	**(103,099)**	**552,371**	**1,176,772**	**5,041,131**	**5,056,643**
Undrawn facilities available to customers	180,940	-	-	-	-	-	180,940
Undrawn committed bank facilities	52,500	-	-	-	-	-	52,500

21 Liquidity risk (continued)

Contractual liquidity profile of financial assets and liabilities (continued)

	On Demand $000	0-6 Months $000	6-12 Months $000	1-2 Years $000	2-5 Years $000	5+ Years $000	Total $000
Jun 2017							
Financial assets							
Cash and cash equivalents	57,040	-	-	-	-	-	57,040
Investments	-	45,849	21,418	112,861	137,419	11,791	329,338
Finance receivables	-	511,529	446,008	748,085	1,275,773	4,285,026	7,266,421
Finance receivables - securitised	-	60,792	54,489	85,155	95,528	-	295,964
Derivative financial assets	-	-	-	-	-	-	-
Other financial assets	-	101	-	-	-	-	101
Total financial assets	**57,040**	**618,271**	**521,915**	**946,101**	**1,508,720**	**4,296,817**	**7,948,864**
Financial liabilities							
Borrowings	836,829	1,163,751	513,671	114,221	729,587	-	3,358,059
Borrowings - securitised	-	2,727	215,474	-	-	-	218,201
Derivative financial liabilities	-	3,349	-	-	-	-	3,349
Other financial liabilities	-	22,130	-	-	-	-	22,130
Total financial liabilities	**836,829**	**1,191,957**	**729,145**	**114,221**	**729,587**	**-**	**3,601,739**
Net financial (liabilities) / assets	**(779,789)**	**(573,686)**	**(207,230)**	**831,880**	**779,133**	**4,296,817**	**4,347,125**
Undrawn facilities available to customers	120,948	-	-	-	-	-	120,948
Undrawn committed bank facilities	85,000	-	-	-	-	-	85,000

Undrawn committed bank facilities of $52.5 million (2017: $85.0 million) were available to be drawn down on demand. To the extent drawn, $52.5 million is contractually repayable in 1 months' time upon facility expiry.

22 Interest rate risk

The Banking Group's market risk is derived primarily of exposure to interest rate risk, predominantly from raising funds through the retail and wholesale deposit market, the debt capital markets and committed and uncommitted bank funding, securitisation of receivables, and offering loan finance products to the commercial and consumer market in New Zealand and Australia.

Interest rate risk is the risk that the value of assets or liabilities will change because of changes in interest rates or that market interest rates may change and thus alter the margin between interest-earning assets and interest-bearing liabilities. Interest rate risk for the Banking Group refers to the risk of loss due to holding assets and liabilities that may mature or re-price in different periods.

The Banking Group’s exposure to market risk is governed by a policy approved by the Board and managed by the ALCO. This policy sets out the nature of risk which may be taken and aggregate risk limits, and the ALCO must conform to this. The objective of the ALCO is to derive the most appropriate strategy for the Banking Group in terms of the mix of assets and liabilities given its expectations of the future and the potential consequences of interest rate movements, liquidity constraints and capital adequacy.

To manage this market risk, the Banking Group measures sensitivity to interest rate changes by frequently testing its position against various interest rate change scenarios to assess potential risk exposure. The Banking Group also manages interest rate risk by:

- Monitoring maturity profiles and seeking to match the re-pricing of assets and liabilities (physical hedging);
- Monitoring interest rates daily and regularly (at least monthly) reviewing interest rate exposure; and
- Entering into forward rate agreements and interest rate swaps and options to hedge against movements in interest rates.

22 Interest rate risk (continued)

Contractual repricing analysis

The interest rate risk profile of financial assets and liabilities that follows has been prepared on the basis of maturity or next repricing date, whichever is earlier.

	0-3 Months $000	3-6 Months $000	6-12 Months $000	1-2 Years $000	2+ Years $000	Non-interest bearing $000	Total $000
Jun 2018							
Financial assets							
Cash and cash equivalents	49,580	-	-	-	-	8	49,588
Investments	44,483	22,935	82,149	111,355	69,930	9,694	340,546
Finance receivables	2,673,338	153,230	264,313	395,785	413,627	4,359	3,904,652
Finance receivables - securitised	14,659	12,671	20,534	23,015	9,410	-	80,289
Other financial assets	-	-	-	-	-	1,613	1,613
Total financial assets	**2,782,060**	**188,836**	**366,996**	**530,155**	**492,967**	**15,674**	**4,376,688**
Financial liabilities							
Borrowings	2,352,604	485,825	543,746	150,230	207,596	8,553	3,748,554
Borrowings - securitised	47,504	-	-	-	-	-	47,504
Other financial liabilities	1,639	-	-	-	-	22,610	24,249
Total financial liabilities	**2,401,747**	**485,825**	**543,746**	**150,230**	**207,596**	**31,163**	**3,820,307**
Effect of derivatives held for risk management	361,760	(44,735)	(75,365)	(242,090)	430	-	-
Net financial assets / (liabilities)	**742,073**	**(341,724)**	**(252,115)**	**137,835**	**285,801**	**(15,489)**	**556,381**
Jun 2017							
Financial assets							
Cash and cash equivalents	57,020	-	-	-	-	20	57,040
Investments	55,929	7,886	9,937	112,747	120,408	11,791	318,698
Finance receivables	2,376,633	138,837	208,917	313,010	281,413	113	3,318,923
Finance receivables - securitised	56,584	27,195	45,529	46,485	51,181	-	226,974
Other financial assets	-	-	-	-	-	101	101
Total financial assets	**2,546,166**	**173,918**	**264,383**	**472,242**	**453,002**	**12,025**	**3,921,736**
Financial liabilities							
Borrowings	1,981,205	576,129	491,038	111,863	47,736	7,405	3,215,376
Borrowings - securitised	214,365	-	-	-	-	-	214,365
Other financial liabilities	3,349	-	-	-	-	22,130	25,479
Total financial liabilities	**2,198,919**	**576,129**	**491,038**	**111,863**	**47,736**	**29,535**	**3,455,220**
Effect of derivatives held for risk management	423,403	(44,010)	(85,588)	(166,735)	(127,070)	-	-
Net financial assets / (liabilities)	**770,650**	**(446,221)**	**(312,243)**	**193,644**	**278,196**	**(17,510)**	**466,516**

The tables above illustrate the periods in which the cash flows from interest rate swaps are expected to occur and affect profit or loss.

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Banking Group's financial assets and liabilities to various standard and non standard interest rate scenarios. Standard scenarios which are considered on a monthly basis include a 100 basis point parallel fall or rise in the yield curve. There is no material impact on profit or loss in terms of a fair value change from movements in market interest rates. Furthermore there is no material cash flow impact on the Statement of Cash Flows from a 100 basis point change in interest rates.

23 Concentrations of funding

(a) Regulatory liquidity ratios

The table below shows the arithmetic 3-month average of the respective daily ratio values in accordance with RBNZ's Liquidity Policy (BS13/BS13A) ("BS13") and the Bank's Conditions of Registration relating to liquidity-risk management.

The one-week mismatch ratio is a measure of the Banking Group's one-week mismatch amount over its total funding, where the one-week mismatch amount represents the Banking Group's portfolio of primary liquid assets plus expected cash inflows minus expected cash outflows during a one-week period of stress. The Bank is required to maintain this ratio at not less than the minimum level of zero percent on a daily basis. The one-week mismatch ratio = 100 x (one-week mismatch dollar amount / total funding).

The one-month mismatch ratio is a measure of the Banking Group's one-month mismatch amount over its total funding, where the one-month mismatch amount represents the Banking Group's portfolio of primary and secondary liquid assets plus expected cash inflows minus expected cash outflows during a one-month period of stress. The Bank is required to maintain this ratio at not less than the minimum level of zero percent on a daily basis. The one-month mismatch ratio = 100 x (one-month mismatch dollar amount / total funding).

The one-year core funding ratio measures the extent to which loans and advances are funded by the funding that is considered stable. The one-year core funding ratio = 100 x (one-year core funding dollar amount / BS13 total loans and advances) and must currently remain at not less than 75% on a daily basis.

	3 months ended 30 Jun 2018	3 months ended 31 Mar 2018
One-week mismatch ratio	5.17%	5.03%
One-month mismatch ratio	4.34%	5.09%
Core funding ratio	94.81%	94.77%

(b) Concentration of funding by industry

	Jun 2018 $000	Jun 2017 $000
Agriculture	69,245	46,058
Forestry and Fishing	23,403	16,073
Mining	38	250
Manufacturing	10,691	7,829
Finance & Insurance	979,871	998,035
Wholesale Trade	9,967	9,808
Retail Trade	14,102	16,899
Households	2,260,330	2,137,159
Property and Business Services	110,385	94,262
Transport and Storage	4,853	7,556
Other	139,148	74,632
	3,622,033	3,408,561
Subordinated notes	22,172	21,180
Unsubordinated notes	151,853	-
Total borrowings	**3,796,058**	**3,429,741**

(c) Concentration of funding by geographical area

	Jun 2018 $000	Jun 2017 $000
Auckland	969,518	993,573
Wellington	270,096	203,652
Rest of North Island	686,208	550,787
Canterbury	885,005	843,919
Rest of South Island	245,830	224,155
Overseas [1]	739,401	613,655
Total borrowings	**3,796,058**	**3,429,741**

[1] Included in Overseas is the CBA bank funding totalling $615 million (2017: $462 million), refer to Note 13 - Borrowings for more information.

Other Disclosures

24 Significant subsidiaries

Significant subsidiaries	Country of incorporation and place of business	Nature of business	Proportion of ownership interest and voting power held Jun 2018	Jun 2017
VPS Properties Limited	New Zealand	Investment property holding company	100%	100%
Heartland Australia Group Pty Limited	Australia	Financial services	100%	100%
Australian Seniors Finance Pty Limited	Australia	Management services	100%	100%
MARAC Insurance Limited	New Zealand	Insurance services	100%	100%

25 Structured entities

A structured entity is one which has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity. Structured entities are created to accomplish a narrow and well-defined objective such as the securitisation or holding of particular assets, or the execution of a specific borrowing or lending transaction. Structured entities are consolidated where the substance of the relationship is that the Banking Group controls the structured entity.

(a) Heartland Cash and Term PIE Fund (Heartland PIE Fund)

The Banking Group controls the operations of Heartland PIE Fund which is a portfolio investment entity that invests in the Bank's deposits. Investments of Heartland PIE Fund are represented as follows:

	Jun 2018 $000	Jun 2017 $000
Deposits	115,095	93,998

(b) Heartland ABCP Trust 1 (ABCP Trust)

The Banking Group has securitised a pool of receivables comprising commercial and motor vehicle loans to ABCP Trust.

The Banking Group continues to recognise the securitised assets and associated borrowings in the Statement of Financial Position through the holding of subordinated debt of the ABCP Trust and the receipt of deferred purchase consideration from that trust. Whilst the Bank has those interests in the ABCP Trust, the loans sold to the Trust are set aside for the benefit of investors in the ABCP Trust and Bank depositors have no recourse to these assets. The ABCP Trust's material assets and liabilities are represented as follows:

	NOTE	Jun 2018 $000	Jun 2017 $000
Cash and cash equivalents - securitised		3,625	9,272
Finance receivables - securitised	11	80,289	226,974
Borrowings - securitised	13	(47,504)	(214,365)
Derivative financial liabilities - securitised		(496)	(1,042)

(c) Seniors Warehouse Trust (SW Trust) and ASF Settlement Trust (ASF Trust)

SW Trust and ASF Trust form part of ASF's reverse mortgage business and were both set up by ASF, as asset holding entities. The Trustee for both Trusts is ASF Custodians Pty Limited and the Trust Manager is ASF. The reverse mortgage loans held by the Trusts are set aside for the benefit of the funder and bank depositors have no recourse to these assets. The balances of SW Trust and ASF Trust are represented as follows:

	Jun 2018 $000	Jun 2017 $000
Cash and cash equivalents	12,207	5,781
Finance receivables - Reverse mortgage loans	676,837	517,488
Borrowings - CBA	(614,510)	(462,298)
Derivative financial liabilities	-	(547)

26 Staff share ownership arrangements

The Banking Group operates a number of share-based compensation plans that are equity settled. The fair value determined at the grant date is expensed on a straight line basis over the vesting period, based on the Banking Group's estimate of equity instruments that will eventually vest, with a corresponding increase in equity. At the end of each reporting period, the Banking Group revises its estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the employee benefits reserve.

(a) Share-based compensation plan details

Heartland LTI Net Share Settled Plan (LTI Plan)

The LTI Plan was allotted under three tranches (referred to as the 2013, 2014 and 2015 tranches). Under the LTI Plan participants were granted an option to acquire shares in the Bank. The number of shares granted upon exercise of the options is based on the difference between the market price of the shares on the exercise date and the reference price.

The options are subject to the participants' continued employment with the Banking Group for the service period of 3 years which begins on 1 July 2014 for the 2015 plan. Participants in the 2015 tranche will be able to exercise their options between September 2017 and 1 July 2019.

2015 Special Grant (LTI SG)

Participants of the LTI SG were able to exercise options in the period beginning on the date the market price of Heartland shares was equal to $1.50 and ending on 1 July 2017. Market price was calculated based on the VWAP of a Heartland share for the 10 business days immediately before (but excluding) the exercise date for those options. The options were subject to the participants' continued employment with the banking group for the service period of 3 years which began on 1 July 2014. Following exercise a lock up period until 1 July 2020 applies during which participants are restricted from disposing of shares.

The reference price was the amount by which the market price of Heartland shares, at the time of exercise, exceeded $1.00 (based on a volume weighted average price of Heartland shares for the prior 20 business days), plus the aggregate amount of cash dividends (cents per Heartland share) paid by the Bank in the period from 1 April 2015 until and including the date the options were exercised. However, for the purpose of calculating the settlement amount, the market price of Heartland shares was capped at $1.50 and any increase above this amount was disregarded.

26 Staff share ownership arrangements (continued)

Senior Executive Scheme (SES)

The SES was established in June 2016 as a replacement of the LTI Plan and LTI SG for certain affected participants only (Senior Executives). Under the SES, Senior Executives forfeited their options under the 2014 and 2015 tranches of the LTI Plan and the LTI SG and purchased Heartland shares with proceeds from a settlement amount paid to them by the Bank. The shares are unable to be sold or otherwise disposed of by the Senior Executive until 30 June 2019. Until then, if the Senior Executive ceases their employment with the Bank, the Bank has a call option requiring the Senior Executive to give the shares back to the Bank for no consideration.

The SES has been treated as a modification of the Senior Executive entitlements under the 2014 and 2015 tranches of the LTI Plan and the LTI SG. The incremental fair value granted is $0.49 million based on the value of shares acquired under the SES less the fair value of the benefits forfeited under the 2014 and 2015 tranches of the LTI Plan and the LTI SG.

Heartland Performance Rights Plan (PR Plan)

The PR Plan was established to enhance the alignment of participants' interests with those of the bank's shareholders. Under the PR Plan participants are issued performance rights which will entitle them to receive shares in the bank.

PR Plan 2016 Tranche (PR plan 2016)

The number of performance rights offered is determined by the participant's LTI value over the volume weighted average of the sales prices (VWAP) of the bank's ordinary shares on the NZX Main Board for the 10 business days immediately before (and including) the issue date. The issue date is 31 August 2016. Performance rights do not entitle participants to dividends or voting rights.

The performance rights are issued subject to the participants' continued employment with the banking group until the measurement date and the bank achieving its Total Shareholder Return (TSR) target. The measurement date is defined as 10 business days following the date on which the bank announces its full year results for the financial year ended 2019. The TSR target has been set at an annual rate of 11%, compounding and is determined primarily by share price movements and cash dividends. Performance rights will vest on the measurement date where these criteria have been met.

PR Plan 2017 Tranche (PR plan 2017)

The number of performance rights offered is determined by the participant’s LTI value over the volume weighted average of the sales prices (VWAP) of the bank’s ordinary shares on the NZX Main Board for the 20 business days immediately before (and excluding) the issue date. The issue date is 12 September 2017. Performance rights do not entitle participants to dividends or voting rights.

The performance rights are issued subject to the participants’ continued employment with the banking group until the measurement date and the bank achieving its share price and/or market capitalisation targets. The targets are dynamic and may be adjusted by the Board from time to time in order to account for unanticipated capital changes during the performance period. The measurement date is 10 business days following the date on which the bank announces its full year results for the financial year ended 2021.

Performance rights will vest on the measurement date to the extent these criteria have been met, but subject to caps and also to retesting on a later measurement date if the criteria are not met on the initial measurement date.

	PR Plan Number of rights	SES Number of shares	LTI SG Number of options	LTI Plan Number of options
1 July 2017	**888,300**	**1,858,676**	**-**	**7,492,753**
Granted [1]	2,291,998	-	-	-
Exercised [2]	-	-	-	(7,300,488)
Forfeited	-	-	-	(192,265)
30 June 2018	**3,180,298**	**1,858,676**	**-**	**-**
1 July 2016	**-**	**1,858,676**	**1,302,101**	**17,455,079**
Granted	888,300	-	-	-
Exercised [2]	-	-	(1,302,101)	(9,912,296)
Forfeited	-	-	-	(50,030)
30 June 2017	**888,300**	**1,858,676**	**-**	**7,492,753**

1 The fair value of performance rights granted during the period is $1.06 million (PR plan 2017: $1.04m, PR plan 2016: $0.02m). This fair value was derived using the Monte Carlo model. The key inputs used in the model are:
- Volatility 18.1% - 21.3% (calculated based on the historical movement in Heartland's shares)
- Risk free rate 2.59% p.a.
- Initial measurement date 10 September 2021
- VWAP on Issue Date $1.877
- Share price at valuation date $1.86

2 Weighted average share price on exercise was $1.83 (2017: $1.54).

26 Staff share ownership arrangements (continued)

(b) Effect of share-based payment transactions

	Jun 2018 $000	Jun 2017 $000
Award of shares	-	86
SES	328	328
LTI SG	-	99
LTI Plan	(34)	415
PR Plan	372	125
Total expense recognised	**666**	**1,053**

As at 30 June 2018, $1.02 million of share scheme awards remain unvested and not expensed (30 June 2017: $0.98 million). This expense will be recognised over the vesting period of the awards.

(c) Number of rights outstanding at 30 June 2018

	Rights Outstanding 000	Remaining life years
PR Plan - 2016	928	1
PR Plan - 2017	2,252	4
Total	**3,180**	

27 Capital adequacy

The Banking Group is subject to regulation by the RBNZ. The RBNZ has set minimum regulatory capital requirements for Banks that are consistent with the internationally agreed framework developed by the Basel Committee on Banking Supervision. The resulting Basel II and III requirements define what is acceptable as capital and provide for methods of measuring the risks incurred by the Banking Group.

The Banking Group's Conditions of Registration prescribes minimum capital adequacy ratios calculated in accordance with the Capital Adequacy Framework (Standardised Approach) BS2A.

The Banking Group has adopted the Basel II standardised approach per RBNZ BS2A to calculate its regulatory requirements. Basel II is made up of the following three Pillars:

- Pillar 1 sets out the minimum capital requirements for credit, market and operational and compliance risks.
- Pillar 2 is designed to ensure that Banks have adequate capital to support all risks (not just those set out under Pillar 1 above) and is enforced through the requirement for supervisory review.
- Pillar 3 outlines the requirements for adequate and transparent disclosure.

Basel III was developed in order to strengthen the regulation, supervision and risk management of the Banking sector. The measures aim to improve the Banking sector's ability to absorb shocks arising from financial and economic stress; improve risk management and governance; and strengthen Banks' transparency and disclosures. The requirements that impact capital are as follows:

- The level of capital required to be held by Banks increased through the introduction of new minimum capital requirements for Common Equity Tier 1 (CET1) capital, Additional Tier 1 (AT1) capital and Total capital as a percentage of risk-weighted-assets (RWA's).
- A capital conservation buffer held over and above the minimum capital ratio requirements used to absorb losses during periods of financial and economic stress.
- A counter-cyclical capital buffer be held and to be used at the RBNZ's discretion, to assist in attaining the macro-prudential goal of protecting the Banking sector from periods of extraordinary excess aggregate credit growth.
- Strengthen the calculation of RWAs, particularly in respect of counterparty credit risk.

The Basel III requirements have not effected the Banking Group's minimum capital requirements as the Banking Group's Conditions of Registration prescribe minimum capital requirements higher than the Basel III requirements.

The capital adequacy tables set out on the following pages summarise the composition of regulatory capital and the capital adequacy ratios for the Banking Group as at 30 June 2018.

Internal Capital Adequacy Assessment Process (ICAAP)

The Banking Group has an ICAAP which complies with the requirements set out in the "Guidelines on a Bank's Internal Capital Adequacy Assessment Process (ICAAP)" BS12 and is in accordance with its Conditions of Registration.

27 Capital adequacy (continued)

Internal Capital Adequacy Assessment Process (ICAAP)

The Board has overall responsibility for ensuring the Banking Group has adequate capital in relation to its risk profile and establishes minimum internal capital levels and limits above the regulatory minimum. The Banking Group has established a Capital Management Policy (CMP) to determine minimum capital levels for Tier 1 and Total capital under Basel III and in accordance with its Conditions of Registration. The documented process ensures that the Banking Group has sufficient available capital to meet minimum capital requirements, even in stressed events. It describes the risk profile of the Banking Group and the risk appetite and tolerances under which it operates, and assesses the level of capital held against the material risks of the Banking Group (both Pillar 1 and Pillar 2).

The ICAAP identifies the capital required to be held against other material risks, being strategic / business risk, reputational risk, regulatory risk and additional credit risk. See Note 27(l) for further details.

Compliance with minimum capital levels is monitored by the Asset and Liability Committee and reported to the Board monthly. The ICAAP and CMP is reviewed annually by the Board.

(a) Capital

	Jun 2018 $000
Tier 1 Capital	
CET1 capital	
Paid-up ordinary shares issued by the Banking Group plus related share premium	542,315
Retained earnings (net of appropriations)	117,260
Accumulated other comprehensive income and other disclosed reserves	4,585
Less foreign currency translation reserve	(1,260)
Less deductions from CET1 capital	
Intangible assets	(74,401)
Deferred tax assets	(5,319)
Hedging reserve	1,080
Excess of loan value over the security value on reverse residential mortgage loans	(165)
Defined benefit superannuation fund assets	(813)
Total CET1 capital	**583,282**
Additional Tier 1 Capital	
Nil	-
Total Tier 1 Capital	**583,282**
Tier 2 Capital	
Subordinated Bonds	486
Subordinated Notes	15,745
Foreign currency translation reserve	1,260
Total Tier 2 Capital	**17,491**
Total Capital	**600,773**

(b) Capital structure

The following details summarise each instrument included within Total Capital. None of these instruments are subject to phase-out from eligibility as capital under the RBNZ's Basel III transitional arrangements.

Ordinary shares

In accordance with BS2A, ordinary share capital is classified as CET1 capital. The ordinary shares have no par value. Each ordinary share of the Bank carries the right to vote on a poll at meetings of shareholders, the right to an equal share in dividends authorised by the Board and the right to an equal share in the distribution of the surplus assets of the Bank in the event of liquidation.

Retained earnings

Retained earnings is the accumulated profit or loss that has been retained in the Banking Group. Retained earnings is classified as CET1 capital.

27 Capital adequacy (continued)

Reserves classified as CET1 capital

Treasury shares reserve	The treasury shares reserve comprises shares in Heartland Bank Limited held by the Bank.
Employee benefits reserve	The employee benefits reserve comprises employee share options which have been recognised as an expense but not yet been exercised and converted into ordinary shares. These are scheduled to vest on 30 June 2019 and 30 June 2021 depending on the employee share option plan the options relate to.
Available for sale reserve	The available-for-sale reserve comprises the changes in the fair value of available-for-sale securities, net of tax. These changes are recognised in profit or loss as other income when the asset is either derecognised or impaired.
Defined benefit reserve	The defined benefit plan reserve represents the excess of the fair value of the assets of the defined benefit superannuation plan over the net present value of the defined benefit obligations.
Hedging reserve	The hedging reserve comprises the fair value gains and losses associated with the effective portion of designated cash flow hedging instruments.

Foreign currency translation reserve

The foreign currency translation reserve represents the differences in translation which arise when converting the financial statements of the Australian controlled entities from their functional currency into the presentational currency. It constitutes Tier 2 capital of the Banking Group.

Subordinated Bonds and Notes

The Bank's 2018 Subordinated Bonds (the Subordinated Bonds) constitute Tier 2 Capital of the Banking Group. The Subordinated Bonds had an issue period from 12 July 2013 to 15 December 2013 and have a maturity date of 15 December 2018. The Subordinated Bonds pay quarterly interest in arrears at a rate of 6.5% per annum, provided the Bank will be solvent immediately after the payment is made. The Bank may elect to repay the Subordinated Bonds prior to 15 December 2018 if a regulatory event or tax event occurs and provided it will be solvent immediately after the repayment and the Reserve Bank has consented to the repayment. The Subordinated Bonds are subordinated to all other general liabilities of the Banking Group and are denominated in New Zealand dollars.

The Bank's 2027 Subordinated Unsecured Convertible Notes (the Subordinated Notes) constitute Tier 2 Capital of the Banking Group. The Subordinated Notes had an issue date of 7 April 2017 and have a maturity date of 7 April 2027. The Subordinated Notes pay quarterly interest in arrears at a rate of BBSW+4.15% per annum, provided the Bank will be solvent immediately after the payment is made. The Bank may elect to repay some or all of the Subordinated Notes on the First Optional Redemption Date (7 April 2022) or on any scheduled Interest Payment Date thereafter, as well as if a regulatory event or tax event occurs. Early repayment may only be made provided the Bank will be solvent immediately after the repayment and the Reserve Bank has consented to the repayment. The Subordinated Notes are subordinated to all other general liabilities of the Banking Group and are denominated in Australian dollars.

If the Reserve Bank or a Statutory Manager requires the Bank to convert all or part of the Subordinated Bonds, or to convert or write off (if conversion is not able to be effected) all or part of the Subordinated Notes, the Subordinated Bonds or Subordinated Notes will be converted or written off (as applicable) and could in each case be reduced to zero to comply with the Reserve Bank's loss absorbency requirements. The Bank has not had any defaults of principal, interest or other breaches with respect to the Subordinated Bonds or Subordinated Notes.

27 Capital adequacy (continued)

(c) Credit risk

(i) On balance sheet exposures

	Total exposure after credit risk mitigation	Average risk weighting	Risk weighted exposure	Minimum Pillar 1 capital requirement
	$000	%	$000	$000
Jun 2018				
Cash and gold bullion	8	0%	-	-
Multilateral development banks	73,323	0%	-	-
Multilateral development banks	61,813	20%	12,363	989
Public sector entities	38,313	20%	7,663	613
Public sector entities	6,998	50%	3,499	280
Banks	123,815	20%	24,763	1,981
Banks	3,897	50%	1,949	156
Banks	28,827	100%	28,827	2,306
Corporates	1,531	20%	306	24
Corporates	17,929	50%	8,965	717
Corporates	23,986	100%	23,986	1,919
Welcome Home Loans - loan to value ratio (LVR) ≤ 90%[1]	3,585	35%	1,255	100
Welcome Home Loans - LVR > 90% and ≤ 100% [1]	200	50%	100	8
Reverse Residential mortgages ≤ 60% LVR	1,099,876	50%	549,938	43,995
Reverse Residential mortgages >60 and ≤ 80% LVR	27,075	80%	21,660	1,733
Reverse Residential mortgages > 80% LVR	3,004	100%	3,004	240
Past due residential mortgages	150	100%	150	12
Other past due assets - provision ≥ 20%	13,906	100%	13,906	1,112
Other past due assets - provision < 20%	58,461	150%	87,692	7,015
Non property investment mortgage loan < 80% LVR	21,690	35%	7,592	607
Non property investment mortgage loan > 80 and ≤ 90% LVR	3,249	50%	1,625	130
Non property investment mortgage loan > 90 and ≤ 100% LVR	455	75%	341	27
Non property investment mortgage loan > 100% LVR	1,812	100%	1,812	145
Property Investment Mortgage Loan ≤ 80% LVR	12,700	40%	5,080	406
Property Investment Mortgage Loan > 100% LVR	2,641	100%	2,641	211
All other equity holdings	9,694	400%	38,776	3,102
Other assets	2,776,290	100%	2,776,290	222,103
Not risk weighted assets	80,698	0%	-	-
Total on balance sheet exposures	**4,495,926**		**3,624,183**	**289,931**

(ii) Off balance sheet exposures

	Total exposure	Average credit conversion factor	Credit equivalent amount	Average risk weight	Risk weighted exposure	Minimum Pillar 1 capital requirement [1]
	$000	$000	$000	%	$000	$000
Jun 2018						
Direct credit substitute	4,537	100%	4,537	100%	4,537	363
Performance-related contingency	2,310	50%	1,155	100%	1,155	92
Other commitments where original maturity is more than one year	211,863	50%	105,932	100%	105,932	8,475
Other commitments where original maturity is more than one year	50,291	50%	25,146	50%	12,573	1,006
Other commitments where original maturity is less than or equal to one year	13,025	20%	2,605	100%	2,605	208
Market related contracts [2]						
Interest rate contracts	353,875	0.0%	-	20%	-	-
Interest rate contracts	411,620	0.5%	2,058	20%	412	33
Total off balance sheet exposures	**1,047,521**		**141,433**		**127,214**	**10,177**

1 The LVR classification above is calculated in line with the Bank's Pillar 1 Capital requirement which includes capital relief for Welcome Home loans that are guaranteed by the Crown.

2 The credit equivalent amount for market related contracts was calculated using the current exposure method.

27 Capital adequacy (continued)

(d) Additional mortgage information - LVR range

	On balance sheet exposures	Off balance sheet exposures[1]	Total exposures
	$000	$000	$000
Jun 2018			
Does not exceed 80%	1,163,372	15,684	1,179,056
Exceeds 80% and not 90%	7,807	-	7,807
Exceeds 90%	5,258	-	5,258
Total exposures	**1,176,437**	**15,684**	**1,192,121**

[1] Off balance sheet exposures means unutilised limits.

At 30 June 2018 $0.2 million relating to Welcome Home loans, whose credit risk is mitigated by the Crown is included in "Exceeds 90% residential mortgages". Other loans in the exceeds 90% LVR range are primarily business and rural lending where residential mortgage security is only a part of the total security. For capital adequacy calculations only the value of first mortgages over residential property is included in the LVR calculation, in accordance with BS2A. All new residential mortgage loans are in respect of non property investments lending and have a loan-to-valuation ratio of less than or equal to 80%.

(e) Reconciliation of mortgage related amounts

	Note	Jun 2018 $000
Loans and advances - loans with residential mortgages	20(a)	1,176,437
On balance sheet residential mortgage exposures subject to the standardised approach		**1,176,437**
Off balance sheet mortgage exposures subject to the standardised approach	27(d)	15,684
Total residential exposures subject to the standardised approach		**1,192,121**

(f) Credit risk mitigation

As at 30 June 2018 the Banking Group had $3.79 million of Welcome Home Loans, whose credit risk was mitigated by the Crown. Other than this the Banking Group does not have any exposures covered by eligible collateral, guarantees and credit derivatives.

(g) Operational Risk

	Implied risk weighted exposure	Aggregate capital charge
	$000	$000
Operational risk	225,066	18,005

Operational risk is calculated based on the previous 12 quarters of the Banking Group.

(h) Market risk

Market risk is the risk that market interest rate risks or foreign exchange rates will change and impact on the Banking Group's earnings due to either mismatches between repricing dates of interest bearing assets and liabilities and/or differences between customer pricing and wholesale rates.

		Implied risk weighted exposure	Aggregate capital charge
		$000	$000
Market risk end-of-period capital charge	Interest rate risk only	152,026	12,162
Market risk peak end-of-day capital charge	Interest rate risk only	156,380	12,510
Market risk end-of-period capital charge	Foreign currency risk only	124,966	9,997
Market risk peak end-of-day capital charge	Foreign currency risk only	124,966	9,997

Peak end-of-day aggregate capital charge at the end of the period is derived by following the risk methodology for measuring capital requirements within Part 10 of the Standardised Approach. Peak end-of-day aggregate capital charge is derived by determining the maximum end of month capital charge over the reporting period. Based on the portfolio of the Banking Group's risk exposures, it is considered by management that the difference between end of month aggregate capital charge and end-of-day aggregate capital charge is insignificant.

27 Capital adequacy (continued)

(i) Total capital requirements

	Total exposure after credit risk mitigation	Risk weighted exposure or implied risk weighted exposure	Total capital requirement
	$000	$000	$000
Total credit risk and equity			
On balance sheet	4,495,926	3,624,183	289,931
Off balance sheet	1,047,521	127,214	10,177
Operational risk	n/a	225,066	18,005
Market risk	n/a	276,992	22,159
Total	**n/a**	**4,253,455**	**340,272**

(j) Capital ratios

	Jun 2018	Jun 2017
	%	%
Capital ratios compared to minimum ratio requirements		
Common Equity Tier 1 Capital expressed as a percentage of total risk weighted exposures	13.71%	13.15%
Minimum Common Equity Tier 1 Capital as per Conditions of Registration	4.50%	4.50%
Tier 1 Capital expressed as a percentage of total risk weighted exposures	13.71%	13.15%
Minimum Tier 1 Capital as per Conditions of Registration	6.00%	6.00%
Total Capital expressed as a percentage of total risk weighted exposures	14.12%	13.56%
Minimum Total Capital as per Conditions of Registration	8.00%	8.00%
Buffer ratio		
Buffer ratio	6.12%	5.56%
Buffer ratio requirement	2.50%	2.50%

(k) Solo capital adequacy

	Jun 2018	Jun 2017
	%	%
Common Equity Tier 1 Capital expressed as a percentage of total risk weighted exposures	15.35%	14.55%
Tier 1 Capital expressed as a percentage of total risk weighted exposures	15.35%	14.55%
Total Capital expressed as a percentage of total risk weighted exposures	15.80%	15.03%

For the purposes of calculating capital adequacy on a solo basis, subsidiaries which are both wholly owned and wholly funded by the Bank are to be consolidated with the Bank. Therefore, capital adequacy on a solo basis is calculated based on the Bank and its subsidiaries excluding ABCP Trust, SW Trust and ASF Trust.

(l) Capital for other material risks

In addition to the material risks included in the calculation of the capital ratios, the Banking Group has identified other material risks to be included in the capital allocation (being strategic/business risk, reputational risk, regulatory and additional credit risk). As at 30 June 2018, the Banking Group has made an internal capital allocation of $48.2 million to cover these risks (2017: $104.89 million).

28 Insurance business, securitisation, funds management, other fiduciary activities

Insurance business

The Banking Group conducts insurance business through its subsidiary MARAC Insurance Limited (MIL).

The Banking Group's aggregate amount of insurance business comprises the total consolidated assets of MIL of $13.2 million, which is 0.29% of the total consolidated assets of the Banking Group.

The Banking Group's objective is to minimise the insurance risk to within acceptable levels through policies and procedures implemented by management. Should adverse conditions arise, these policies and procedures are expected to mitigate the impact of the conditions on the Banking Group.

Marketing and distribution of insurance products

The Banking Group markets and distributes term life insurance and general insurance covering risks such as redundancy, bankruptcy or suspension of employment. The insurance products are either underwritten by MIL, a subsidiary of the Banking Group, or sold by MIL on behalf of other parties who underwrite those products themselves. There have been no material changes in the Banking Group's marketing and distribution of insurance products since the reporting date of the previous disclosure statement.

Securitisation

As at 30 June 2018, the Banking Group had securitised assets amounting to $80 million (2017: $227 million). These assets have been sold to ABCP Trust (a special purpose vehicle investing in motor vehicle, truck and trailer and commercial loans originated by the Banking Group and funded through the issuance of commercial paper and also through liquidity facilities). Note 25 - Structured entities provides further information on the securitised assets.

The Bank received fees for various services provided to the securitisation vehicles on an arm's length basis, including servicing fees. These fees were recognised as earned. All securitisation vehicles form part of the Banking Group.

There have been no material changes to the Banking Group's involvement in the securitisation activities.

Funds management and other fiduciary activities

The Banking Group, through Heartland PIE Fund Limited, controls, manages and administers the Heartland Cash and Term PIE Fund and its products (Heartland Call PIE and Heartland Term Deposit PIE). Note 25 - Structured entities has further details. The Heartland Cash and Term PIE Fund deals with the Bank in the normal course of business, in the Bank's capacity as Registrar of the Fund and also invests in the Bank's deposits. The Banking Group is considered to control the Heartland Cash and Term PIE Fund, and as such the Heartland Cash and Term PIE Fund is consolidated within the financial statements of the Banking Group.

Heartland NZ Trustee Limited (HNZT), a subsidiary of the Bank, acts as manager for a superannuation scheme. The assets and liabilities of this scheme are not included in the financial statements of the Banking Group as the Banking Group does not control the scheme. The Bank provides services to HNZT and its fees for performance of those services are included in other income.

Risk management

The Banking Group has in place policies and procedures to ensure that the fiduciary activities identified above are conducted in an appropriate manner. It is considered that these policies and procedures will ensure that any difficulties arising from these activities will not impact adversely on the Banking Group. The policies and procedures include comprehensive and prominent disclosure of information regarding products, and formal and regular review of operations and policies by management and internal and external auditors. Further information on the Banking Group's risk management policies and practices is included in Note 18 - Enterprise risk management program.

Provision of financial services and asset purchases

Over the accounting period, financial services provided by the Banking Group to entities which were involved in the activities above (including trust, custodial, funds management and other fiduciary activities) were provided on arm's length terms and conditions and at fair value.

Any assets purchased from such entities have been purchased on arm's length terms and conditions and at fair value.

28 Insurance business, securitisation, funds management, other fiduciary activities (continued)

Peak aggregate funding to entities

The Banking Group did not provide any funding to entities conducting funds management and other fiduciary activities, or insurance product or marketing and distribution activities described in this note, during the year (2017: nil).

The Bank provided funding to ABCP Trust, which is a member of the Banking Group involved in securitisation activities. This funding is provided to facilitate the purchase of asset backed securities from the Banking Group in order to support the securitisation facility.

	Total Trusts	
	Jun 2018	Jun 2017
Peak end-of-day aggregate amount of funding provided ($000s)	90,439	86,110
Peak end-of-day aggregate amount of funding provided as a percentage of the Banking Group's Tier 1 Capital as at the end of the year	15.5%	17.5%

	Seniors Warehouse Trust		ASF Settlement Trust		ABCP Trust	
	Jun 2018	Jun 2017	Jun 2018	Jun 2017	Jun 2018	Jun 2017
Peak end-of-day aggregate amount of funding provided ($000s)	51,875	51,979	4,077	3,980	38,219	32,621
Peak end-of-day aggregate amount of funding provided as a percentage of the total assets of the individual entity as at the end of the year	7.6%	10.1%	71.8%	68.6%	45.6%	13.8%

For this purpose, peak ratio information was derived by determining the maximum end-of-day aggregate amount of funding and then dividing that amount by the amount of the entity's assets or the Banking Group's Tier 1 Capital (as the case required) as at the end of the year.

29 Contingent liabilities and commitments

Contingent liabilities are possible obligations, whose existence will be confirmed only by uncertain future events, or present obligations where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised, but are disclosed, unless they are remote. Where some loss is probable, provisions have been made.

Contingent liabilities and credit related commitments arising in respect of the Banking Group's operations were:

	Jun 2018	Jun 2017
	$000	$000
Letters of credit, guarantee commitments and performance bonds	6,847	10,903
Total contingent liabilities	**6,847**	**10,903**
Undrawn facilities available to customers	180,940	154,848
Conditional commitments to fund at future dates	94,239	119,266
Total commitments	**275,179**	**274,114**

30 Events after the reporting date

On 1 August 2018, Heartland Bank announced its intention to conduct a corporate restructure and seek a Foreign Exempt Listing on the Australian Securities Exchange (ASX) (see Group Restructure on page 10). As the proposed restructure is subject to shareholder approval, and has not been authorised, it has not been reflected in the financial statements as at 30 June 2018.

There have been no other material events after the reporting date that would affect the interpretation of the financial statements or the performance of the Banking Group.

HISTORICAL SUMMARY OF FINANCIAL STATEMENTS

Statements of Comprehensive Income

For the year ended	Audited 30 Jun 18 $000	Audited 30 Jun 17 $000	Audited 30 Jun 16 $000	Audited 30 Jun 15 $000	Audited 30 Jun 14 $000
Interest income	309,284	278,279	265,475	260,468	210,297
Interest expense	125,483	115,169	118,815	126,041	101,221
Net interest income	**183,801**	**163,110**	**146,660**	**134,427**	**109,076**
Other net income	12,993	8,142	10,901	10,280	13,079
Total operating income before other gains	**196,794**	**171,252**	**157,561**	**144,707**	**122,155**
Employee benefits	46,460	41,547	39,799	40,401	35,765
Other operating expenses	33,973	30,137	30,073	28,002	28,974
Profit before impairment and tax	**116,361**	**99,568**	**87,689**	**76,304**	**57,416**
Impaired asset expense	22,067	15,015	13,501	12,105	5,895
Decrease in fair value of investment properties	-	-	-	-	1,203
Net profit before tax	**94,294**	**84,553**	**74,188**	**64,199**	**50,318**
Share of joint arrangement profit	-	-	-	137	486
Profit before income tax	**94,294**	**84,553**	**74,188**	**64,336**	**50,804**
Income tax expense / (benefit)	26,781	23,745	20,024	16,173	14,765
Net profit after tax attributable to owners of the entity	**67,513**	**60,808**	**54,164**	**48,163**	**36,039**
Other comprehensive income for the year net of tax					
Items that are or may be reclassified subsequently to profit or loss:					
Effective portion of changes in fair value of cash flow hedges, net of tax	72	1,108	(708)	(2,709)	1,111
Net change in available-for-sale reserve, net of tax	981	(353)	(208)	898	(12)
Movement in foreign currency translation reserve, net of income tax	2,315	761	(4,047)	2,136	95
Items that will not be reclassified to profit or loss:					
Net change in defined benefit reserve, net of income tax	340	(84)	(93)	50	3
Total comprehensive income for the year, net of tax	**71,221**	**62,240**	**49,108**	**48,538**	**37,236**
Dividends paid to equity holders	47,895	41,977	37,690	30,188	19,930

Statements of Financial Position

As at	Audited 30 Jun 18 $000	Audited 30 Jun 17 $000	Audited 30 Jun 16 $000	Audited 30 Jun 15 $000	Audited 30 Jun 14 $000
Total assets	4,495,926	4,034,671	3,547,181	3,359,259	3,016,888
Individually impaired assets	45,186	32,084	33,764	25,622	27,617
Total liabilities	3,831,766	3,465,076	3,048,840	2,879,134	2,564,266
Total equity	664,160	569,595	498,341	480,125	452,622

Historical financial information has been taken from the audited financial statements of the Banking Group.

Independent auditor's report

To the shareholders of Heartland Bank Limited

Report on the financial statements

Opinion

In our opinion, the accompanying financial statements (excluding supplementary information relating to capital adequacy and regulatory liquidity requirements) of Heartland Bank Limited (the "Bank") and its subsidiaries (the "Banking Group") on pages 11 to 54:

i. give a true and fair view of the Banking Group's financial position as at 30 June 2018 and its financial performance and cash flows for the year ended on that date; and

ii. comply with New Zealand Generally Accepted Accounting Practice, which in this instance means New Zealand Equivalents to International Financial Reporting Standards ("NZ IFRS") and International Financial Reporting Standards.

In our opinion, the supplementary information (excluding supplementary information relating to capital adequacy and regulatory liquidity requirements) that is required to be disclosed in accordance with schedules 4, 7, 13, 14, 15 and 17 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order"):

i. has been prepared, in all material respects, in accordance with the guidelines issued pursuant to section 78(3) of the Reserve Bank of New Zealand Act 1989 and any conditions of registration;

ii. is in accordance with the books and records of the Bank and Banking Group in all material respects; and

iii. fairly states the matters to which it relates in accordance with those schedules.

We have audited the accompanying financial statements and supplementary information (excluding supplementary information relating to capital adequacy and regulatory liquidity requirements) which comprise:

- the statement of financial position as at 30 June 2018;
- the statements of comprehensive income, changes in equity and cash flows for the year then ended;
- notes, including a summary of significant accounting policies and other explanatory information; and
- the information that is required to be disclosed in accordance with schedules 4, 7, 13, 14, 15 and 17 of the Order.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) ("ISAs (NZ)"). We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Bank and Banking Group in accordance with Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the "IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our responsibilities under ISAs (NZ) are further described in the 'Auditor's responsibilities for the audit of the financial statements (excluding supplementary information relating to capital adequacy and regulatory liquidity requirements)' section of our report.

Our firm has also provided other services to the Bank and Banking Group in relation to the review of the Bank's half-year disclosure statement, regulatory assurance services, agreed upon procedures engagements, supervisor reporting, health and safety advisory services, and tax, regulatory and accounting advisory services. Subject to certain restrictions, partners and employees of our firm may also deal with the Bank and Banking Group on normal terms within the ordinary course of trading activities of the business of the Bank and Banking Group. These matters have not impaired our independence as auditor of the Bank and Banking Group. The firm has no other relationship with, or interest in, the Banking Group.

Materiality

The scope of our audit was influenced by our application of materiality. Materiality helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole. The materiality for the financial statements as a whole was set at $4,665,000 determined with reference to a benchmark of the Banking Group's profit before tax. We chose the benchmark because, in our view, it is the key measure of the Banking Group's performance.

We agreed with the Audit Committee that we would report misstatements identified during our audit, to them, above $230,000 as well as misstatements below that amount that in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements in the current period. We summarise below those matters and our key audit procedures to address those matters, and our findings, in order that the shareholders may better understand the process by which we arrived at our audit opinion. Our procedures were undertaken in the context of and solely for the purpose of our statutory audit opinion on the financial statements as a whole and we do not express discrete opinions on separate elements of the financial statements.

The key audit matter	How the matter was addressed in our audit and our findings

Provision for impairment of finance receivables

Refer to notes 11 and 20 to the financial statements.

The provision for impairment of finance receivables is a key audit matter owing to the financial significance of finance receivables, the high degree of complexity and judgement applied by management in determining the provision. There is a high level of subjectivity involved in estimating the provision for impairment.

The provision for impairment of finance receivables comprises a provision for both individually and collectively impaired assets.

The provision for individually impaired assets is based on the application of management judgement, with the assessment of expected future cash flows being inherently uncertain and judgemental. The provision for individually impaired assets for 'rural' and other 'corporate' loans is of particular audit focus, owing to its financial significance and inherent uncertainties of expected future cash flows, which may include estimated timing and proceeds from the future sale of assets securing the debt, in addition to repayments from borrowers.

The provision for collectively impaired assets is determined based on the Bank's classification of lending. Finance receivables are classified as either 'judgemental' or 'behavioural':

- judgemental loans are individually risk graded based on an internal model, incorporating loan status, financial information, security and debt servicing ability; and
- behavioural loans consist of 'consumer', 'retail' and 'home equity release' receivables. Behavioural loans are classified based on their arrears status.

Based on the assigned risk grading or arrears status, an estimate of the likelihood of default and the potential loss given default will be applied to determine the collective provision based on historical loss data.

Additionally management apply judgement in the determination of provision overlays where historic losses are not considered to be an accurate reflection on future market conditions.

The level of judgement involved in determining the provision for collectively impaired assets requires us to challenge the appropriateness of management's assumptions.

Our audit procedures, amongst others, included:

- Testing key controls over arrears calculations, customer loan ratings, annual loan reviews, credit risk reviews and model validations.
- Evaluating credit assessments for a sample of 'rural' and other 'corporate' loans that are either individually above $10 million or on management's credit watchlist. This included inspection of the latest correspondence with the borrower, assessment of the provision estimates prepared by credit risk officers, and consideration of the resolution strategy; including challenging assumptions based on our experience and industry knowledge, and assessing collateral values by comparing them to valuations performed by independent valuers.
- Assessing individually significant loans in arrears not specifically provided for, to determine whether they were being appropriately monitored and incorporated into the provision for collectively impaired assets.
- Testing key inputs used in the collective provision calculation for significant portfolios. This included the loan rating for judgemental loans and arrears profile for behavioural loans including comparison to historic losses.
- Benchmarking collective provision rates against the historic losses incurred by the Banking Group, and comparator analysis against other relevant banks and finance companies.
- Assessing management's judgement in the application of overlays by applying sensitivities to assumptions underlying the overlays, and evaluating current economic and climatic conditions linked to the overlays, including actuarial inputs, not captured in the Bank's models.

The estimates and assumptions used to determine the provision for impairment of finance receivables are reasonable, with no evidence of management bias or influence identified from our procedures.

We did not identify any material issues or exceptions from our procedures.

The key audit matter	How the matter was addressed in our audit and our findings
Operation of IT systems and controls	
The Banking Group is heavily dependent on complex IT systems for the processing and recording of significant volumes of transactions and other core banking activity. For significant financial statement balances, such as finance receivables and deposits, our audit involves an assessment of the design of the Banking Group's internal control environment relevant to the preparation of these financial statements. There are some areas of the audit where we seek to test and place reliance on IT systems, automated controls and reporting. The effective operation of these controls is dependent upon the Banking Group's general IT control environment, which incorporates controls relevant to IT system changes and development, IT operations, developer and user access controls.	Our audit procedures, amongst others, included: • Gaining an understanding of business processes, key controls, and IT systems relevant to significant financial statement balances, including technology services are provided by a third party. • Assessing the design and operating effectiveness of IT control environment, including core banking IT systems, key automated controls and reporting. • Evaluating general IT controls relevant to IT system changes and development, IT operations, developer and user access controls. In performing our work, we identified design and operating effectiveness control observations that impacted the level of reliance we could place on IT systems, automated controls and reports. In response, we performed additional compensating control tests and substantive audit procedures: • We carried out substantive testing on IT systems and controls to assess: (i) the accuracy of automated controls and IT system calculated transactions and balances, such as interest income and expense; (ii) the reliability of automated reporting, such as IT system generated arrears reporting; (iii) the operation of technology dependent manual controls. • We performed additional control testing on compensating controls, including management and governance review controls. • We completed further substantive audit procedures over significant financial statement balances, where required to support our audit. We did not identify any material issues or exceptions from those additional procedures.

Other information

The directors, on behalf of the Banking Group, are responsible for the other information included in the Bank's disclosure statement, annual review report and market announcements. Other information comprises the information required to be included in the disclosure statement in accordance with schedule 2 of the Order, financial commentary and other information including in the annual review report, and market announcements. Our opinion on the financial statements does not cover any other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the financial statements our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have received the Bank's disclosure statement, annual review report and market announcements and have nothing to report in this regard.

Report on other legal and regulatory requirements

In accordance with the requirements of clauses 2(1)(d) and 2(1)(e) of Schedule 1 of the Order, we report that:

- we have obtained all the information and explanations we have required; and
- in our opinion, proper accounting records have been kept by the Banking Group, as far as appears from our examination of those records.

Responsibilities of directors for the financial statements and supplementary information (excluding supplementary information relating to capital adequacy and regulatory liquidity requirements)

The directors, on behalf of the Banking Group, are responsible for:

- the preparation and fair presentation of the financial statements in accordance with clause 24 of the Order, NZ IFRS and International Financial Reporting Standards;
- the preparation and fair presentation of supplementary information (excluding the supplementary information relating to capital adequacy and regulatory liquidity requirements), in accordance with schedules 2, 4, 7, 13, 14, 15 and 17 of the Order;
- implementing necessary internal control to enable the preparation of financial statements that are fairly presented and free from material misstatement, whether due to fraud or error; and
- assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements and supplementary information (excluding supplementary information relating to capital adequacy and regulatory liquidity requirements)

Our objective is:

- to obtain reasonable assurance about whether the disclosure statement, including the financial statements prepared in accordance with clause 24 of the Order, and supplementary information (excluding the supplementary information relating to capital adequacy and regulatory liquidity requirements), in accordance with schedules 4, 7, 13, 14, 15 and 17 of the Order as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an independent auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (NZ) will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial statements.

A further description of our responsibilities for the audit of these financial statements is located at the External Reporting Board (the "XRB") website at:

http://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1/

This description forms part of our independent auditor's report.

Report on the supplementary information relating to capital adequacy and regulatory liquidity requirements

Review conclusion

Based on our review, nothing has come to our attention that causes us to believe that the supplementary information relating to capital adequacy and regulatory liquidity requirements, disclosed in notes 23(a) and 27 to the financial statements, is not, in all material respects, disclosed in accordance with schedule 9 of the Order.

We have reviewed the supplementary information relating to capital adequacy and regulatory liquidity requirements, as disclosed in notes 23(a) and 27 to the financial statements for the year ended 30 June 2018. The supplementary information relating to capital adequacy and regulatory liquidity requirements comprises the information that is required to be disclosed in accordance with schedule 9 of the Order.

Basis for conclusion on the supplementary information relating to capital adequacy and regulatory liquidity requirements

A review of the supplementary information relating to capital adequacy and regulatory liquidity requirements, in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity* ("NZ SRE 2410") is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. Our responsibilities under that standard are further described in the 'Auditor's responsibilities for the review of the supplementary information relating to capital adequacy and regulatory liquidity requirements' section of our report.

As the auditor of the Bank, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

Responsibilities of directors for the supplementary information relating to capital adequacy and regulatory liquidity requirements

The directors are responsible for the preparation of supplementary information relating to capital adequacy and regulatory liquidity requirements that is required to be disclosed under schedule 9 of the Order and described in notes 23(a) and 27 to the financial statements.

Auditor's responsibilities for the review of the supplementary information relating to capital adequacy and regulatory liquidity requirements

Our responsibility is to express a conclusion on the supplementary information relating to capital adequacy and regulatory liquidity requirements based on our review. We conducted our review in accordance with NZ SRE 2410. As the auditor of the Bank, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements, and plan and perform the review to obtain limited assurance about whether the supplementary information relating to capital adequacy and regulatory liquidity requirements is, in all material respects, disclosed in accordance with schedule 9 of the Order.

A review of the supplementary information relating to capital adequacy and regulatory liquidity requirements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with ISAs (NZ). Accordingly we do not express an audit opinion on the supplementary information relating to capital adequacy and regulatory liquidity requirements disclosures.

Use of this independent auditor’s report

This independent auditor’s report is made solely to the shareholders as a body. Our work has been undertaken so that we might state to the shareholders those matters we are required to state to them in the independent auditor’s report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the shareholders as a body for our work, this independent auditor’s report, or any of the opinions or conclusions we have formed.

The engagement partner on the audit resulting in this independent auditor’s report is **Jamie Munro**.

For and on behalf of

KPMG

15 August 2018
KPMG
Auckland