

Disclosure Statement

For the year ended 30 June 2022



HEARTLAND
BANK

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General Information

This Disclosure Statement has been issued by Heartland Bank Limited (**HBL** or the **Bank**) and its subsidiaries (the **Banking Group**) for the year ended 30 June 2022 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 2022 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 Banking Group consists of the Bank and all of its subsidiaries.

The Bank's address for service is Level 3, 35 Teed Street, Newmarket, Auckland 1023.

The address for service of the ultimate parent, Heartland Group Holdings Limited (**HGH**), is Level 3, 35 Teed Street, Newmarket, Auckland 1023.

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
Heartland Group Holdings Limited	100%

Heartland Group Holdings Limited have the ability to appoint 100% of Directors, subject to Reserve Bank of New Zealand (**RBNZ**) restrictions and RBNZ Director approval.

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.

Guarantee Arrangements

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

Auditor

KPMG
KPMG Centre
18 Viaduct Harbour Avenue
Auckland 1010

Directors

All Directors of the Bank reside in New Zealand. Communications to the Directors can be sent to Heartland Bank Limited, Level 3, 35 Teed Street, Newmarket, Auckland 1023.

There have been no changes in the composition of the Board of Directors of the Bank for the year ended 30 June 2022.

The Directors of the Bank and their details at the time this Disclosure Statement was signed were:

Chairman – Board of Directors

Name: Bruce Robertson Irvine

Qualifications: BCom, LLB, FCA, CFInstD

Type of Director: Independent Non-Executive Director

Occupation: Company Director

External Directorships:

Air Rarotonga Limited, Amaia Day Spa (Tonga) Limited, Amaia Luxury Spa Limited, Amyes Road Limited (in liquidation), B R Irvine Limited, Blackbyre Horticulture Limited, Bowdens Mart Limited, MG Sustainable Operations Limited, Chambers @151 Limited, Clipper Investments (2002) Limited, Cockerill and Campbell (2007) Limited, Embassy Hotels Limited, GZ Capital Limited, GZ NZ Limited, GZ RES Limited, Hansons Lane International Holdings Limited, Hawling Holdings Limited, House of Travel ESP Trustee Limited, House of Travel Holdings Limited, J.S. Ewers Limited, Kaipaki Holdings Limited, Kaipaki Properties Limited, Lake Angelus Holdings Limited, Lamanna Bananas (NZ) Limited, Lamanna Premier Group Pty Limited, Lamanna Limited, Market Fresh Wholesale Limited, Market Gardeners Limited, MG Group Holdings Limited, MG Marketing Limited, MG New Zealand Limited, Monarch Hotels Limited, Noblesse Oblige Limited, Paradise Islands Limited, Phimai Holdings Limited, Quitachi Limited, Scenic Hotels (Karapiro) Limited, Scenic Hotels (Hamilton) Limited, Scenic Circle Convention Services Limited, Scenic Hotel (Haast) Limited, Scenic Circle (Napier) Limited, Scenic Hotel Group Limited, Scenic Hotels (Ashburton) Limited, Scenic Hotels (International) Limited, Scenic Circle MLC Café & Bar Limited, Skope Industries Limited, Southland Produce Markets Limited, Stark Holdings (NZ) Limited, Wavell Resources Limited, Scenic Circle (Rotorua) Limited, Scenic Circle (Queenstown) Limited, Scenic Hotels Limited, Abalon Investments Limited, Airedale Developments (Auckland) Limited, Scenic Hotels (Tonga) Limited, Waiho Investments Limited, Scenic Circle Hotels Management Services Limited, Scenic Circle Punakaiki Rocks Hotel Limited, Scenic Hotel Collection New Zealand Limited, Scenic Hotels (Auckland) Limited, Scenic Hotels (Niue) Limited, Scenic Hotels (Kaikoura) Limited, Heartland Hotels Limited, Scenic (Franz Josef) Limited, Scenic Circle (Airedale) Limited, Scenic Circle (Bay Of Islands) Limited, Platinum Hotels Limited, Scenic Aviation Limited, Scenic Circle (Bay Of Plenty) Limited, Scenic Circle (Blenheim) Limited, Karma Finance Limited, Scenic Circle Hotels (Dunedin) Limited, Refined Hotels Limited, Scenic Hospitality Services Limited, Scenic Circle Glacier Country Hotel Limited, Scenic Circle (North Island) Limited, Scenic Hotels Technology Limited, Scenic Circle (Rotorua Lakes) Limited, Ezibed (2022) Limited, Mainstay International Hotels (NZ)(2022) Limited, Golden Chain (NZ) Limited, Mainstay International Hotels (2022) Limited, Mitchell Corp New Zealand (2022) Limited, Te Kaikoura Investments Limited, MLC Scenic Limited, Wagstaff Holdings Limited, Heartland PIE Fund Limited.

Name: Jeffrey Kenneth Greenslade

Qualifications: LLB

Type of Director: Non-Independent Non-Executive Director

Occupation: Chief Executive Officer of Heartland Group Holdings

External Directorships:

Heartland Australia Group Pty Limited, Heartland Australia Holdings Pty Limited, Australian Seniors Finance Pty Limited, ASF Custodians Pty Limited, Heartland Group Holdings Limited, Henley Family Investments Limited, StockCo Holdings 2 Pty Limited, StockCo Australia Management Pty Limited.

Name: Edward John Harvey

Qualifications: BCom, CA, CFInstD

Type of Director: Independent Non-Executive Director

Occupation: Company Director

External Directorships:

KMD Brands Limited, Napier Port Holdings Limited, Pomare Investments Limited, Port of Napier Limited.

Name: Geoffrey Thomas Ricketts CNZM

Qualifications: LLB (Hons), LLD

Type of Director: Non-Independent Non-Executive Director

Occupation: Company Director

External Directorships:

Heartland Group Holdings Limited, Janmac Capital Limited, Maisemore Enterprises Limited, MCF2 Message4U Limited, MCF 10 Limited, MCF2 (Fund 1) Limited, MCF2A General Partner Limited, MCF2 GP Limited, MCF3 GP Limited, MCF3B General Partner Limited, MCF3A General Partner Limited, MCF2 FFF-GK Limited, MCF3 Cook Limited, MCF3 TEG Limited, MCF3 Squiz Limited, MC Medical Properties Limited, Mercury Capital No.1 Fund Limited, Mercury Capital No. 1 Trustee 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 North Limited, Oceania Securities Limited, Quartet Equities Limited,

Directors (continued)

MCF3 RE.Group Limited, MCF11 Limited, MCF3 Resourceco Limited, MCF3 Green Limited, MCF E&P Holdco Limited, MCF3 Amplify Limited, MCF3 Architectus Limited.

Name: Kathryn Mitchell

Qualifications: BA, CMIInstD

Type of Director: Independent Non-Executive Director

Occupation: Company Director

External Directorships:

Chambers@151 Limited, Christchurch International Airport Limited, Farmright Limited, Firsttrax Limited, Helpings Hands Holdings Limited, Link Engine Management Limited, Morrison Horgan Limited, The New Zealand Merino Company Limited, Heartland Group Holdings Limited.

Name: Shelley Maree Ruha

Qualifications: BCom, DipBank

Type of Director: Independent Non-Executive Director

Occupation: Company Director

External Directorships:

Analey Holdings Limited, IT & Business Consulting Limited, New Zealand Rural Land Management Limited, Partners Group Holdings Limited, Partners Life Limited, 9 Spokes International Limited, Taxgift Limited, Hobson Wealth Holdings Limited, Hobson Wealth Partner's Limited, Paysauce Limited.

Conflicts of interest policy

All Directors are required to disclose to the Board any actual or potential conflicts 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 by 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:

Edward John Harvey (Chairperson)

Independent Non-Executive Director

Bruce Robertson Irvine

Independent Non-Executive Director

Geoffrey Thomas Ricketts

Non-Independent Non-Executive Director

Shelley Maree Ruha

Independent Non-Executive Director

Directors' Statements

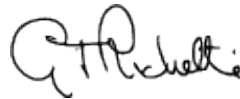
Each Director of the Bank states that he or she believes, after due enquiry, that:

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 2022:
 - (a) the Bank complied with all Conditions of Registration applicable during the period;
 - (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 22 August 2022 and has been signed by all the Directors.



B. R. Irvine (Chair)



G. T. Ricketts



J. K. Greenslade



K. Mitchell



E. J. Harvey



S. M. Ruha

Consolidated Statement of Comprehensive Income

For the year ended 30 June 2022

\$000's	Note	June 2022	June 2021
Interest income	3	275,770	272,562
Interest expense	3	66,205	73,753
Net interest income		209,565	198,809
Operating lease income	4	5,284	5,004
Operating lease expense	4	3,383	3,149
Net operating lease income		1,901	1,855
Lending and credit fee income		6,943	6,455
Other income	5	24,860	6,696
Net operating income		243,269	213,815
Operating expenses	6	96,203	100,852
Profit before impaired asset expense and income tax		147,066	112,963
Fair value (loss)/gain on investments		(315)	215
Impaired asset expense	8	14,692	14,579
Profit before income tax		132,059	98,599
Income tax expense	9	36,068	27,090
Profit for the year		95,991	71,509
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss, net of income tax:			
Effective portion of change in fair value of derivative financial instruments		6,540	8,928
Movement in fair value reserve		(712)	(5,646)
Items that will not be reclassified to profit or loss, net of income tax:			
Movement in defined benefit reserve		(171)	-
Other comprehensive income		(473)	-
Other comprehensive income for the year, net of income tax		5,184	3,282
Total comprehensive income for the year		101,175	74,791

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

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 30 June 2022

\$000's	Note	June 2022				June 2021			
		Share Capital	Reserves	Retained Earnings	Total Equity	Share Capital	Reserves	Retained Earnings	Total Equity
Balance at beginning of year		553,239	755	87,834	641,828	553,239	(2,527)	46,325	597,037
Total comprehensive income for the year									
Profit for the year		-	-	95,991	95,991	-	-	71,509	71,509
Other comprehensive (loss), net of income tax	16	-	5,657	(473)	5,184	-	3,282	-	3,282
Total comprehensive income for the year		-	5,657	95,518	101,175	-	3,282	71,509	74,791
Contributions by and distributions to owner									
Dividend to Heartland Group Holdings Limited	15	-	-	(35,500)	(35,500)	-	-	(30,000)	(30,000)
Total transactions with owner		-	-	(35,500)	(35,500)	-	-	(30,000)	(30,000)
Balance at end of the year		553,239	6,412	147,852	707,503	553,239	755	87,834	641,828

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Financial Position

As at 30 June 2022

\$000's	Note	June 2022	June 2021
Assets			
Cash and cash equivalents		221,469	112,903
Investments	10	275,714	358,975
Investment properties		11,832	11,832
Derivative financial instruments	11	44,487	14,111
Due from related parties	18	1,540	146
Finance receivables	12	3,762,231	3,213,593
Finance receivables - reverse mortgages	12	721,264	601,505
Operating lease vehicles	13	15,161	10,865
Right of use assets	17	13,660	15,654
Other assets	17	13,338	14,822
Intangible assets	17	58,418	52,831
Deferred tax asset	9	15,538	12,251
Total assets		5,154,652	4,419,488
Liabilities			
Deposits	14	3,597,144	3,219,522
Other borrowings	14	749,478	502,885
Due to related parties	18	1,535	3,210
Lease liabilities	17	15,726	17,780
Tax liabilities		22,479	7,556
Derivative financial instruments	11	6,335	4,789
Trade and other payables	17	54,452	21,918
Total liabilities		4,447,149	3,777,660
Equity			
Share capital	15	553,239	553,239
Retained earnings and other reserves		154,264	88,589
Total equity		707,503	641,828
Total equity and liabilities		5,154,652	4,419,488
<hr/>			
Total interest earning and discount bearing assets		4,918,261	4,215,116
Total interest and discount bearing liabilities		4,312,180	3,704,130

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 30 June 2022

\$000's	Note	June 2022	June 2021
Cash flows from operating activities			
Interest received		232,601	236,081
Operating lease income received		3,913	5,046
Lending, credit fees and other income received		11,740	8,431
Operating inflows		248,254	249,558
Interest paid		(87,131)	(88,635)
Payments to suppliers and employees		(47,169)	(86,261)
Taxation paid		(26,616)	(27,518)
Operating outflows		(160,916)	(202,414)
Net cash flows from operating activities before changes in operating assets and liabilities		87,338	47,144
Proceeds from sale of operating lease vehicles		4,482	6,821
Purchase of operating lease vehicles		(10,758)	(1,788)
Net movement in finance receivables		(636,981)	(136,202)
Net movement in deposits		376,052	(43,587)
Net movement in related party balances		(3,069)	(3,399)
Net cash flows (applied to) operating activities¹		(182,936)	(131,011)
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets		(11,889)	(6,520)
Net increase in investments		82,946	24,215
Total cash from investing activities		71,057	17,695
Net cash flows from investing activities		71,057	17,695
Cash flows from financing activities			
Net increase in wholesale funding		258,127	152,783
Total cash provided from financing activities		258,127	152,783
Dividends paid	15	(35,500)	(30,000)
Payment of lease liabilities		(2,182)	(2,027)
Total cash (applied to) financing activities		(37,682)	(32,027)
Net cash flows from financing activities		220,445	120,756
Net increase in cash held		108,566	7,440
Opening cash and cash equivalents		112,903	105,463
Closing cash and cash equivalents		221,469	112,903

¹Cash flows from operating activities do not include cash flows from wholesale funding which are included as part of financing activities.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 30 June 2022

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

\$000's	Note	June 2022	June 2021
Profit for the year		95,991	71,509
Add/(less) non-cash items:			
Depreciation and amortisation expense		10,294	14,293
Depreciation on lease vehicles	13	3,103	2,801
Capitalised net interest income and fee income		(41,863)	(34,555)
Impaired asset expense	8	14,692	14,579
Investment fair value movement		315	(215)
Other non-cash items		(17,490)	(23,210)
Total non-cash items		(30,949)	(26,307)
Add/(less) movements in operating assets and liabilities:			
Finance receivables		(636,981)	(136,202)
Operating lease vehicles		(6,276)	5,033
Other assets		(1,780)	2,884
Current tax		14,923	(3,715)
Derivative financial instruments		(23,002)	(122)
Deferred tax		(3,287)	3,076
Deposits		376,052	(43,587)
Other liabilities		32,373	(3,580)
Total movements in operating assets and liabilities		(247,978)	(176,213)
Net cash flows applied to operating activities		(182,936)	(131,011)

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Notes to the Financial Statements

For the year ended 30 June 2022

1 Financial statements preparation

Reporting entity

The financial statements presented are the consolidated financial statements comprising HBL and the Banking Group. Refer Note 26 – Significant subsidiaries for further details.

As at 30 June 2022, the Bank is a company incorporated in New Zealand under the Companies Act 1993, a registered bank under the Reserve Bank of New Zealand Act 1989 and a Financial Market Conduct (**FMC**) reporting entity for the purposes of the Financial Markets Conduct 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 Banking Group's functional and presentation currency. Unless otherwise indicated, amounts are rounded to the nearest thousand dollars.

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

The accounting policies adopted have been applied consistently throughout the periods presented in these financial statements.

Certain comparative balances have been reclassified to align with the presentation used in the current financial year. These reclassifications have no impact on the overall financial performance or financial position for the comparative year.

Basis of measurement

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

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 to, or has rights to, variable returns from its involvement with the entities and has the ability to affect those returns through its power over the entities. Intercompany transactions, balances and any unrealised income and expense (except for foreign currency transaction gains or losses) between controlled entities are eliminated.

Assets and liabilities in a transactional currency that is not the New Zealand dollar, are translated at the exchange rates ruling at balance date. Revenue and expense items are translated at the average rate at the balance date. Exchange differences are taken to the consolidated statement of comprehensive income.

1 Financial statements preparation (continued)

Changes in accounting standards

Accounting standards issued and effective

There have been no changes to accounting policies or new or amended standards that are issued and effective that are expected to have a material impact on the Banking Group.

Accounting standards issued not yet effective

The final version of NZ IFRS 17 Insurance Contracts was issued in August 2017 and is applicable to general and life insurance contracts. The standard will be effective for the Banking Group's reporting for the financial year ending 30 June 2024, including 30 June 2023 comparatives.

MARAC Insurance Limited (**MIL**), a subsidiary of HBL, ceased writing insurance policies in 2020 with the periodic policies expected to expire in 2025.

Other amendments to existing standards that are not yet effective are not expected to have a material impact on the Banking Group.

Estimates and judgements

The preparation of the Banking Group's consolidated financial statements requires the use of estimates and judgements. 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 the Banking Group's best estimate of future cash repayments and proceeds from any security held or by reference to risk profile groupings, historical loss data and forward-looking information. Refer to Note 8 - Impaired asset expense, and Note 12 - Finance receivables for further details.
- Fair value of reverse mortgages - Fair value is quantified by the transaction price and the Banking Group's subsequent best estimate of the risk profile of the reverse mortgage portfolio. Refer to Note 19 - Fair value for further details.
- Goodwill - Determining the fair value of assets and liabilities of acquired businesses requires the Banking Group to exercise judgement. The carrying value of goodwill is tested annually for impairment, refer to Note 17 - Other balance sheet items.

Assumptions made at each reporting date (e.g. the calculation of the provision for impairment and fair value adjustments) are based on best estimates as at that date. Although the Banking Group has internal controls in place to ensure that estimates can be reliably measured, actual amounts may differ from these estimates. 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. Revisions to accounting estimates are recognised in the reporting period in which the estimates are revised and in any future periods affected.

COVID-19 Pandemic - Impact on Estimates and Judgements

The COVID-19 pandemic resulted in the Banking Group adopting an economic overlay for expected credit losses (**ECL**) to its portfolios as at 30 June 2020 of pre-tax \$9.6 million in response to the uncertain but potential economic impact of COVID-19 on HBL's borrowers (**COVID Overlay**). The COVID Overlay was sized based on a range of techniques including stress testing, benchmarking, scenario analysis and expert judgement.

Whilst economic uncertainty remains, credit risk factors arising from the impact of COVID-19 are now apparent. Consequently the COVID Overlay has been released in full and it has been considered appropriate to create an economic overlay of \$8.0 million as at 30 June 2022, resulting in a net \$1.6 million release to profit or loss.

1 Financial statements preparation (continued)

COVID-19 Pandemic - Impact on Estimates and Judgements (continued)

The accounting judgement that is most impacted by the economic overlay is the ECL on finance receivables at amortised cost. The Banking Group measures the allowance for ECL using an impairment model in compliance with NZ IFRS 9 Financial Instruments.

Financial assets and liabilities

Financial Assets

Financial assets are classified based on:

- The business model within which the assets are managed; and
- Whether the contractual cash flows of the instrument represent solely payment of principal and interest (**SPPI**).

The Banking Group determines the business model at the level that reflects how groups of financial assets are managed. When assessing the business model, the Banking Group considers factors including how performance and risks are managed, evaluated and reported and the frequency and volume of, and reason for sales in previous periods.

Financial assets are classified into the following measurement categories:

Financial Assets	Measurement Category	Note
Bank bonds and floating rate notes	Fair value through other comprehensive income (FVOCI)	10
Public sector securities and corporate bonds	FVOCI	10
Local authority stock	FVOCI	10
Equity investments	Fair value through profit or loss (FVTPL) and FVOCI	10
Finance receivables – reverse mortgages	FVTPL	12
Finance receivables	Amortised cost	12

Financial assets measured at amortised cost

Financial assets are measured at amortised cost if they are held within a business model whose objective is achieved through holding the financial asset to collect contractual cash flows which represent SPPI.

Financial assets at amortised cost are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method.

Financial assets measured at FVOCI

Financial assets are measured at FVOCI if they are held within a business model whose objective is achieved both through collecting contractual cash flows which represent SPPI or selling the financial asset.

Financial assets at FVOCI are measured at fair value with unrealised gains and losses recognised in other comprehensive income except for interest income, impairment charges and foreign exchange gains and losses, which are recognised in profit or loss.

1 Financial statements preparation (continued)

Financial assets and liabilities (continued)

Financial Assets (continued)

Financial assets measured at FVTPL

Financial assets are measured at FVTPL if:

- They are held within a business model whose objective is achieved through selling or repurchasing the financial asset in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking; or
- They are designated at FVTPL upon initial recognition to eliminate or reduce an accounting mismatch.

Financial assets at FVTPL are measured at fair value with subsequent changes in fair value recognised in profit or loss.

Financial Liabilities

Financial liabilities are classified into the following measurement categories:

- Those to be measured at amortised cost;
- Those to be measured at FVTPL.

Financial liabilities measured at amortised cost

Financial liabilities are measured at amortised cost if they are not held for trading or designated at FVTPL.

Financial liabilities measured at amortised cost are accounted for using the effective interest rate method.

Financial liabilities measured at FVTPL

Financial liabilities are measured at FVTPL if:

- They are held for trading whose principal objective is achieved through selling or repurchasing the financial liability in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking; or
- They are designated at FVTPL upon initial recognition to eliminate or reduce an accounting mismatch.

Financial liabilities at FVTPL are measured at fair value with subsequent changes in fair value recognised in profit or loss.

Further details of the accounting policy for each category of financial asset or financial liability mentioned above is set out in the note for the relevant item.

The Banking Group's policies for determining the fair value of financial assets and financial liabilities are set out in Note 19 - Fair value.

Recognition

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 FVTPL) are initially recognised on the trade date at which the Banking Group becomes a party to the contractual provisions of the instrument.

1 Financial statements preparation (continued)

Derecognition

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.

The Banking Group enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all risks or 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 consolidated 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.

Financial liabilities are derecognised when the obligation is discharged, cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, the exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, with the difference in the respective carrying amounts recognised in profit or loss.

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

2 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.

Operating segments

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

Motor	Motor vehicle finance.
Reverse mortgages	Reverse mortgage lending in New Zealand. Refer to Note 21 - Credit risk exposure for details of this product.
Personal lending	Transactional, home loans and personal loans to individuals.
Business	Term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium sized businesses.
Rural	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.

Certain operating expenses, such as premises, IT and support centre costs are not allocated to operating segments and are included in Other. Finance receivables are allocated across the operating segments as assets and liabilities are managed centrally and therefore are not allocated across the operating segments.

The Banking Group's operating segments are different from the industry categories detailed in Note 21 - Credit risk exposure. The operating segments are primarily categorised by sales channel, whereas Note 21 - Credit risk exposure categorises exposures based on credit risk concentrations.

\$000's	Motor	Reverse Mortgages	Personal Lending	Business	Rural	Other	Total
June 2022							
Net interest income	69,730	29,957	10,218	70,602	29,460	(402)	209,565
Net other income	3,326	2,583	1,562	2,679	739	22,815	33,704
Net operating income	73,056	32,540	11,780	73,281	30,199	22,413	243,269
Operating expenses	3,792	4,485	6,417	9,358	3,038	69,113	96,203
Profit/(loss) before impaired asset expense and income tax	69,264	28,055	5,363	63,923	27,161	(46,700)	147,066
Fair value (loss) on investments	-	-	-	-	-	(315)	(315)
Impaired asset expense/(benefit)	1,481	-	(877)	11,831	2,257	-	14,692
Profit before income tax	67,783	28,055	6,240	52,092	24,904	(47,015)	132,059
Income tax expense	-	-	-	-	-	36,068	36,068
Profit/(loss) for the year	67,783	28,055	6,240	52,092	24,904	(83,083)	95,991
Total assets	1,382,367	721,264	332,783	1,387,352	687,232	643,654	5,154,652
Total liabilities							4,447,149

2 Segmental analysis (continued)

\$000's	Motor	Reverse Mortgages	Personal Lending	Business	Rural	Other	Total
June 2021							
Net interest income	65,829	23,098	13,648	66,112	30,579	(457)	198,809
Net other income	3,343	2,369	2,767	2,963	1,581	1,983	15,006
Net operating income	69,172	25,467	16,415	69,075	32,160	1,526	213,815
Operating expenses	3,787	4,397	6,241	11,340	2,124	72,963	100,852
Profit/(loss) before impaired asset expense and income tax	65,385	21,070	10,174	57,735	30,036	(71,437)	112,963
Fair value gain on investments	-	-	-	-	-	215	215
Impaired asset expense	5,298	-	1,977	5,655	1,649	-	14,579
Profit/(loss) before income tax	60,087	21,070	8,197	52,080	28,387	(71,222)	98,599
Income tax expense	-	-	-	-	-	27,090	27,090
Profit/(loss) for the year	60,087	21,070	8,197	52,080	28,387	(98,312)	71,509
Total assets	1,287,978	601,505	137,910	1,225,710	586,318	580,067	4,419,488
Total liabilities							3,777,660

3 Net interest income

Policy

Interest income and expense on financial instruments is measured using the effective interest rate method that discounts the financial instruments' future cash flows to their present value and allocates the interest income or expense over the life of the financial instrument. The effective interest rate is established on initial recognition of the financial assets or liabilities and is not subsequently revised. For financial instruments at amortised cost, the calculation of the effective interest rate includes all yield related fees and commissions paid or received that are an integral part of the underlying financial instrument.

\$000's	June 2022	June 2021
Interest income		
Cash and cash equivalents	805	117
Investments	5,156	6,979
Finance receivables	230,514	231,659
Finance receivables - reverse mortgages	39,295	33,807
Total interest income	275,770	272,562
Interest expense		
Retail deposits	45,387	55,295
Other borrowings	20,727	14,935
Net interest expense on derivative financial instruments	91	3,523
Total interest expense	66,205	73,753
Net interest income	209,565	198,809

4 Net operating lease income

Policy

As a lessor, the Banking Group retains substantially all the risks and rewards incidental to ownership of the assets and therefore classifies the leases 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.

\$000's	June 2022	June 2021
Operating lease income		
Lease income	4,161	3,908
Gain on disposal of lease assets	1,123	1,096
Total operating lease income	5,284	5,004
Operating lease expense		
Depreciation on lease assets	3,103	2,801
Direct lease costs	280	348
Total operating lease expense	3,383	3,149
Net operating lease income	1,901	1,855

5 Other income

Policy

Rental income from investment properties

Rental income from investment properties is recognised on a straight-line basis over the term of the relevant lease.

Insurance income

Insurance premium income and commission expense are recognised in profit or loss from the date of attachment of the risk over the period of the insurance contract. Claim expense is recognised in the profit or loss on an accrual basis once our liability to the policyholder has been confirmed under the terms of the contract.

\$000's	June 2022	June 2021
Rental income from investment properties	833	1,055
Insurance income	664	1,096
Gain on sale of investments	-	157
Other income	6,624	4,211
Fair value gain on derivative financial instruments	16,723	-
FX gain / (loss)	16	177
Total other income	24,860	6,696

6 Operating expenses

Policy

Operating expenses are recognised as the underlying service is rendered or over a period in which an asset is consumed or a liability is incurred.

\$000's	June 2022	June 2021
Personnel expenses	53,826	57,036
Directors' fees	542	676
Superannuation	1,045	979
Depreciation - property, plant and equipment	2,342	2,883
Legal and professional fees	1,697	2,110
Advertising and public relations	2,814	3,972
Depreciation - right of use asset	2,122	2,123
Technology services	9,014	6,908
Telecommunications, stationary and postage	1,492	1,610
Customer acquisition costs	2,419	2,123
Amortisation of intangible assets	5,830	9,285
Other operating expenses ¹	13,060	11,147
Total operating expenses	96,203	100,852

¹Other operating expenses include compensation of auditor which is disclosed in Note 7.

7 Compensation of auditor

\$000's	June 2022	June 2021
Audit and review of the financial statements ¹	593	599
Other assurance services paid to auditor ²	20	20
Total compensation of auditor	613	619

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

² Other assurance related services paid to the auditor comprise regulatory assurance services, trust deed reporting and registry audits.

8 Impaired asset expense

Policy

Impairment of finance receivables

At each reporting date, the Banking Group applies a three stage approach to measuring ECL to finance receivables not carried at fair value. The ECL model assesses whether there has been a significant increase in credit risk since initial recognition.

The ECL model is a forward looking model where impairment allowances are recognised before losses are actually incurred. On initial recognition, an impairment allowance is required, based on events that are possible in the next 12 months.

Assets may migrate between the following stages based on their change in credit quality:

Stage 1 - 12 months ECL (past due 30 days or less)

Where there has been no evidence of increased credit risk since initial recognition, and finance receivables are not credit impaired upon origination, the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months is recognised.

Stage 2 - Lifetime ECL not credit impaired (greater than 30 but less than 90 days past due)

Where there has been a significant increase in credit risk.

Stage 3 - Lifetime ECL credit impaired (90 days past due or more)

Objective evidence of impairment, so are considered to be in default or otherwise credit impaired.

In determining whether credit risk has increased all available information relevant to the assessment of economic conditions at the reporting date are taken into consideration. To do this the Banking Group considers its historical loss experience and adjusts this for current observable data. In addition to this the Banking Group uses reasonable and supportable forecasts of future economic conditions including experienced judgement to estimate the amount of an expected impairment loss. Future economic conditions consider macroeconomic factors such as unemployment, interest rate, gross domestic product, and inflation, and requires an evaluation of both the current and forecast direction of the economic cycle. The methodology and assumptions including any forecasts of future economic conditions are reviewed regularly as incorporating forward-looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the ECL.

The calculation of expected credit loss is modelled for portfolios of like assets. For portfolios which are either new or too small to model, judgement is used to determine impairment provisions.

For assets that are individually assessed for ECL, the allowance for ECL is calculated directly as the difference between the defaulted assets carrying value and the recoverable amount (being the present value of expected future cash flows, including cash flows from the realisation of collateral or guarantees, where applicable).

8 Impaired asset expense (continued)

\$000's	June 2022	June 2021
Non-securitised		
Individually impaired asset expense	10,782	9,131
Collectively impaired asset expense	3,980	5,606
Total non-securitised impaired asset expense	14,762	14,737
Securitised		
Collectively impaired asset expense	(70)	(158)
Total securitised impaired asset expense	(70)	(158)
Total		
Individually impaired asset expense	10,782	9,131
Collectively impaired asset expense	3,910	5,448
Total impaired asset expense	14,692	14,579

The Banking Group's models for estimating ECL for each of its portfolios are based on the historic credit experience of those portfolios. The models assume that economic conditions (such as Gross Domestic Product (GDP) growth, unemployment rates, and house price index forecasts) remain static over time. If the Banking Group forecasts that economic conditions may change in the foreseeable future, the Banking Group applies judgement to determine whether the modelled output should be subject to an economic overlay. Judgement is required to establish clear correlation between key economic indicators and the credit performance of the Group's unique portfolios.

9 Taxation

Policy

Income tax

Income tax expense for the year comprises current tax and movements in deferred tax balances, including any adjustment required for prior years' tax expense. Income tax expense is recognised in profit and 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.

Current tax

Current tax is the expected tax payable or receivable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to the tax payable or receivable 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).

Deferred tax

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for taxation purposes. As required by NZ IAS 12 Income Taxes, a deferred tax asset is recognised only to the extent that it is probable that a future taxable profit will be available to realise the asset.

Goods and services tax (GST)

Revenues, expenses and assets are recognised net 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 an expense or, if relevant, as part of the cost of acquisition of an asset.

9 Taxation (continued)

Income tax expense		
\$000's	June 2022	June 2021
Income tax recognised in profit or loss		
Current tax		
Current year	40,104	24,823
Adjustments for prior year	(748)	(483)
Deferred tax		
Current year	(2,895)	2,573
Adjustments for prior year	(393)	177
Total income tax expense recognised in profit or loss	36,068	27,090
Income tax recognised in other comprehensive income		
Current tax		
Derivatives at fair value reserve	(5,271)	(2,197)
Fair value movements of cash flow hedge	7,537	3,457
Total income tax expense recognised in other comprehensive income	2,266	1,260
Reconciliation of effective tax rate		
Profit before income tax	132,059	98,599
Prima facie tax @ 28%	36,976	27,607
Adjusted tax effect of items not taxable/deductible	232	(211)
Adjustments for prior year	(1,140)	(306)
Total income tax expense	36,068	27,090
Deferred tax assets comprise the following temporary differences:		
\$000's	June 2022	June 2021
Employee entitlements	1,234	1,009
Share based payment	501	202
Provision for impairment	14,176	14,305
Intangibles and property, plant and equipment	(2,972)	(3,800)
Deferred acquisition costs	(196)	(475)
Operating lease vehicles	680	479
Other temporary differences	2,116	531
Total deferred tax assets	15,538	12,251
Opening balance of deferred tax assets	12,251	15,327
Movement recognised in profit or loss	3,287	(3,076)
Closing balance of deferred tax assets	15,538	12,251

Financial Position

10 Investments

Policy

Investments are classified into one of the following categories:

Fair value through profit or loss

Investments under this category include equity investments and are measured at fair value plus transaction costs. Changes in fair value of these investments are recognised in profit or loss in the period in which they occur.

Fair value through other comprehensive income

Investments under this category include bank bonds, floating rate notes, local authority stock, public securities, corporate bonds and equity investments. These are initially measured at fair value, including transaction costs, and subsequently carried at fair value. Changes in fair value of these investments are recognised in other comprehensive income and presented within the fair value reserve.

Amortised cost

Investments under this category include bank deposits and are measured using effective interest rate method. They are held to collect contractual cash flows that are solely payments of principal and interest on the principal amount outstanding.

\$000's	June 2022	June 2021
Bank deposits, bank bonds and floating rate notes	261,258	351,614
Public sector securities and corporate bonds	12,953	5,543
Equity investments	1,503	1,818
Total investments	275,714	358,975

Refer to Note 19 - Fair value for details of the split between investments measured at fair value through profit or loss, fair value through other comprehensive income and amortised cost.

11 Derivative financial instruments

Policy

The Banking Group uses derivatives for risk management purposes. Derivatives held for risk management purposes include hedges that either meet the hedge accounting requirements set out in NZ IAS 39, or economic hedges not placed into an accounting hedge relationship.

Derivatives are recognised at their fair value, with the derivatives being carried as assets when their fair value is positive and as liabilities when their fair value is negative.

A hedged item is an asset, liability, firm commitment or highly probable forecast transaction that exposes the Banking Group to risk of changes in fair value or cash flows, and that is designated as being hedged. The Banking Group applies fair value hedge accounting to hedge movements in the value of fixed interest rate assets and liabilities subject to interest rate risk. The Banking Group applies cash flow hedge accounting to hedge the variability in highly probable forecast future cash flows attributable to interest rate risk on variable rate assets and liabilities.

Fair value hedge accounting

The criteria that must be met for a relationship to qualify for hedge accounting include:

- the hedging relationship must be formally designated and documented at inception of the hedge,
- effectiveness testing must be carried out on an on-going basis to ensure the hedge is effective, consistent with the originally documented risk management strategy, and
- the instruments or counterparty must be a third party external to the Banking Group.

The Banking Group documents, at the inception of the transaction, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Banking Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair value of hedged items.

Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify for fair value hedge accounting are recorded through profit or loss alongside any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

Where the hedged item is carried at amortised cost, the movement in fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to carrying amount of a hedged item carried at amortised cost is amortised to the consolidated statement of comprehensive income on an effective yield basis over the remaining period to maturity of the hedged item. Where a hedged item carried at amortised cost is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the consolidated statement of comprehensive income.

Cash flow hedge accounting

The criteria that must be met for a relationship to qualify for hedge accounting include:

- the hedging relationship must be formally designated and documented at inception of the hedge,
- effectiveness testing must be carried out on an on-going basis to ensure the hedge is effective, consistent with the originally documented risk management strategy, and
- the instruments or counterparty must be a third party external to the Banking Group.

11 Derivative financial instruments (continued)

Cash flow hedge accounting (continued)

The Banking Group documents, at the inception of the transaction, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Banking Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

A fair value gain or loss associated with the effective portion of a derivative designated as a cash flow hedge is recognised initially in the hedging reserve. The ineffective portion of a fair value gain or loss is recognised immediately in the consolidated statement of comprehensive income.

When a hedging derivative expires or is sold, the hedge no longer meets the criteria for hedge accounting, or the Banking Group elects to revoke the hedge designation, the cumulative gain or loss on the hedging derivative remains in the cash flow hedging reserve until the forecast transaction occurs and affects income, at which point it is transferred to the corresponding income or expense line. If a forecast transaction is no longer expected to occur, the cumulative gain or loss on the hedging derivative previously reported in the cash flow hedging reserve is immediately transferred to the consolidated statement of comprehensive income.

\$000's	June 2022			June 2021		
	Notional Principal	Fair Value Assets	Fair Value Liabilities	Notional Principal	Fair Value Assets	Fair Value Liabilities
Held for risk management						
Interest rate related contracts						
Swaps	1,478,151	44,487	6,335	1,104,012	14,106	4,520
Foreign currency related contracts						
Forwards	-	-	-	27,846	5	269
Total derivative financial instruments	1,478,151	44,487	6,335	1,131,858	14,111	4,789

The Banking Group has entered into credit support annexes (CSAs) which form a part of International Swaps and Derivatives Association (ISDA) Master Agreement, in respect of certain exposures relating to derivative transactions. As per these CSAs, the Banking Group or the counterparty needs to collateralise the market value of outstanding derivative transactions. As at 30 June 2022, the Banking Group has received \$32.34 million of cash collateral (2021: \$4.09 million) against derivative assets. The cash collateral received is not netted off against the balance of derivative assets disclosed in the consolidated statement of financial position.

The Banking Group actively manages interest rate risk by entering into derivative contracts to hedge against movements in interest rates. During the year interest rate swaps entered into by the Banking Group could not be designated into a hedging relationship with the portfolio of financial assets and liabilities held considering their underlying risks could no longer be critically matched against those of the interest rate swaps. Consequently, hedge accounting could not be established resulting in the recognition of fair value gains from the interest rate swaps in the consolidated statement of comprehensive income.

12 Finance receivables

(a) Finance receivables held at amortised cost

Policy

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 rate 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.

In determining whether credit risk has increased 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 are taken into consideration.

The calculation of expected credit loss is modelled for portfolios of like assets. For portfolios which are either new or too small to model, judgement is used to determine impairment provisions.

\$000's	June 2022	June 2021
Non-securitised		
Neither at least 90 days past due nor impaired	3,391,832	3,063,258
At least 90 days past due - at amortised cost	41,279	36,602
Individually impaired - at amortised cost	66,183	38,143
Gross finance receivables	3,499,294	3,138,003
Less provision for impairment	(50,232)	(50,809)
Total non-securitised finance receivables	3,449,062	3,087,194
Securitised		
Neither at least 90 days past due nor impaired	313,364	126,638
At least 90 days past due - at amortised cost	-	-
Individually impaired - at amortised cost	-	-
Gross finance receivables	313,364	126,638
Less provision for impairment	(195)	(239)
Total securitised finance receivables	313,169	126,399
Total		
Neither at least 90 days past due nor impaired	3,705,196	3,189,896
At least 90 days past due - at amortised cost	41,279	36,602
Individually impaired - at amortised cost	66,183	38,143
Gross finance receivables	3,812,658	3,264,641
Less provision for impairment	(50,427)	(51,048)
Total finance receivables	3,762,231	3,213,593

Refer to Note 22 - Asset quality for further analysis of finance receivables by credit risk concentration.

12 Finance receivables (continued)

(a) Finance receivables held at amortised cost (continued)

Movement in provision

The following table details the movement from the opening balance to the closing balance of the provision for impairment losses by class.

\$000's	12 - Month ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Specific Provision	Total
June 2022					
Non-securitised					
Impairment allowance as at 30 June 2021	24,216	2,334	16,630	7,629	50,809
Changes in loss allowance					
Transfer between stages	(3,800)	(2,391)	916	5,275	-
New and increased provision (net of collective provision releases)	(1,411)	1,922	11,499	5,507	17,517
Recovery of amounts written off	-	-	(2,755)	-	(2,755)
Credit impairment charge	(5,211)	(469)	9,660	10,782	14,762
Recovery of amounts previously written off	-	-	2,755	-	2,755
Write offs	-	-	(14,684)	(3,410)	(18,094)
Impairment allowance as at 30 June 2022	19,005	1,865	14,361	15,001	50,232
Securitised					
Impairment allowance as at 30 June 2021	216	22	1	-	239
Changes in loss allowance					
Transfer between stages	(6)	(109)	115	-	-
New and increased provision (net of collective provision releases)	(14)	85	(141)	-	(70)
Recovery of amounts written off	-	-	-	-	-
Credit impairment charge	(20)	(24)	(26)	-	(70)
Recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	26	-	26
Impairment allowance as at 30 June 2022	196	(2)	1	-	195
Total					
Impairment allowance as at 30 June 2021	24,432	2,356	16,631	7,629	51,048
Changes in loss allowance					
Transfer between stages	(3,806)	(2,500)	1,031	5,275	-
New and increased provision (net of collective provision releases)	(1,425)	2,007	11,358	5,507	17,447
Recovery of amounts written off	-	-	(2,755)	-	(2,755)
Credit impairment charge	(5,231)	(493)	9,634	10,782	14,692
Recovery of amounts previously written off	-	-	2,755	-	2,755
Write offs	-	-	(14,658)	(3,410)	(18,068)
Impairment allowance as at 30 June 2022	19,201	1,863	14,362	15,001	50,427

12 Finance receivables (continued)

(a) Finance receivables held at amortised cost (continued)

Movement in provision (continued)

\$000's	12 - Month ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Specific Provision	Total
June 2021					
Non-securitised					
Impairment allowance as at 30 June 2020	32,160	2,144	22,667	5,301	62,272
Changes in loss allowance					
Transfer between stages	(2,466)	(1,081)	(50)	3,597	-
New and increased provision (net of collective provision releases)	(3,495)	1,309	13,295	6,034	17,143
Recovery of amounts written off	-	-	(2,406)	-	(2,406)
Credit impairment charge	(5,961)	228	10,839	9,631	14,737
Recovery of amounts previously written off	-	-	2,406	-	2,406
Write offs	-	-	(19,291)	(7,303)	(26,594)
Effect of changes in foreign exchange rate	(33)	2	6	-	(25)
Acquisition of portfolio	133	22	188	-	343
Sale of portfolio	(2,083)	(62)	(185)	-	(2,330)
Impairment allowance as at 30 June 2021	24,216	2,334	16,630	7,629	50,809
Securitised					
Impairment allowance as at 30 June 2020	260	23	114	-	397
Changes in loss allowance					
Transfer between stages	(4)	(3)	7	-	-
New and increased provision (net of collective provision releases)	(40)	2	(120)	-	(158)
Recovery of amounts written off	-	-	-	-	-
Credit impairment charge	(44)	(1)	(113)	-	(158)
Recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	-	-	-
Effect of changes in foreign exchange rate	-	-	-	-	-
Acquisition of portfolio	-	-	-	-	-
Sale of portfolio	-	-	-	-	-
Impairment allowance as at 30 June 2021	216	22	1	-	239
Total					
Impairment allowance as at 30 June 2020	32,420	2,167	22,781	5,301	62,669
Changes in loss allowance					
Transfer between stages	(2,470)	(1,084)	(43)	3,597	-
New and increased provision (net of collective provision releases)	(3,535)	1,311	13,175	6,034	16,985
Recovery of amounts written off	-	-	(2,406)	-	(2,406)
Credit impairment charge	(6,005)	227	10,726	9,631	14,579
Recovery of amounts previously written off	-	-	2,406	-	2,406
Write offs	-	-	(19,291)	(7,303)	(26,594)
Effect of changes in foreign exchange rate	(33)	2	6	-	(25)
Acquisition of portfolio	133	22	188	-	343
Sale of portfolio	(2,083)	(62)	(185)	-	(2,330)
Impairment allowance as at 30 June 2021	24,432	2,356	16,631	7,629	51,048

12 Finance receivables (continued)

(a) Finance receivables held at amortised cost (continued)

Impact of changes in gross finance receivables held at amortised cost on allowance for ECL

\$000's	12 - Month ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Specific Provision	Total
June 2022					
Gross finance receivables as at 30 June 2021	3,016,571	164,728	45,199	38,143	3,264,641
Transfer between stages	(109,051)	24,871	28,786	55,394	-
Additions	2,059,181	-	-	3,002	2,062,183
Deletions	(1,383,366)	(72,084)	(13,341)	(26,946)	(1,495,737)
Write offs	-	-	(15,019)	(3,410)	(18,429)
Gross finance receivables as at 30 June 2022	3,583,335	117,515	45,625	66,183	3,812,658
June 2021					
Gross finance receivables as at 30 June 2020	2,825,973	183,260	73,729	24,667	3,107,629
Transfer between stages	(102,624)	67,219	12,906	22,499	-
Additions	1,421,835	-	-	955	1,422,790
Deletions	(1,128,613)	(85,751)	(20,815)	(466)	(1,235,645)
Write offs	-	-	(20,621)	(9,512)	(30,133)
Gross finance receivables as at 30 June 2021	3,016,571	164,728	45,199	38,143	3,264,641

(b) Finance receivables held at fair value

Policy

Finance receivables – reverse mortgages are initially recognised, and subsequently measured, at fair value through profit or loss.

\$000's	June 2022	June 2021
Finance receivables - reverse mortgages	721,264	601,505
Total finance receivables - reverse mortgages	721,264	601,505

Note 19 (a) - Financial instruments measured at fair value discloses further information regarding the Banking Group's valuation policy.

Note 21 - Credit risk exposure discloses further information regarding how reverse mortgage loans operate.

Credit risk adjustments on financial assets designated at fair value through profit or loss

There were no credit risk adjustments on individual financial assets.

13 Operating lease vehicles

Policy

Operating lease vehicles are stated at cost less accumulated depreciation.

Operating lease vehicles are depreciated on a straight-line basis over their expected useful 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.

\$000's	June 2022	June 2021
Cost		
Opening balance	16,114	24,098
Additions	10,758	1,788
Disposals	(6,422)	(9,772)
Closing balance	20,450	16,114
Accumulated depreciation		
Opening balance	5,249	6,495
Depreciation charge for the year	3,103	2,801
Disposals	(3,063)	(4,047)
Closing balance	5,289	5,249
Opening net book value	10,865	17,603
Closing net book value	15,161	10,865

The future minimum lease payments receivable under operating leases not later than one year is \$3.057 million (2021: \$2.141 million), within one to five years is \$6.465 million (2021: \$1.406 million) and over five years is nil (2021: nil).

14 Borrowings

Policy

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.

\$000's	June 2022	June 2021
Deposits	3,597,144	3,219,522
Total borrowings related to deposits	3,597,144	3,219,522
Unsubordinated notes	272,983	284,517
Securitised borrowings	267,779	108,150
Certificate of deposit	198,715	69,853
Money market borrowings	10,001	-
Repurchase agreement	-	40,365
Total other borrowings	749,478	502,885

Deposits and unsubordinated notes rank equally and are unsecured.

14 Borrowings (continued)

The Banking Group has the following unsubordinated notes on issue at balance sheet date:

Principal	Valuation	Issue Date	Maturity Date	Frequency of Interest Repayment
\$125 million	Amortised cost	12 April 2019	12 April 2024	Semi-annually
\$150 million	Amortised cost	21 September 2017	21 September 2022	Semi-annually

At 30 June 2022 the Banking Group had the following securitised borrowings outstanding:

- Heartland Auto Receivables Warehouse Trust 2018-1 securitisation facility \$400 million, drawn \$268 million (2021: \$300 million, drawn \$108 million). Notes issued to investors are secured over the assets of the Heartland Auto Receivables Warehouse Trust 2018-1. The facility has a maturity date of 26 August 2023.

15 Share capital and dividends

Policy

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 effect.

	June 2022 Number of Shares	June 2021 Number of Shares
000's		
Issued shares		
Opening balance	565,430	565,430
Closing balance	565,430	565,430

There were nil new shares issued during the period (2021:nil).

Dividends paid

	June 2022 Date Declared	\$000's	June 2021 Date Declared	\$000's
Dividend to HGH	21 February 2022	35,500	18 June 2021	30,000
Total dividends paid		35,500		30,000

16 Other reserves

\$000's	Fair Value Reserve	Defined Benefit Reserve	Cash Flow Hedge Reserve	Total
June 2022				
Balance as at 30 June 2021	(322)	171	906	755
Other comprehensive income, net of income tax	(712)	(171)	6,540	5,657
Balance as at 30 June 2022	(1,034)	-	7,446	6,412
June 2021				
Balance as at 30 June 2020	5,324	171	(8,022)	(2,527)
Other comprehensive income, net of income tax	(5,646)	-	8,928	3,282
Balance as at 30 June 2021	(322)	171	906	755

17 Other balance sheet items

Policy

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

\$000's	June 2022	June 2021
Other assets		
Trade receivables	-	635
GST receivables	1,506	1,476
Prepayments	4,697	2,832
Property, plant and equipment	6,960	8,830
Other receivables	175	1,049
Total other assets	13,338	14,822

Policy

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. 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 the assets' estimated useful lives. The expected useful life of the software varies up to ten years.

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 acquired. 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.

17 Other balance sheet items (continued)

\$000's	June 2022	June 2021
Computer software		
Cost	54,777	43,360
Accumulated depreciation	26,158	20,328
Net carrying value of computer software	28,619	23,032
Goodwill		
Cost	29,799	29,799
Net carrying value of goodwill	29,799	29,799
Total intangible assets	58,418	52,831

For the purposes of impairment testing, goodwill is allocated to cash generating units. A Cash Generating Unit (**CGU**) is the smallest identifiable group of assets that generate independent cash inflows. The Banking Group has assessed that goodwill should be allocated to Heartland Bank Limited as the smallest identifiable CGU.

Goodwill is tested for impairment at a cash generating unit level. The recoverable amounts are determined on a value in use basis using a five-year discounted cash flow methodology based on financial budget and forecasts. Key assumptions used in the models included a discount rate of 10% and a terminal growth rate of 2% which reflect both past experience and external sources of information. The recoverable amounts for each CGU are compared to the respective carrying value of net assets.

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 2022 (30 June 2021: nil).

Policy

Employee benefits

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

\$000's	June 2022	June 2021
Trade and other payables		
Trade payables	13,329	9,218
Insurance liability	1,840	3,354
Employee benefits	5,810	4,625
Other tax payables	1,132	630
Collateral received on derivatives	32,341	4,091
Total trade and other payables	54,452	21,918

17 Other balance sheet items (continued)

Policy

Leases

The Banking Group leases office space, car parks, equipment and cars. Rental contracts are typically made for fixed periods but may have extension options. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions.

In determining the lease term, all facts and circumstances that create an economic incentive to exercise an extension option are considered. Extension options are only included in the lease term if the lease is reasonably certain to be extended.

Lease liabilities are measured at the present value of the remaining lease payments and discounted using the Banking Group's incremental borrowing rate (**IBR**). Lease liabilities are measured using the effective interest method. Carrying amounts are remeasured only upon reassessments and lease modifications.

Right of use assets are depreciated at the shorter of lease term or the Banking Group's depreciation policy for that asset class.

\$000's	June 2022	June 2021
Right of use assets		
Balance at beginning of year	15,654	17,843
Depreciation charge for the year, included within depreciation expense in the income statement	(2,122)	(2,123)
Additions/(terminations) to right of use assets	128	(66)
Total right of use assets	13,660	15,654
Lease liability		
Current	3,181	2,124
Non-current	12,545	15,656
Total lease liability	15,726	17,780
Interest expense relating to lease liability	470	555

18 Related party transactions and balances

Policy

A person or entity is a related party under the following circumstances:

- a) A person or a close member of that person's family if that person:
 - i) has control or joint control over the Bank;
 - ii) has significant influence over the Bank; or
 - iii) is a member of the key management personnel of the Bank.
- b) An entity is related to the Bank if any of the following conditions applies:
 - i) The entity and the Bank are members of the same group;
 - ii) One entity is an associate or joint venture of the other entity;
 - iii) Both entities are joint ventures of the same third party;
 - iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity;
 - v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the bank;
 - vi) The entity is controlled, or jointly controlled by a person identified in (a); and
 - vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(a) Transactions with key management personnel

Key management personnel (**KMP**), are those who, directly or indirectly, have authority and responsibility for planning, directing and controlling the activities of HGH and HBL. This includes all executive staff, Directors and their close family members.

18 Related party transactions and balances (continued)

(a) Transactions with key management personnel (continued)

KMP receive personal banking and financial investment services from the Bank in the ordinary course of business. The terms and conditions, for example interest rates and collateral, and the risks to the Bank are comparable to transactions with other employees and did not involve more than the normal risk of repayment or present other unfavourable features.

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

\$000's	June 2022	June 2021
Transactions with key management personnel		
Interest income receivable	26	39
Interest expense payable	(24)	(22)
Key management personnel compensation		
Short-term employee benefits	(2,373)	(2,793)
Short-term employee benefits - HGH parent	(6,417)	(6,591)
Share-based payment expense	(1,915)	(1,797)
Total transactions with key management personnel	(10,703)	(11,164)
Due from/(to) key management personnel		
Lending	229	415
Borrowings - deposits	(508)	(23,409)
Total due (to) key management personnel	(279)	(22,994)

(b) Transactions with related parties

The Banking Group's ultimate parent company is HGH.

The Bank has regular transactions with its ultimate parent company, fellow subsidiaries and subsidiaries (collectively known as the Heartland Group) on agreed terms. The transactions include the provision of tax and administrative services and customer operations. Banking facilities are provided by HBL to other Banking Group entities on normal commercial terms as with other customers. There is no lending from the Banking Group to HGH.

Related party transactions between the Banking Group eliminate on consolidation. Related party transactions outside of the Banking Group are as follows:

\$000's	June 2022	June 2021
Heartland Group Holdings Limited (HGH)		
Interest expense	68	21
Deposits/(withdrawals)	(31,500)	31,000
Dividends paid to HGH	35,500	30,000
Management fees payable to HGH	8,327	15,785
Management fees receivable from HGH	2,164	1,149
Heartland Australia Group Pty Limited (HAG)		
Sale of Spotcap facility	-	28,049
Sale of Harmony Australia Fund	-	40,966

18 Related party transactions and balances (continued)

(b) Transactions with related parties (continued)

\$000's	June 2022	June 2021
Australian Seniors Finance Pty Limited (ASF)		
Management fees payable to ASF	-	4
Management fees receivable from ASF	2,752	1,707
ASF Settlement Trust		
Sale of Australian dollar reverse mortgage loan book	-	45,971
Southern Cross Building Society Staff Superannuation (SCBS)		
Interest expense payable to SCBS	6	12
Management fees receivable from SCBS	10	10
Cash received from SCBS	350	-

(c) Due from/to related parties

\$000's	June 2022	June 2021
Due from		
Australian Seniors Finance Pty Limited	1,540	146
Total due from related parties	1,540	146
Due to		
Heartland Group Holdings Limited	1,535	3,210
Total due to related parties	1,535	3,210

(d) Other balances with related parties

\$000's	June 2022	June 2021
Heartland Group Holdings Limited		
Retail deposits owing to HGH	4,636	36,068
Southern Cross Building Society Staff Superannuation		
Retail deposits owing to SCBS ¹	35	1,760

¹ During the year, the beneficiaries of SCBS accepted a settlement offer and were paid a final lump sum totalling \$1.3 million. This was supported by an actuarial valuation and approved by the Financial Markets Authority (FMA). The residual balance was transferred to HBL as the employer, leaving the above balance to cover remaining costs.

HGH has indemnified HBL against a non performing loan which had a balance of \$4.3 million as at 30 June 2022 (2021: nil).

19 Fair value

Policy

Fair value is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

On initial recognition, the transaction price generally represents the fair value of the financial instrument, unless there is observable information from an active market that provides a more appropriate 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.

19 Fair value (continued)

The Banking Group measures fair values using the following fair value hierarchy, which reflects the observability of the inputs used in measuring fair value:

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 consolidated statement of financial position.

The Banking Group has an established framework in performing valuations required for financial reporting purposes including Level 3 fair values. The Banking Group regularly reviews and calibrates significant unobservable inputs and valuation adjustments in accordance with market participants' views. If external valuation specialists are engaged to measure fair values, the Banking Group assesses the evidence obtained from these specialists to support the conclusion of these valuations. All significant valuations are reported to the Banking Group's Board Audit Committee for approval prior to its adoption in the financial statements.

Investments

Investments in public sector securities and corporate bonds are stated at fair value through other comprehensive income (**FVOCI**), 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 - 10 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 equity securities are classified as fair value through profit or loss unless an irrevocable election is made by the Banking Group to measure at FVOCI. Investment in listed securities traded in liquid, active markets where prices are readily observable are measured under Level 1 of the fair value hierarchy with no modelling or assumptions used in the valuation. Investments in unlisted equity securities are measured under Level 3 of the fair value hierarchy with the fair value being based on unobservable inputs using market accepted valuation techniques. Where appropriate, the Banking Group may apply adjustments to the above-mentioned techniques to determine fair value of an equity security to reflect the underlying characteristics. These adjustments are reflective of market participant considerations in valuing the said security.

Investment properties

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

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).

Finance receivables - reverse mortgages

Reverse mortgage loans are classified at FVTPL. On initial recognition the Banking Group considers the transaction price to represent the fair value of the loan.

19 Fair value (continued)

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

Finance receivables - reverse mortgages (continued)

For subsequent measurement the Banking Group has considered if the fair value can be determined by reference to a relevant active market or observable inputs, but has concluded relevant support is not currently available. In the absence of such market evidence the Banking Group has used valuation techniques (income approach) including actuarial assessments to consider the fair value.

When the Banking Group enters into a reverse mortgage loan the Banking Group has set expectations regarding the loan's current and future risk profile and expectation of performance. This expectation references a wide range of assumptions including:

- mortality and potential move into care;
- voluntary exits;
- house price changes;
- no negative equity guarantee; and
- interest rate margin.

At balance date the Banking Group does not consider any of the above expectations to have moved outside of the original expectation range. Therefore, the Banking Group has continued to estimate the fair value of the portfolio at transaction price. There has been no fair value movement recognised in profit or loss during the period (2021: nil). Fair value is not highly sensitive to the above assumptions due to the nature of reverse mortgage loans. In particular, given conservative origination loan-to-value ratio criteria, a material deterioration in house prices combined with a material increase in interest rates over a sustained period of time would likely need to occur before any potential impact to fair value. While noting the significant uncertainty around future economic conditions, based on current judgement there is no evidence that COVID-19 has impacted or will have a long-term adverse impact on market conditions, particularly regarding the key elements of house prices or interest rates, that would materially influence the fair value of the reverse mortgage portfolio at balance date.

The Banking Group will continue to reassess the existence of a relevant active market and movements in expectations on an on-going basis.

Derivative financial instruments

Interest rate and foreign currency related contracts are recognised in the financial statements at fair value. Fair values are determined from observable market prices as at the reporting date, discounted cash flow models or option pricing models as appropriate (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 consolidated statement of financial position.

19 Fair value (continued)

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

\$000's	Level 1	Level 2	Level 3	Total
June 2022				
Assets				
Investments	271,790	-	1,503	273,293
Investment properties	-	-	11,832	11,832
Derivative financial instruments	-	44,487	-	44,487
Finance receivables - reverse mortgages	-	-	721,264	721,264
Total financial assets measured at fair value	271,790	44,487	734,599	1,050,876
Liabilities				
Derivative financial instruments	-	6,335	-	6,335
Total financial liabilities measured at fair value	-	6,335	-	6,335
June 2021				
Assets				
Investments	259,041	92,476	1,818	353,335
Investment properties	-	-	11,832	11,832
Derivative financial instruments	-	14,111	-	14,111
Finance receivables - reverse mortgages	-	-	601,505	601,505
Total financial assets measured at fair value	259,041	106,587	615,155	980,783
Liabilities				
Derivative financial instruments	-	4,789	-	4,789
Total financial liabilities measured at fair value	-	4,789	-	4,789

There were no transfers between levels in the fair value hierarchy in the year ended 30 June 2022 (2021: nil).

19 Fair value (continued)

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

The movement in Level 3 assets measured at fair value are below:

\$000's	Finance Receivables - Reverse Mortgage	Investments	Investment Properties	Total
June 2022				
As at 30 June 2021	601,505	1,818	11,832	615,155
New loans	162,166	-	-	162,166
Repayments	(83,629)	-	-	(83,629)
Capitalised Interest and fees	41,864	-	-	41,864
Fair value (loss) on investment	-	(315)	-	(315)
Other	(642)	-	-	(642)
As at 30 June 2022	721,264	1,503	11,832	734,599
June 2021				
As at 30 June 2020	609,346	2,303	11,132	622,781
New loans	99,510	-	-	99,510
Repayments	(97,577)	-	-	(97,577)
Capitalised Interest and fees	35,775	-	-	35,775
Disposal	(45,650)	-	-	(45,650)
Fair value (loss)/gain on investment	-	(485)	700	215
Other	101	-	-	101
As at 30 June 2021	601,505	1,818	11,832	615,155

(b) Financial instruments not measured at fair value

The following assets and liabilities of the Banking Group are not measured at fair value in the consolidated statement of financial position.

Cash and cash equivalents

Cash and cash equivalents are measured at amortised cost and their carrying value is considered equivalent to their fair 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 7.77% (2021: 7.08%). 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.

19 Fair value (continued)

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

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 average current market rate used to fair value borrowings was 3.57% (2021: 1.23%).

Due to and from related parties

The fair value of amounts due to and from related parties is considered equivalent to their carrying value due to their short term nature.

Other financial assets and financial liabilities

The fair value of financial instruments such as short-term trade receivables and payables is considered equivalent to their carrying value due to their short-term nature.

The following table sets out financial instruments not measured at fair value, compares their carrying value against their fair value and analyses them by level in the fair value hierarchy.

\$000's	June 2022			June 2021		
	Fair Value Hierarchy	Total Fair Value	Total Carrying Value	Fair Value Hierarchy	Total Fair Value	Total Carrying Value
Assets						
Cash and cash equivalents	Level 1	221,469	221,469	Level 1	112,903	112,903
Investments ¹	Level 2	2,418	2,421	Level 2	5,640	5,639
Finance receivables	Level 3	3,701,694	3,762,231	Level 3	3,283,159	3,213,593
Due from related parties	Level 3	1,540	1,540	Level 3	146	146
Other financial assets	Level 3	175	175	Level 3	1,684	1,684
Total financial assets		3,927,296	3,987,836		3,403,532	3,333,965
Liabilities						
Retail deposits	Level 2	3,595,554	3,597,144	Level 2	3,228,791	3,219,522
Borrowings - securitised	Level 2	267,779	267,779	Level 2	108,150	108,150
Other borrowings	Level 2	481,699	481,699	Level 2	394,735	394,735
Due to related parties	Level 3	1,535	1,535	Level 3	3,210	3,210
Other financial liabilities	Level 3	47,510	47,510	Level 3	16,663	16,663
Total financial liabilities		4,394,077	4,395,667		3,751,549	3,742,280

¹Included within investments are bank deposits which are held to support the Banking Group's contractual cash flows. Such investments are measured at amortised cost.

19 Fair value (continued)

(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:

\$000's	FVOCI	FVTPL	Amortised Cost	Total Carrying Value	Total Fair Value
June 2022					
Assets					
Cash and cash equivalents	-	-	221,469	221,469	221,469
Investments	271,790	1,503	2,421	275,714	275,711
Investment properties	-	11,832	-	11,832	11,832
Finance receivables	-	-	3,762,231	3,762,231	3,701,694
Finance receivables - reverse mortgages	-	721,264	-	721,264	721,264
Derivative financial instruments	25,403	19,084	-	44,487	44,487
Due from related parties	-	-	1,540	1,540	1,540
Other financial assets	-	-	175	175	175
Total financial assets	297,193	753,683	3,987,836	5,038,712	4,978,172
Liabilities					
Deposits	-	-	3,597,144	3,597,144	3,595,554
Other borrowings	-	-	749,478	749,478	749,478
Derivative financial instruments	1,099	5,236	-	6,335	6,335
Due to related parties	-	-	1,535	1,535	1,535
Other financial liabilities	-	-	47,510	47,510	47,510
Total financial liabilities	1,099	5,236	4,395,667	4,402,002	4,400,412
June 2021					
Assets					
Cash and cash equivalents	-	-	112,903	112,903	112,903
Investments	351,518	1,818	5,639	358,975	358,975
Investment properties	-	11,832	-	11,832	11,832
Finance receivables	-	-	3,213,593	3,213,593	3,283,159
Finance receivables - reverse mortgages	-	601,505	-	601,505	601,505
Derivative financial instruments	3,213	10,898	-	14,111	14,111
Due from related parties	-	-	146	146	146
Other financial assets	-	-	1,684	1,684	1,684
Total financial assets	354,731	626,053	3,333,965	4,314,749	4,384,315
Liabilities					
Deposits	-	-	3,219,522	3,219,522	3,228,791
Other borrowings	-	-	502,885	502,885	502,885
Derivative financial instruments	4,395	394	-	4,789	4,789
Due to related parties	-	-	-	3,210	3,210
Other financial liabilities	-	-	16,663	16,663	16,663
Total financial liabilities	4,395	394	3,739,070	3,747,069	3,756,338

Risk Management

20 Enterprise risk management program

The board of directors (the **Board**) sets and monitors the Banking Group's risk appetite across the primary risk domains of credit, capital, liquidity, market (including interest rate), operational and 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, as outlined within the Enterprise Risk Management Framework (**ERMF**). Collectively, these processes are known as the Bank's Enterprise Risk Management Program (**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:

- The Board's Risk Appetite Statement.
- Heartland's Internal Capital Adequacy Assessment Program (**ICAAP**) including appropriate stress testing scenarios.
- The effectiveness of the ERMF and internal compliance and risk related policies, including approval or variation of policies, procedures and standards.
- Respond to changes anticipated in the economic, business and regulatory environment.
- Conduct, culture and customer outcomes, including emerging risks and any areas of concern.
- Credit exposures of the Bank, including the Delegated Lending Authority Policy and Framework.
- New products, including the process for approval of new products.

The BRC consists of three non-executive directors. Two members of the BRC sit on the Board Audit Committee (**BAC**). In addition, the CEO HBL, CRO, Head of Internal Audit and the CFO Heartland Group Holdings Limited (or their nominee, subject to the Chair's prior approval) attend the BRC meetings, and the directors who are not members of the BRC are entitled to attend meetings and to receive copies of the BRC papers.

Board Audit Committee

The BAC focuses on financial reporting and application of accounting policies as part of the internal control and risk assessment framework. The BAC 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 BAC receives regular reports from Internal Audit.

Charters for both the BRC and the BAC 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 Chair of the BRC. The Head of Internal Audit has a direct reporting line to the Chair of the BAC.

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 Banking Group 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.

20 Enterprise risk management program (continued)

Internal Audit (continued)

A regular cycle of review has been implemented to cover all areas of the business, focused on assessment, management and control of risks identified. 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 to the BAC of the Bank. A schedule of all outstanding internal control issues is maintained and presented to the BAC to assist the BAC 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.

Asset and Liability Committee (ALCO)

The ALCO comprises the CEO HBL, CFO, CRO, Head of Retail, Financial Controller HBL and Chief Distribution Officer. The ALCO has responsibility for overseeing aspects of risk management of the Banking Group's financial position. 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 HBL, CRO, CFO, Financial Controller HBL and Head of Internal Audit. The ERC has responsibility for overseeing 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 generally meets monthly, and provides minutes to the BRC. ERC's specific responsibilities include decision making and oversight of operational risk, compliance risk, and credit risk.

Operational and compliance risk

Operational and 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 and 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 and compliance risk, the Banking Group operates a "three lines of defence" model which outlines principles for the roles, responsibilities and accountabilities for operational and compliance risk management:

20 Enterprise risk management program (continued)

Operational and compliance risk (continued)

- 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 and 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 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 its stated risk appetite.

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

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.

Interest rate risk

Interest rate risk refers to exposure of an entity's earnings and / or capital because of a mismatch between the interest rate exposures of its assets and liabilities. Interest rate risk for the Banking Group arises from the provision of non-traded retail banking products and services and from traded wholesale transactions entered into to reduce aggregate interest rate risk (known as hedges). This risk arises from four key sources:

- Mismatches between the repricing dates of interest bearing assets and liabilities (yield curve and repricing risk);
- Banking products repricing differently to changes in wholesale market rates (basis risk);
- Loan prepayment or deposit early withdrawal behaviour from customers that deviates from the expected or contractually agreed behaviour (optionality risk); and
- The effect of internal or market forces on a bank's net interest margin where, for example, in a low rate environment any fall in rates will further decrease interest income earned on the assets whereas funding cost cannot be reduced as it is already at the minimum level (margin compression risk).

Refer Note 24 - Interest rate risk for further details regarding interest rate risk.

Foreign exchange 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 holding of AUD assets.

20 Enterprise risk management program (continued)

Counterparty Credit Risk

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

- Cash and cash equivalents;
- Finance receivables;
- Holding of investment securities; and
- 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.

21 Credit risk exposure

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 BRC has authority from the Board for approval of all credit exposures. Lending authority has been provided to the Banking Group's Credit Committee, 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 Committee and ultimately through to the BRC.

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

21 Credit risk exposure (continued)

Reverse mortgage loans and negative equity risk

Reverse mortgage loans are a form of mortgage lending designed for the needs of people over 60 years of age. 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 into 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. Negative equity risk arises from the promise by the Banking Group that the maximum repayment amount is limited to the net sale proceeds of the borrowers' 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 the Banking Group will accept for reverse mortgage lending, a key aspect of the Banking Group'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. The policy is managed and reviewed periodically to ensure appropriate consistency across locations.

Business Finance Guarantee Scheme (BFGS)

The Bank, along with other registered banks in New Zealand, has entered into a Deed of Indemnity with the New Zealand Government to implement the New Zealand Government's Business Finance Guarantee Scheme. The purpose of the scheme is to provide short term credit to eligible small and medium size businesses, who have been impacted by the economic effects of COVID-19. The scheme allows banks to lend to a maximum of \$5 million for a maximum of five years. The New Zealand Government will guarantee 80% of any loss incurred (credit risk) with the Bank holding the remaining 20%. As at 30 June 2022 the Bank had a total exposure of \$64.8 million (2021: \$64.3 million) to its customers under the scheme. BFGS has concluded on 30 June 2021 with scheme loans no longer being available.

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 on balance sheet exposures set out below are based on net carrying amounts as reported in the consolidated statement of financial position.

\$000's	June 2022	June 2021
On balance sheet:		
Cash and cash equivalents	221,469	112,903
Investments	274,211	357,157
Finance receivables	3,762,231	3,213,593
Finance receivables - reverse mortgages	721,264	601,505
Derivative financial assets	44,487	14,111
Due from related parties	1,540	146
Other financial assets	175	1,684
Total on balance sheet credit exposures	5,025,377	4,301,099
Off balance sheet:		
Letters of credit, guarantee commitments and performance bonds	8,969	13,484
Undrawn facilities available to customers	272,735	208,855
Conditional commitments to fund at future dates	34,791	19,083
Total off balance sheet credit exposures	316,495	241,422
Total credit exposures	5,341,872	4,542,521

As at 30 June 2022 there was \$0.003 million undrawn lending commitments available to counterparties for whom drawn balances are classified as individually impaired (2021: \$0.216 million).

21 Credit risk exposure (continued)

Concentration of credit risk by geographic region

\$000's	June 2022	June 2021
New Zealand	5,176,026	4,332,737
Australia	3,520	753
Rest of the world ¹	212,753	260,079
	5,392,299	4,593,569
Provision for impairment	(50,427)	(51,048)
Total credit exposures	5,341,872	4,542,521

¹ These overseas assets are primarily NZD-denominated investments in AA+ and high quality investment grade securities issued by offshore supranational agencies ("Kauri Bonds").

Concentration of credit risk by industry sector

The Australian and New Zealand Standard Industrial Classification (**ANZSIC**) codes have been used as the basis for categorising customer and investee industry sectors.

\$000's	June 2022	June 2021
Agriculture	747,618	670,428
Forestry and fishing	148,797	153,160
Mining	12,524	12,684
Manufacturing	78,432	76,951
Finance and insurance	685,938	577,486
Wholesale trade	41,986	56,522
Retail trade and accommodation	423,975	279,388
Households	2,134,097	1,780,799
Other business services	189,860	148,011
Construction	291,971	241,668
Rental, hiring and real estate services	199,388	185,320
Transport and storage	323,732	297,920
Other	113,981	113,232
	5,392,299	4,593,569
Provision for impairment	(50,427)	(51,048)
Total credit exposures	5,341,872	4,542,521

Credit exposures to connected persons

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.

21 Credit risk exposure (continued)

Credit exposures to connected persons (continued)

In accordance with its conditions of registration, the Banking Group's aggregate credit exposures to all connected persons must not exceed its rating contingent limit of 15% of tier one capital. Within the overall rating contingent limit, there is a sub-limit of 15% of tier one capital which applies to the aggregate credit exposures to non-bank connected persons. There have been no rating-contingent limit changes during the accounting period.

	Peak End-of-Day for	
	As at June 2022	Year Ended June 2022
Credit exposures to connected persons (\$000's)	1,540	1,540
As a percentage of Tier 1 capital of the Banking Group at end of the year (%)	0.25%	0.25%
Credit exposures to non-bank connected persons (\$000's)	1,540	1,540
As a percentage of Tier 1 capital of the Banking Group at end of the year (%)	0.25%	0.25%

As at 30 June 2022, the Banking Group had no aggregate contingent exposures to connected persons arising from risk lay-off arrangements in respect of credit exposures to counterparties (excluding counterparties that are connected persons). The aggregate amount of the Banking Group's individual credit provisions provided against credit exposure to connected persons was nil at 30 June 2022.

Credit exposure to individual counterparties

The Banking Group's aggregate concentration of credit exposure to individual counterparties is calculated based on the actual credit exposure. Credit 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 supranational or quasi-sovereign agency with a long-term credit rating of A- or A3 or above, or its equivalent are excluded.

The peak end-of-day aggregate concentration of credit exposure to individual counterparties has been calculated by determining the maximum end-of-day aggregate amount of credit exposure over the relevant six-month period and then dividing the amount by the Banking Group's common equity tier one capital as at 30 June 2022.

	Number of Exposures	
	Number of Exposures	Peak End-of-Day over
	As at June 2022	6 Months to June 2022
Exposures to banks		
With a long-term credit rating of A- or A3 or above, or its equivalent:		
10% to less than 15% of CET1 capital	-	-
15% to less than 20% of CET1 capital	1	1
20% to less than 25% of CET1 capital	1	1
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent		
	-	-
Exposures to non-banks		
Total number of exposures to non-banks that are greater than 10% to less than 15% of CET1 capital that do not have a long-term credit rating.	1	1

22 Asset quality

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

Corporate Business lending including 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.

All Other This relates primarily to consumer lending to individuals.

(a) Finance receivables by credit risk concentration

\$000's	Corporate	Residential	All Other	Total
June 2022				
Neither at least 90 days past due nor impaired	2,377,755	1,006,977	1,041,728	4,426,460
At least 90 days past due	15,276	131	25,872	41,279
Individually impaired	65,970	-	213	66,183
Gross finance receivables	2,459,001	1,007,108	1,067,813	4,533,922
Provision for impairment	(40,196)	(115)	(10,116)	(50,427)
Total net finance receivables	2,418,805	1,006,993	1,057,697	4,483,495
June 2021				
Neither at least 90 days past due nor impaired	2,054,020	663,891	1,073,490	3,791,401
At least 90 days past due	13,854	139	22,609	36,602
Individually impaired	37,561	9	573	38,143
Gross finance receivables	2,105,435	664,039	1,096,672	3,866,146
Provision for impairment	(30,277)	(88)	(20,683)	(51,048)
Total net finance receivables	2,075,158	663,951	1,075,989	3,815,098

(b) Past due but not impaired

\$000's	Corporate	Residential	All Other	Total
June 2022				
Less than 30 days past due	4,147	171	3,249	7,567
At least 30 but less than 60 days past due	15,320	263	10,751	26,334
At least 60 but less than 90 days past due	4,621	85	5,071	9,777
At least 90 days past due	15,276	131	25,872	41,279
Total past due but not impaired	39,364	650	44,943	84,957
June 2021				
Less than 30 days past due	6,882	357	8,330	15,569
At least 30 but less than 60 days past due	11,950	-	7,829	19,779
At least 60 but less than 90 days past due	4,429	-	3,798	8,227
At least 90 days past due	13,854	139	22,609	36,602
Total past due but not impaired	37,115	496	42,566	80,177

22 Asset quality (continued)

(c) Individually impaired assets

\$000's	Corporate	Residential	All Other	Total
June 2022				
Opening	37,561	9	573	38,143
Additions	58,396	-	-	58,396
Deletions	(26,577)	(9)	(360)	(26,946)
Write offs	(3,410)	-	-	(3,410)
Closing gross individually impaired assets	65,970	-	213	66,183
Less: provision for individually impaired assets	15,001	-	-	15,001
Total net individually impaired assets	50,969	-	213	51,182
June 2021				
Opening	22,774	9	1,884	24,667
Additions	23,454	-	-	23,454
Deletions	-	-	(466)	(466)
Write offs	(8,667)	-	(845)	(9,512)
Closing gross individually impaired assets	37,561	9	573	38,143
Less: provision for individually impaired assets	7,629	-	-	7,629
Total net individually impaired assets	29,932	9	573	30,514

(d) Credit risk grading

The Banking Group's finance receivables are monitored either by account behaviour (**Behavioural portfolio**) or a regular assessment of their credit risk grade based on an objective review of defined risk characteristics (**Judgemental portfolio**).

Finance receivables - reverse mortgages have no arrears characteristics and are assessed on origination against a pre-determined criteria.

The Judgemental portfolio consists mainly of business and rural lending where an on-going and detailed working relationship with the customer has been developed while the Behavioural portfolio consists of consumer, retail and smaller business receivables.

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 where grade 1 is the strongest risk. Grade 8 and grade 9 are the weakest risk grades where a loss is probable. Behavioural loans are managed based on their arrears status.

22 Asset quality (continued)

(d) Credit risk grading (continued)

All loans past due but not impaired have been categorised into three impairments stages (refer Note 8) which are in most cases based on arrears status. If a Judgemental loan is risk graded 6 or above it will be classified as stage 2 as a minimum and carry a provision based on lifetime expected credit losses.

\$000's	Lifetime ECL		Lifetime ECL Credit Impaired	Specifically Provided	Fair value	Total
	12 Months ECL	Not Credit Impaired				
June 2022						
Judgemental portfolio						
Grade 1 - Very Strong	26	-	-	-	-	26
Grade 2 - Strong	10,859	-	-	-	-	10,859
Grade 3 - Sound	53,756	-	-	-	-	53,756
Grade 4 - Adequate	697,590	5,382	1,052	-	-	704,024
Grade 5 - Acceptable	994,079	1,823	53	-	-	995,955
Grade 6 - Monitor	-	25,106	2,308	-	-	27,414
Grade 7 - Substandard	-	64,203	4,727	-	-	68,930
Grade 8 - Doubtful	-	-	-	62,672	-	62,672
Grade 9 - At risk of loss	-	-	-	3,511	-	3,511
Total Judgemental portfolio	1,756,310	96,514	8,140	66,183	-	1,927,147
Total Behavioural portfolio	1,827,025	21,001	37,485	-	721,264	2,606,775
Gross finance receivables	3,583,335	117,515	45,625	66,183	721,264	4,533,922
Provision for impairment	(19,201)	(1,863)	(14,362)	(15,001)	-	(50,427)
Total finance receivables	3,564,134	115,652	31,263	51,182	721,264	4,483,495
June 2021						
Judgemental portfolio						
Grade 1 - Very Strong	34	-	-	-	-	34
Grade 2 - Strong	10,854	64	-	-	-	10,918
Grade 3 - Sound	50,816	163	-	-	-	50,979
Grade 4 - Adequate	580,289	4,675	1,734	-	-	586,698
Grade 5 - Acceptable	849,286	5,658	1,882	-	-	856,826
Grade 6 - Monitor	-	58,178	1,038	-	-	59,216
Grade 7 - Substandard	-	71,718	8,107	-	-	79,825
Grade 8 - Doubtful	-	-	-	33,228	-	33,228
Grade 9 - At risk of loss	-	-	-	4,915	-	4,915
Total Judgemental portfolio	1,491,279	140,456	12,761	38,143	-	1,682,639
Total Behavioural portfolio	1,525,293	24,272	32,437	-	601,505	2,183,507
Gross finance receivables	3,016,572	164,728	45,198	38,143	601,505	3,866,146
Provision for impairment	(24,432)	(2,356)	(16,631)	(7,629)	-	(51,048)
Total finance receivables	2,992,140	162,372	28,567	30,514	601,505	3,815,098

22 Asset quality (continued)

(e) Provision for impairment

\$000's	12 Months ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Specific Provision	Total
June 2022					
Corporate					
Impairment allowance as at 30 June 2021	16,586	1,214	4,848	7,629	30,277
Changes in loss allowance					
Transfer between stages	(3,614)	(1,060)	(601)	5,275	-
New and increased provision (net of collective provision releases)	6,381	739	4,164	5,507	16,791
Recovery of amounts written off	-	-	(193)	-	(193)
Credit impairment charge	2,767	(321)	3,370	10,782	16,598
Recovery of amounts previously written off	-	-	193	-	193
Write offs	-	-	(3,462)	(3,410)	(6,872)
Impairment allowance as at 30 June 2022	19,353	893	4,949	15,001	40,196
Residential					
Impairment allowance as at 30 June 2021	88	4	(4)	-	88
Changes in loss allowance					
New and increased provision (net of collective provision releases)	27	-	-	-	27
Recovery of amounts written off	-	-	-	-	-
Credit impairment charge	27	-	-	-	27
Recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	-	-	-
Impairment allowance as at 30 June 2022	115	4	(4)	-	115
All Other					
Impairment allowance as at 30 June 2021	7,758	1,138	11,787	-	20,683
Changes in loss allowance					
Transfer between stages	(192)	(1,440)	1,632	-	-
New and increased provision (net of collective provision releases)	(7,833)	1,268	7,194	-	629
Recovery of amounts written off	-	-	(2,562)	-	(2,562)
Credit impairment charge	(8,025)	(172)	6,264	-	(1,933)
Recovery of amounts previously written off	-	-	2,562	-	2,562
Write offs	-	-	(11,196)	-	(11,196)
Impairment allowance as at 30 June 2022	(267)	966	9,417	-	10,116

22 Asset quality (continued)

(e) Provision for impairment (continued)

\$000's	12 Months ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Specific Provision	Total
June 2022					
Total					
Impairment allowance as at 30 June 2021	24,432	2,356	16,631	7,629	51,048
Changes in loss allowance					
Transfer between stages	(3,806)	(2,500)	1,031	5,275	-
New and increased provision (net of collective provision releases)	(1,425)	2,007	11,358	5,507	17,447
Recovery of amounts written off	-	-	(2,755)	-	(2,755)
Credit impairment charge	(5,231)	(493)	9,634	10,782	14,692
Recovery of amounts previously written off	-	-	2,755	-	2,755
Write offs	-	-	(14,658)	(3,410)	(18,068)
Impairment allowance as at 30 June 2022	19,201	1,863	14,362	15,001	50,427
June 2021					
Corporate					
Impairment allowance as at 30 June 2020	18,782	829	9,702	5,301	34,614
Changes in loss allowance					
Transfer between stages	(2,239)	(422)	(936)	3,597	-
New and increased provision (net of collective provision releases)	93	807	1,364	6,034	8,298
Recovery of amounts written off	-	-	(380)	-	(380)
Credit impairment charge	(2,146)	385	48	9,631	7,918
Recovery of amounts previously written off	-	-	380	-	380
Write offs	-	-	(5,282)	(7,303)	(12,585)
Effect of changes in foreign exchange rate	-	-	-	-	-
Acquisition of portfolio	-	-	-	-	-
Sale of portfolio	(50)	-	-	-	(50)
Impairment allowance as at 30 June 2021	16,586	1,214	4,848	7,629	30,277
Residential					
Impairment allowance as at 30 June 2020	10	1	(4)	-	7
Changes in loss allowance					
Transfer between stages	(1)	1	-	-	-
New and increased provision (net of collective provision releases)	79	2	-	-	81
Recovery of amounts written off	-	-	-	-	-
Credit impairment charge	78	3	-	-	81
Recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	-	-	-
Effect of changes in foreign exchange rate	-	-	-	-	-
Acquisition of portfolio	-	-	-	-	-
Sale of portfolio	-	-	-	-	-
Impairment allowance as at 30 June 2021	88	4	(4)	-	88

22 Asset quality (continued)

Provision for impairment (continued)

\$000's	12 Months ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Specific Provision	Total
June 2021					
All Other					
Impairment allowance as at 30 June 2020	13,628	1,337	13,083	-	28,048
Changes in loss allowance					
Transfer between stages	(230)	(663)	893	-	-
New and increased provision (net of collective provision releases)	(3,707)	502	11,811	-	8,606
Recovery of amounts written off	-	-	(2,026)	-	(2,026)
Credit impairment charge	(3,937)	(161)	10,678	-	6,580
Recovery of amounts previously written off	-	-	2,026	-	2,026
Write offs	-	-	(14,009)	-	(14,009)
Effect of changes in foreign exchange rate	(33)	2	6	-	(25)
Acquisition of portfolio	133	22	188	-	343
Sale of portfolio	(2,033)	(62)	(185)	-	(2,280)
Impairment allowance as at 30 June 2021	7,758	1,138	11,787	-	20,683
Total					
Impairment allowance as at 30 June 2020	32,420	2,167	22,781	5,301	62,669
Changes in loss allowance					
Transfer between stages	(2,470)	(1,084)	(43)	3,597	-
New and increased provision (net of collective provision releases)	(3,535)	1,311	13,175	6,034	16,985
Recovery of amounts written off	-	-	(2,406)	-	(2,406)
Credit impairment charge	(6,005)	227	10,726	9,631	14,579
Recovery of amounts previously written off	-	-	2,406	-	2,406
Write offs	-	-	(19,291)	(7,303)	(26,594)
Effect of changes in foreign exchange rate	(33)	2	6	-	(25)
Acquisition of portfolio	133	22	188	-	343
Sale of portfolio	(2,083)	(62)	(185)	-	(2,330)
Impairment allowance as at 30 June 2021	24,432	2,356	16,631	7,629	51,048

(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 2022, the Banking Group had \$1.0 million assets under administration (2021: \$0.3 million).

23 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 in all banking operations is closely monitored by the Banking Group.

Measurement 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 Asset and Liability Committee. This policy sets out the nature of the risk which may be taken and aggregate risk limits, and the ALCO must observe. Within this, the objective of the ALCO is to derive the most appropriate strategy for the Banking Group in terms of a mix of assets and liabilities given its expectations of future cash flows, liquidity constraints and capital adequacy. The ALCO employs asset and liability cash flow modelling to determine appropriate liquidity and funding strategies.

Reserve Bank of New Zealand facilities

In March 2020, the Bank was onboarded by the Reserve Bank of New Zealand (**RBNZ**) as an approved counterparty and executed a 2011 Global Master Repo Agreement providing an additional source for intra-day liquidity for the Banking Group if required.

From 26 May 2020, the RBNZ made available a Term Lending Facility (**TLF**) to offer loans for a fixed term of three years at the Official Cash Rate, with access to the funds linked to banks' lending under the Business Finance Guarantee Scheme. On 25 May 2021, RBNZ announced to close TLF applications on 28 July 2021.

Additional stimulus provided through a Funding for Lending Programme also commenced in December 2020 designed to enable banks to provide low-cost lending to the customer.

The Banking Group had not utilised any of these facilities as at 30 June 2022.

The Banking Group holds the following liquid assets and committed funding sources for the purpose of managing liquidity risk:

\$000's	June 2022	June 2021
Cash and cash equivalents	221,469	112,903
Investments	274,211	357,157
Undrawn committed bank facilities	132,221	191,850
Total liquidity	627,901	661,910

23 Liquidity risk (continued)

Contractual liquidity profile of financial liabilities

The following tables present the Banking Group's financial 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 consolidated statement of financial position.

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. These accounts provide a stable source of long term funding for the Banking Group.

\$000's	On Demand	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
June 2022							
Non - derivative financial liabilities							
Retail Deposits	892,612	2,028,225	561,468	103,192	41,655	-	3,627,152
Other borrowings	-	368,926	7,251	397,859	-	-	774,036
Due to related parties	-	1,535	-	-	-	-	1,535
Lease liabilities	-	1,282	1,292	2,615	6,985	4,911	17,085
Other financial liabilities	-	47,510	-	-	-	-	47,510
Total non - derivative financial liabilities	892,612	2,447,478	570,011	503,666	48,640	4,911	4,467,318
Derivative financial liabilities							
Inflows from derivatives	-	5,007	1,759	3,505	813	-	11,084
Outflows from derivatives	-	3,893	3,227	6,621	839	-	14,580
Total derivative financial liabilities	-	(1,114)	1,468	3,116	26	-	3,496
Undrawn facilities available to customers	272,735	-	-	-	-	-	272,735
Undrawn committed bank facilities	132,221	-	-	-	-	-	132,221
June 2021							
Non - derivative financial liabilities							
Retail Deposits	974,984	1,324,902	560,232	292,091	91,107	-	3,243,316
Other borrowings	-	116,944	6,468	264,639	128,489	-	516,540
Due to related parties	-	3,210	-	-	-	-	3,210
Lease liabilities	-	1,308	1,320	2,663	7,605	7,085	19,981
Other financial liabilities	-	16,663	-	-	-	-	16,663
Total non - derivative financial liabilities	974,984	1,463,027	568,020	559,393	227,201	7,085	3,799,710
Derivative financial liabilities							
Inflows from derivatives	-	14,251	610	800	12	-	15,673
Outflows from derivatives	-	16,750	2,174	1,316	16	-	20,256
Total derivative financial liabilities	-	2,499	1,564	516	4	-	4,583
Undrawn facilities available to customers	208,855	-	-	-	-	-	208,855
Undrawn committed bank facilities	191,850	-	-	-	-	-	191,850

24 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.

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.

The objective of the Banking Group's interest rate risk policies is to limit underlying net profit after tax (**NPAT**) volatility. The measurement comprises net interest income the Banking Group generates from its interest earning assets and interest bearing liabilities.

The exposure to net interest income comes from a reduction in margins on interest earning assets or interest bearing liabilities and is managed when setting rates by taking into consideration wholesale rates, liquidity premiums, as well as appropriate lending credit margins.

An analysis of the Banking Group's sensitivity to an increase (+) or decrease (-) in market interest rates by 100 basis points (**BP**) is as follows. An (+)/(-) to market interest rates of 100 BP would result in a \$0.7 million (+)/(-) to NPAT (2021: \$0.2 million (+)/(-)) with a corresponding impact to equity.

The Banking Group also manages interest rate risk by:

- Monitoring maturity profiles and seeking to match the re-pricing of assets and liabilities;
- Monitoring interest rates daily and regularly (at least monthly) reviewing interest rate exposures; and
- Entering into derivatives to hedge against movements in interest rates.

24 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.

\$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non- Interest Bearing	Total
June 2022							
Financial assets							
Cash and cash equivalents	221,460	-	-	-	-	9	221,469
Investments	1,568	854	51,144	91,974	128,672	1,502	275,714
Finance receivables	1,730,148	178,756	323,766	558,256	910,399	60,906	3,762,231
Finance receivables - reverse mortgages	721,264	-	-	-	-	-	721,264
Due from related parties	-	-	-	-	-	1,540	1,540
Derivative financial assets	-	-	-	-	-	44,487	44,487
Other financial assets	-	-	-	-	-	175	175
Total financial assets	2,674,440	179,610	374,910	650,230	1,039,071	108,619	5,026,880
Financial liabilities							
Deposits	2,194,973	684,378	546,718	99,196	38,325	33,554	3,597,144
Other borrowings	548,488	78,911	-	121,191	-	888	749,478
Derivative financial liabilities	-	-	-	-	-	6,335	6,335
Due to related parties	-	-	-	-	-	1,535	1,535
Lease liabilities	-	-	-	-	-	15,726	15,726
Other financial liabilities	-	-	-	-	-	47,510	47,510
Total financial liabilities	2,743,461	763,289	546,718	220,387	38,325	105,548	4,417,728
Effect of derivatives held for risk management	986,194	(76,349)	(127,004)	(309,781)	(473,060)	-	-
Net financial assets/(liabilities)	917,173	(660,028)	(298,812)	120,062	527,686	3,071	609,152

24 Interest rate risk (continued)

Contractual repricing analysis (continued)

\$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non- Interest Bearing	Total
June 2021							
Financial assets							
Cash and cash equivalents	112,893	-	-	-	-	10	112,903
Investments	31,897	8,034	19,669	53,505	244,052	1,818	358,975
Finance receivables	1,554,461	147,303	291,415	450,415	699,967	70,032	3,213,593
Finance receivables - reverse mortgages	601,505	-	-	-	-	-	601,505
Due from related parties	-	-	-	-	-	146	146
Derivative financial assets	-	-	-	-	-	14,111	14,111
Other financial assets	-	-	-	-	-	1,068	1,068
Total financial assets	2,300,756	155,337	311,084	503,920	944,019	87,185	4,302,301
Financial liabilities							
Deposits	1,706,735	570,068	554,340	285,025	85,077	18,277	3,219,522
Other borrowings	170,364	50,837	-	153,751	127,933	-	502,885
Derivative financial liabilities	-	-	-	-	-	4,789	4,789
Due to related parties	-	-	-	-	-	3,210	3,210
Lease liabilities	-	-	-	-	-	17,780	17,780
Other financial liabilities	-	-	-	-	-	16,663	16,663
Total financial liabilities	1,877,099	620,905	554,340	438,776	213,010	60,719	3,764,849
Effect of derivatives held for risk management	474,010	(9,023)	(146,067)	(85,670)	(233,250)	-	-
Net financial assets/(liabilities)	897,667	(474,591)	(389,323)	(20,526)	497,759	26,466	537,452

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

25 Concentrations of funding

(a) Regulatory liquidity ratios

RBNZ requires banks to hold minimum amounts of liquid assets to help ensure that they are effectively managing their liquidity risks. The mismatch ratio is a measure of a bank's liquid assets, adjusted for contractual cash inflows and outflows during a 1-month or 1-week period of stress. It is expressed as a ratio over the bank's total funding. The Banking Group must maintain its 1-month and 1-week mismatch ratios above zero on a daily basis. The below 1-month and 1-week mismatch ratios are averaged over the quarter.

RBNZ requires banks to get a minimum amount of funding from stable sources called core funding. RBNZ requires banks to get a minimum amount of funding from stable sources called core funding. From 1 January 2022, the minimum amount of core funding was increased from 50% to 75% of a bank's total loans. The Banking Group must maintain its core funding ratio above the regulatory minimum on a daily basis. The below measure of the core funding ratio is averaged over the quarter.

	Average for the 3 Months Ended 30 June 2022	Average for the 3 Months Ended 31 March 2022
One-week mismatch ratio	6.05	6.81
One-month mismatch ratio	6.24	7.30
Core funding ratio	89.06	90.45

25 Concentrations of funding (continued)

(b) Concentration of funding by industry

The Australian and New Zealand Standard Industrial Classification codes have been used as the basis for categorising customer and investee industry sectors.

\$000's	June 2022	June 2021
Agriculture	113,848	102,107
Forestry and fishing	14,391	14,226
Mining	1,524	94
Manufacturing	18,643	11,592
Finance and insurance	960,175	769,757
Wholesale trade	5,854	11,218
Retail trade and accommodation	19,491	28,521
Households	2,754,452	2,322,514
Rental, hiring and real estate services	43,797	46,245
Construction	28,449	24,231
Other business services	66,731	58,334
Transport and storage	4,598	4,337
Other	41,686	44,714
Total	4,073,639	3,437,890
Unsubordinated Notes	272,983	284,517
Total borrowings	4,346,622	3,722,407

(c) Concentration of funding by geographical area

\$000's	June 2022	June 2021
New Zealand	4,241,026	3,635,405
Overseas	105,596	87,002
Total borrowings	4,346,622	3,722,407

Other Disclosures

26 Significant subsidiaries

Significant Subsidiaries	Country of Incorporation and Place of business	Nature of business	Proportion of ownership and voting power held	
			June 2022	June 2021
VPS Properties Limited	New Zealand	Investment property holding company	100%	100%
Marac Insurance Limited	New Zealand	Insurance services	100%	100%

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

\$000's	June 2022	June 2021
Deposits	149,824	153,244

(b) Heartland Auto Receivable Warehouse Trust 2018-1 (Auto Warehouse)

The Auto Warehouse securitises motor loan receivables as a source of funding.

The Banking Group continues to recognise the securitised assets and associated borrowings in the consolidated statement of financial position as the Banking Group remains exposed to and has the ability to affect variable returns from those assets and liabilities. Although the Banking Group recognises those interests in Auto Warehouse, the loans sold to the Trust are set aside for the benefit of investors in Auto Warehouse and other depositors and lenders to the Banking Group have no recourse to those assets.

\$000's	June 2022	June 2021
Cash and cash equivalents	20,197	9,047
Finance receivables	312,239	126,399
Other borrowings	(315,308)	(128,125)

28 Capital adequacy

The Banking Group is subject to regulation by the Reserve Bank of New Zealand. 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 Banking Prudential Requirements documents (**BPRs**).

The Banking Group has adopted the Basel II standardised approach per RBNZ BPRs 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 CET1 Capital, Additional Tier 1 (**AT1**) Capital and Total Capital as a percentage of risk-weighted-assets (**RWAs**).
- 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 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 affected 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 2022.

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**)" Part D of the Banking Prudential Requirements (**BPR**) documents: BPR100 and is in accordance with its Conditions of Registration.

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.

28 Capital adequacy (continued)

Internal Capital Adequacy Assessment Process (ICAAP) (continued)

Compliance with minimum capital levels is monitored by the ALCO and reported to the Board. The ICAAP and CMP is reviewed annually by the Board.

RBNZ capital review

The RBNZ released a consultation paper in December 2018 in relation to proposed changes to the Capital Adequacy Framework for Registered Banks in New Zealand (the **Framework**). On 5 December 2019, the RBNZ released its final decision on the revised Framework.

The revised Framework requires the Bank, as a standardised registered bank, to increase its Total Capital ratio to 16% over a seven-year transitional period, being from 1 July 2021. The Bank's Total Capital ratio is 13.39% as at 30 June 2022. This means the revised Framework requires the Bank to increase its Total Capital ratio by 2.61% over the transitional period.

The Bank does not expect the revised Framework to result in any changes to the underlying business model or its approach to raising equity, given:

- The quantum of the capital requirement;
- That some of the capital requirement may be satisfied through hybrid capital instruments rather than common equity;
- The length of the transitional period;
- The Bank's existing capital position.

The corporate structure of HGH, the ultimate parent company provides the Banking Group with flexibility to mitigate the impact of the revised Framework. Various capital raising options available include using HGH's dividend reinvestment plan, or raise debt and use the proceeds to subscribe for new capital in the Bank.

The Bank will continue to assess the options available to it to meet the requirements of the revised Framework over the transitional period.

28 Capital adequacy (continued)

(a) Capital

\$000's	June 2022
Tier 1 Capital	
CET1 capital	
Paid-up ordinary shares issued by the Banking Group plus related share premium	553,239
Retained earnings (net of appropriations)	147,852
Accumulated other comprehensive income and other disclosed reserves	6,412
Less deductions from CET1 capital	
Intangible assets	(58,433)
Deferred tax assets	(15,538)
Hedging reserve	(7,446)
Total CET1 capital	626,086
AT1 capital	-
Total Tier 1 capital	626,086
Tier 2 capital	-
Total Tier 2 capital	-
Total capital	626,086

(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 BPR110, 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.

Reserves classified as CET1 capital

Fair value reserve	The debt instrument fair value reserve comprises the changes in the fair value of investments, net of tax.
Cash flow hedge reserve	The hedging reserve comprises the fair value gains and losses associated with the effective portion of designated cash flow hedging instruments.

28 Capital adequacy (continued)

(c) Credit risk

On balance sheet exposures

	Total Exposure After Credit Risk Mitigation \$000's	Average Risk Weight %	Risk Weighted Exposure \$000's	Minimum Pillar 1 Capital Requirement \$000's
June 2022				
Cash	-	0%	-	-
Sovereigns and central banks	1,506	0%	-	-
Multilateral development banks	119,079	0%	-	-
Multilateral development banks	91,425	20%	18,285	1,463
Banks - Short term - Tier 1	-	20%	-	-
Banks - Short term - Tier 2	221,819	20%	44,364	3,549
Banks - Short term - Tier 3	-	20%	-	-
Banks - Long term - Tier 1	-	20%	-	-
Banks - Long term - Tier 2	50,405	50%	25,202	2,016
Banks - Long term - Tier 3	35	50%	18	1
Public sector entity (AA- and above)	12,953	20%	2,591	207
Public sector entity (A- and above)	-	50%	-	-
Public sector entity (BBB+, BBB, BBB-)	-	100%	-	-
Corporates (AA- and above)	-	20%	-	-
Corporates (A- and above)	-	50%	-	-
Corporates (BBB- and above)	-	100%	-	-
Corporate Exposures - BFGS	54,892	20%	10,978	878
Corporate Exposures- unrated	1,993,591	100%	1,993,591	159,487
Welcome Home Loans - loan to value ratio (LVR) <= 80% ¹	1,591	35%	557	45
Welcome Home Loans - loan to value ratio (LVR) <= 90% ¹	-	35%	-	-
Welcome Home Loans - LVR 90% >= 100% ¹	-	50%	-	-
Welcome Home Loans - LVR > 100% ¹	-	100%	-	-
Reverse Residential mortgages <= 60% LVR	718,022	50%	359,011	28,721
Reverse Residential mortgages 60 <= 80% LVR	3,045	80%	2,436	195
Reverse Residential mortgages > 80% LVR	197	100%	197	16
Reverse Residential mortgages > 100% LVR	-	100%	-	-
Non Property Investment Mortgage Loan <=80% LVR	281,118	35%	98,391	7,871
Non Property Investment Mortgage Loan 80 <= 90% LVR	-	50%	-	-
Non Property Investment Mortgage Loan 90 <= 100% LVR	543	75%	408	33
Non Property Investment Mortgage Loan > 100% LVR	-	100%	-	-
Property Investment Mortgage Loan <= 80% LVR	2,345	40%	938	75
Property Investment Mortgage Loan 80 <= 90% LVR	-	70%	-	-
Property Investment Mortgage Loan 90 <= 100% LVR	-	90%	-	-
Property Investment Mortgage Loan < 100% LVR	-	100%	-	-
Past due residential mortgages	131	100%	131	10
Other past due assets - provision >= 20%	37,144	100%	37,144	2,972
Other past due assets - provision < 20%	41,816	150%	62,724	5,018
Equity holdings	-	300%	-	-
All other equity holdings	1,488	400%	5,950	476
Fixed Assets	6,960	100%	6,960	557
Leased Assets	13,660	100%	13,660	1,093
Other assets	1,382,907	100%	1,382,907	110,633
Not risk weighted assets	73,971	0%	-	-
Total on balance sheet exposures	5,110,643		4,066,443	325,316

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

28 Capital adequacy (continued)

(c) Credit risk (continued)

Off balance sheet exposures

	Total Exposure \$000's	Credit Conversion Factor %	Credit Equivalent Amount \$000's	Average Risk Weight %	Risk Weighted Exposure \$000's	Minimum Pillar 1 Capital Requirement \$000's
June 2022						
Direct credit substitute	4,010	100%	4,010	100%	4,010	321
Performance-related contingency	4,959	50%	2,480	100%	2,480	198
Other commitments where original maturity is more than one year	198,367	50%	99,184	100%	99,184	7,935
Other commitments where original maturity is more than one year	22,480	50%	11,240	35%	3,934	315
Other commitments where original maturity is less than or equal to one year	48,865	20%	9,773	100%	9,773	782
Other commitments where original maturity is less than or equal to one year	36,116	20%	7,223	50%	3,612	289
Other commitments where original maturity is less than or equal to one year	1,698	20%	340	35%	119	10
Market related contracts¹						
Interest rate contracts	1,478,151	N/A	45,019	32%	14,616	1,169
FX forward contracts	-	N/A	-	0%	-	-
Credit valuation adjustment	-	-	-	-	12,951	1,036
Total off balance sheet exposures	1,794,646		179,269		150,679	12,055

¹ The credit equivalent amount for market related contracts was calculated using the current exposure method.

(d) Additional mortgage information – LVR range

\$000's	On Balance Sheet Exposures	Off Balance Sheet Exposures ²	Total Exposures
June 2022			
Does not exceed 80%	1,006,121	60,295	1,066,416
Exceeds 80% and not 90%	197	-	197
Exceeds 90%	675	-	675
Total exposures	1,006,993	60,295	1,067,288

² Off balance sheet exposures means unutilised limits.

At 30 June 2022, there were no Welcome Home loans whose credit risk is mitigated by the Crown included in "Exceeds 90% residential mortgages". Other loans in the exceeds 90% LVR range is 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 the first mortgages over residential property is included in the LVR calculation, in accordance with BPR131. All new residential mortgages in respect of non-property investments lending have a loan-to-valuation ratio of less than or equal to 80%.

28 Capital adequacy (continued)

(e) Reconciliation of mortgage related amounts

\$000's	Note	June 2022
Gross finance receivables - reverse mortgages	12b	721,264
Loans and advances - loans with residential mortgages		285,844
On balance sheet residential mortgage exposures subject to the standardised approach	22a	1,007,108
Less: collective provision for impairment		(115)
Off balance sheet mortgage exposures subject to the standardised approach	28d	60,295
Total residential exposures subject to the standardised approach		1,067,288

(f) Credit risk mitigation

As at 30 June 2022 the Banking Group had \$1.6 million of Welcome Home Loans (2021: \$1.8 million), 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

\$000's	Implied Risk Weighted Exposure	Total Operational Risk Capital Requirement
June 2022		
Operational risk	279,018	22,321

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 rates 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.

\$000's		Implied Risk Weighted Exposure	Aggregate Capital Charge
June 2022			
Market risk end-of-period capital charge	Equity rate risk only	1,488	119
Market risk peak end-of-day capital charge	Equity rate risk only	1,488	119
Market risk end-of-period capital charge	Interest rate risk only	144,627	11,570
Market risk peak end-of-day capital charge	Interest rate risk only	150,608	12,049
Market risk end-of-period capital charge	Foreign currency risk only	69	5
Market risk peak end-of-day capital charge	Foreign currency risk only	165	13

The Banking Group's aggregate market exposure is derived in accordance with BPR140. Peak end-of-day capital charge disclosure is derived by taking the highest month end market exposure over the six months ended 30 June 2022. Interest rate risk, foreign exchange risk and equity risk are calculated monthly using the month end position. While the Banking Group views this methodology as being materially correct, it is currently investigating the impact a daily aggregate market risk exposure would have for future reporting periods.

28 Capital adequacy (continued)

(i) Total capital requirement

\$000's	Total Exposure After Credit Risk Mitigation	Risk Weighted Exposure or Implied Risk Weighted Exposure	Total Capital Requirement
June 2022			
Total credit risk			
On balance sheet	5,110,643	4,066,443	325,316
Off balance sheet	1,794,647	150,679	12,055
Operational risk	n/a	279,018	22,321
Market risk	n/a	146,184	11,694
Total	6,905,290	4,642,324	371,386

(j) Capital ratios

%	June 2022	June 2021
Capital ratios compared to minimum ratio requirements		
Common Equity Tier 1 Capital expressed as a percentage of total risk weighted exposures	13.49%	13.88%
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	13.49%	13.88%
Minimum Tier 1 Capital as per Conditions of Registration	6.00%	6.00%
Total Capital expressed as a percentage of total risk weighted exposures	13.49%	13.88%
Minimum Total Capital as per Conditions of Registration	8.00%	8.00%
Prudential capital buffer ratio		
Prudential capital buffer ratio	5.49%	5.88%
Buffer trigger ratio	2.50%	2.50%

(k) Solo capital adequacy

%	June 2022	June 2021
Capital ratios compared to minimum ratio requirements		
Common Equity Tier 1 Capital expressed as a percentage of total risk weighted exposures	14.37%	14.24%
Tier 1 Capital expressed as a percentage of total risk weighted exposures	14.37%	14.24%
Total Capital expressed as a percentage of total risk weighted exposures	14.37%	14.24%

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.

(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, regulatory and additional credit risk). As at 30 June 2022, the Banking Group has made an internal capital allocation of \$8.4 million to cover these risks (2021: \$8.9 million).

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

Insurance business

Marac Insurance Limited (**MIL**), a subsidiary of HBL, no longer conducts insurance business as HBL entered into a distribution agreement with DPL Insurance Limited (**DPL**) to distribute DPL's insurance products through HBL's network. MIL ceased writing insurance policies in 2020 with the periodic policies expected to expire in 2025.

The Banking Group's aggregate amount of insurance business comprises the total consolidated assets of MIL of \$7.4 million (2021: \$8.5 million), which represents 0.14% of the total consolidated assets of the Banking Group (2021: 0.19%).

Marketing and distribution of the insurance products

Pre February 2020's distribution agreement with DPL, the Banking Group marketed and distributed term life insurance and general insurance covering risks such as redundancy, bankruptcy or suspension of employment. The insurance products were either underwritten by MIL, a subsidiary of the Banking Group or sold by MIL on behalf of other parties who underwrite those products themselves.

Securitisation

As at 30 June 2022, the Banking Group had \$312.24 million securitised assets (2021: \$126.40 million).

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 27 - 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 20 - 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.

29 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 (2021: nil).

The Bank provided the following funding in relation to securitisation entities.

	Total Trusts	
	June 2022	June 2021
Peak end-of-day aggregate amount of funding provided (\$000's)	305,038	110,000
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 (%)	49.0%	19.1%

For this purpose, peak ratio information was derived by determining the maximum end-of-day aggregate amount of funding over the financial year 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.

	Auto Warehouse	
	June 2022	June 2021
Peak end-of-day aggregate amount of funding provided (\$000's)	305,038	110,000
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	93.5%	86.5%

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.

30 Contingent liabilities and commitments

The Banking Group in the ordinary course of business will be subject to claims and proceedings against it whereby the validity of the claim will only be confirmed by uncertain future events. In such circumstances the contingent liabilities are possible obligations, or present obligations if known, 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 on a case by case basis.

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

\$000's	June 2022	June 2021
Letters of credit, guarantee commitments and performance bonds	8,969	13,484
Total contingent liabilities	8,969	13,484
Undrawn facilities available to customers	272,735	208,855
Conditional commitments to fund at future dates	34,791	19,083
Total commitments	307,526	227,939

31 Events after reporting date

The Bank resolved to pay a cash dividend to its parent company HGH of \$30 million on its ordinary shares on 22 August 2022.

There were no other events subsequent to the reporting period which would materially affect the consolidated financial statements.

Historical Summary of Financial Statements

For the year ended 30 June 2022

\$000's	Audited June 2022	Audited June 2021	Audited June 2020	Audited June 2019	Audited June 2018
Interest income	275,770	272,562	297,512	284,064	272,323
Interest expense	66,205	73,753	108,476	111,665	108,737
Net interest income	209,565	198,809	189,036	172,399	163,586
Other net income	33,704	15,006	15,742	9,409	12,683
Net operating income	243,269	213,815	204,778	181,808	176,269
Operating expenses	96,203	100,852	90,782	76,298	76,291
Profit before impaired asset expense and income tax	147,066	112,963	113,996	105,510	99,978
Fair value (loss)/gain on investments	(315)	215	-	1,936	-
Impaired asset expense	14,692	14,579	29,372	20,554	21,833
Profit before income tax	132,059	98,599	84,624	86,892	78,145
Profit before income tax from discontinued operations	-	-	-	6,169	16,149
Income tax expense	36,068	27,090	23,924	24,762	26,781
Profit for the year	95,991	71,509	60,700	68,299	67,513
Other comprehensive income					
Items that are or may be reclassified subsequently to profit or loss, net of income tax:					
Effective portion of change in fair value of derivative financial instruments	6,540	8,928	(2,179)	(4,762)	72
Movement in fair value reserve	(712)	(5,646)	766	2,968	981
Movement in foreign currency translation reserve	-	-	-	(4,229)	2,315
Items that will not be reclassified to profit or loss, net of income tax:					
Movement in defined benefit reserve	(171)	-	-	(86)	340
Other comprehensive income	(473)	-	-	-	-
Other comprehensive income / (loss) for the year, net of income tax	5,184	3,282	(1,413)	(6,109)	3,708
Total comprehensive income for the year	101,175	74,791	59,287	62,190	71,221
Dividends paid to equity holders	35,500	30,000	65,000	112,042	47,895

As at 30 June 2022

\$000's	Audited June 2022	Audited June 2021	Audited June 2020	Audited June 2019	Audited June 2018
Total assets	5,154,652	4,419,488	4,314,559	4,143,828	4,496,849
Individually impaired assets	66,183	38,143	24,667	26,412	45,186
Total liabilities	4,447,149	3,777,660	3,717,522	3,540,438	3,832,689
Total equity	707,503	641,828	597,037	603,390	664,160

Amendments to Conditions of Registration

Changes in Conditions of Registration

With effect from 1 July 2021:

- the bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued on or after 1 July 2021 in the calculation of its capital ratios unless it has completed the notification requirements.
- A Tier 2 capital instrument is an instrument that meets the requirements of subsection B3.2(2)(a) or (c) of Banking Prudential Regulations BPR110: Capital Definitions.

With effect from 1 October 2021:

- Capital instrument translations of the banking capital adequacy requirements were updated from the BS2A documentation to the new Banking Prudential Requirements (BPR) documents.
- The bank's earnings payable to holders of CET1 capital to the percentage limit on distributions that corresponds to the banking group's buffer PCB ratio where revised.

Banking group's PCB ratio	Revised - Banking group's PCB ratio	Percentage limit on distributions of the bank's earnings	Revised - Percentage limit on distributions of the bank's earnings
0% – 0.625%	0% – 0.5%	0%	0%
>0.625 – 1.25%	>0.5 – 1%	20%	30%
>1 – 2%	>1 – 2%	40%	50%
>2 – 2.5%	>2 – 2.5%	50%	50%

The RBNZ further amended the Conditions of Registration on 1 January 2022 to increase the Core Funding Ratio minimum requirement from 50% to 75%.

The RBNZ further amended the Conditions of Registration on 23 June 2022, to make reference to the new versions of the Outsourcing Policy (BS11) and the Open Bank Resolution Policy (BS17), which in turn, incorporate a change in definition of "Business Day".

As at 30 June 2022, there have been no other changes to the Conditions of Registration.

Conditions of Registration

These conditions apply on and after 23 June 2022.

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.

For the purposes of this condition of registration,—

“Total capital ratio”, “Tier 1 capital ratio”, and “Common Equity Tier 1 capital ratio” have the same meaning as in Subpart B2 of BPR100: Capital Adequacy;

“Total capital” has the same meaning as in BPR110: Capital Definitions.

1A. That—

- (a) the bank has an internal capital adequacy assessment process (“ICAAP”) that accords with the requirements set out in Part D of BPR100: Capital Adequacy;
- (b) under its ICAAP the bank identifies and measures its “other material risks” defined in Part D of BPR100: Capital Adequacy; and
- (c) the bank determines an internal capital allocation for each identified and measured “other material risk”.

1B. That, if the Prudential Capital Buffer (PCB) 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, other than discretionary payments payable to holders of Additional Tier 1 capital instruments, to the percentage limit on distributions that corresponds to the banking group’s PCB ratio; and

Banking group’s PCB ratio	Percentage limit on distributions of the bank’s earnings	Capital Buffer Response Framework stage
0% – 0.5%	0%	Stage 3
>0.5 – 1%	30%	Stage 2
>1 – 2%	50%	Stage 1
>2 – 2.5%	50%	None

- (b) comply with the Capital Buffer Response Framework requirements as set out in Part D of BPR120: Capital Adequacy Process Requirements.

For the purposes of this condition of registration,—

“prudential capital buffer ratio”, “distributions”, and “earnings” have the same meaning as in Subpart B2 of BPR100: Capital Adequacy;

an Additional Tier 1 capital instrument is an instrument that meets the requirements of B2.2(2)(a), (c) or (d) of BPR110: Capital Definitions.

1BA. That the bank must not make any distribution on a transitional AT1 capital instrument on or after the date on which on any conversion or write-off provision in the terms and conditions of the instrument is triggered due to either a loss absorption trigger event or a non-viability trigger event.

Conditions of Registration (continued)

For the purposes of this condition of registration, “transitional AT1 capital instrument” has the meaning given in section A2.3 of BPR110: Capital Definitions and “loss absorption trigger event” and “non-viability trigger event” have the meanings given in sub-section C2.2(3) of BPR120: Capital Adequacy Requirements.

- 1C. That, if the prudential capital buffer ratio of the banking group is more than 2.5%, the bank must limit aggregate distributions, other than discretionary payments payable to holders of Additional Tier 1 capital instruments, to no more than 50% of the bank’s earnings.

For the purposes of this condition of registration,—

“prudential capital buffer ratio”, “distributions”, and “earnings” have the same meaning as in Subpart B2 of BPR100: Capital Adequacy;

an Additional Tier 1 capital instrument is an instrument that meets the requirements of B2.2(2)(a), (c) or (d) of BPR110: Capital Definitions;

the bank must not make any individual dividend payment contributing to aggregate distributions for a financial year until it has completed its interim financial accounts for the first six months of its financial year or its annual financial accounts for its full financial year, and must not make any such dividend payment less than six months after any previous such dividend payment.

- 1D. That:

- (a) the bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued on or after 1 July 2021 in the calculation of its capital ratios unless it has completed the notification requirements in Part B of BPR120: Capital Adequacy Process Requirements in respect of the instrument; and
- (b) the bank meets the requirements of Part C of BPR120: Capital Adequacy Process Requirements in respect of regulatory capital instruments.

For the purposes of this condition of registration, —

an Additional Tier 1 capital instrument is an instrument that meets the requirements of subsection B2.2(2)(a) or (c) of BPR110: Capital Definitions;

a Tier 2 capital instrument is an instrument that meets the requirements of subsection B3.2(2)(a) or (c) of BPR110: Capital Definitions.

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

Conditions of Registration (continued)

- (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

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

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 exposure policy” (BS8) dated October 2021.

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:
- the board of the Bank must have at least five directors;
 - the majority of the board members must be non-executive directors;
 - at least half of the board members must be independent directors;
 - an alternate director,—
 - for a non-executive director must be non-executive; and
 - for an independent director must be independent;
 - at least half of the independent directors of the Bank must be ordinarily resident in New Zealand;
 - the chairperson of the board of the Bank must be independent; and
 - 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,”—

- 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
- in relation to a person who is the chairperson of the board of the Bank, means a person who—
 - meets the criteria for independence set out in section 10 except for those in paragraph 10(1)(a) in BS14; and
 - 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:

Conditions of Registration (continued)

“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 October 2018.

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 June 2022.

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 June 2022.

19. That, for a loan-to-valuation measurement period ending on or after 31 October 2021, 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 60%, 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 ending on or before 31 March 2022, 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 20% 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, for a loan-to-valuation measurement period ending on or after 30 April 2022, 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 10% 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.
22. 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 these conditions of registration, the version dates of the Reserve Bank of New Zealand Banking Prudential Requirement (BPR) documents that are referred to in the capital adequacy conditions 1 to 1D, or are referred to in turn by those documents or by Banking Supervision Handbook (BS) documents, are—

BPR document	Version date
BPR100: Capital adequacy	1 October 2021
BPR110: Capital definitions	1 October 2021
BPR120: Capital adequacy process requirements	1 July 2021
BPR130: Credit risk RWAs overview	1 July 2021
BPR131: Standardised credit risk RWAs	1 October 2021
BPR132: Credit risk mitigation	1 October 2021
BPR133: IRB credit risk RWAs	1 October 2021
BPR134: IRB minimum system requirements	1 July 2021
BPR140: Market risk exposure	1 October 2021
BPR150: Standardised operational risk	1 July 2021
BPR151: AMA operational risk	1 July 2021
BPR160: Insurance, securitisation, and loan transfers	1 July 2021
BPR001: Glossary	1 July 2021

Conditions of Registration (continued)

In conditions of registration 19 to 22,—

“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 October 2021:

“loan-to-valuation measurement period” means a period of six calendar months ending on the last day of the sixth calendar month.

Conditions of Registration – Non Compliance

Conditions of Registration Non-Compliance

The Bank has complied with the conditions of registrations since its last disclosure statement.

Conditions of Registration Non-Compliance Prior Period

In July 2021 the Bank was made aware of the RBNZ’s Liquidity Thematic review quantitative findings. These identified four issues where the Bank’s calculation of its liquidity ratios was not in compliance with its Condition of Registration 11 (COR 11).

All non-compliance issues identified have now been remedied, and the ratios when recalculated remained at all times within the Bank’s Conditions of Registration.

Pending Proceedings

There are no pending legal proceedings or arbitrations concerning any member of the Banking Group at the date of 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 7 April 2022.

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 already 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.



Independent Auditor's Report

To the shareholder of Heartland Bank Limited

Report on the audit of the consolidated disclosure statement

Opinion

In our opinion, the accompanying consolidated 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 7 to 72:

- i. give a true and fair view of the Banking Group's financial position as at 30 June 2022 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 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 consolidated financial statements and supplementary information (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements) which comprise:

- the consolidated statement of financial position as at 30 June 2022;
- the consolidated 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) ("ISA's (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 Banking Group in accordance with Professional and Ethical Standard 1 International Code of Ethics for Assurance Practitioners (Including International Independence Standards) (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards) (the "IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our responsibilities under ISA (NZ) are further described in the auditor's responsibilities for the audit of the consolidated 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 Banking Group in relation to the review of the Banking Group's half year disclosure statement, regulatory assurance services and supervisor reporting. Subject to certain restrictions, partners and employees of our firm may also deal with the Banking Group on normal terms within the ordinary course of trading activities of the business of the Banking Group. These matters have not impaired our independence as auditor of the 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 consolidated financial statements as a whole. The materiality for the consolidated financial statements as a whole was set at \$5,800,000 determined with reference to a benchmark of the Banking Group's profit before tax. We chose the benchmark because, in our view, this is a key measure of the Banking Group's performance.

We agreed with the Board Audit Committee that we would report to them, misstatements identified during our audit above \$290,000 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 consolidated disclosure statement in the current period. We summarise below those matters and our key audit procedures to address those matters in order that the shareholder as a body 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 consolidated disclosure statement as a whole and we do not express discrete opinions on separate elements of the consolidated disclosure statement.

The key audit matter

How the matter was addressed in our audit

Provision for impairment of finance receivables

Refer to notes 1, 12 and 22 to the consolidated disclosure statement.

The provision for impairment of finance receivables is a key audit matter due to the financial significance and the inherent complexity of the Banking Group's

Our procedures, amongst others, included:

- Assessing the Banking Group's governance and oversight, including the continuous reassessment of overall provisioning;
- Assessing the Banking Group's significant accounting policies and expected credit loss ("ECL") modelling methodology against the requirements of the standards and underlying accounting records;



The key audit matter

How the matter was addressed in our audit

expected credit loss ("ECL") models.

Significant judgement and estimates are required to incorporate forward-looking information to reflect future economic conditions.

The collective provision is estimated through the ECL models using historical data which is adjusted for forward looking information and the assigned risk grade or arrears status. Additionally, management apply judgement in the determination of provision overlays to adjust for 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.

The provision for individually impaired assets is based on the application of management judgement regarding expected future cashflows, which are inherently uncertain.

- Testing key controls including the arrears calculations, customer loan ratings, annual loan reviews, credit risk reviews and data reconciliations between the ECL models and source systems;
- Assessing the model output against actual losses incurred by the Banking Group;
- Challenging the key assumptions, including forward looking economic assumptions, against external information including benchmarking management's estimates to a range of observable industry data and market forecasts;
- Evaluating individual credit assessments for a sample of 'rural' and other 'corporate' loans 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. We challenged assumptions and assessed collateral values by comparing them to valuations performed by independent valuers; and
- Assessing the disclosures in the consolidated disclosure statement against the requirements of NZ IFRS.

From the procedures performed we consider the Banking Group appropriately identified and considered the uncertainties in the provision estimates.

Valuation of finance receivables – reverse mortgages

Refer to note 19 of the consolidated disclosure statement.

The Banking Group's reverse mortgage portfolio is held at fair value.

The fair value calculation is based on the application of management judgement. In assessing the fair value, the Banking Group continuously considers evidence of a relevant active market. In the absence of such a market, in the current period, the Banking Group considered changes since loan origination and expected future cashflows.

The inherent uncertainties include estimated exits, interest rates and security property values.

Our procedures over the fair value loan portfolios, amongst others, included:

- Testing key controls over the accuracy of data impacting the fair value assessment;
- Assessing evidence of a relevant active market or observable inputs; and
- Challenging the key assumptions used by the Banking Group in determining the portfolio's fair value.

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



The key audit matter

How the matter was addressed in our audit

Operation of IT systems and controls

The Banking Group is reliant 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, where relevant, our audit involves an assessment of the design of the Banking Group's internal control environment. 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, and developer and user access.

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 provided by a third party;
- Assessing the effectiveness of the IT control environment, including core banking IT systems, key automated controls and reporting; and
- Evaluating general IT controls relevant to IT system changes and development, IT operations, and developer and user access.

Where we noted design or operating effectiveness matters relating to IT system or application controls relevant to our audit, we performed alternative audit procedures. We also identified and tested mitigating controls in order to respond to the impact on our overall audit approach.

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 Banking Group's consolidated disclosure statement. Other information includes the information required to be included in the consolidated disclosure statement in accordance with schedule 2 of the Order. Our opinion on the consolidated disclosure statement does not cover any other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated disclosure statement our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated disclosure statement 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 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 consolidated 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 consolidated 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 consolidated 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 consolidated 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 consolidated 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 ISA's (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 consolidated financial statements.

A further description of our responsibilities for the audit of these consolidated financial statements is located at the External Reporting Board (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.

Review conclusion on the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements

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 note 25(a) and 28 to the disclosure statement, 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 note 25(a) and 28 of the consolidated disclosure statement for the year ended 30 June 2022. 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. 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 Heartland Bank Limited, 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 in accordance with the requirements of that Schedule and as described in note 25(a) and 28 to the consolidated disclosure statement.



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 Capital Adequacy and Regulatory Liquidity Requirements based on our review. We conducted our review in accordance with NZ SRE 2410 issued by the New Zealand External Reporting Board. As the auditor of Heartland Bank Limited, NZ SRE 2410 requires that we plan and perform the review to obtain limited assurance about whether the supplementary information relating 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 ISA's (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 shareholder as a body. Our work has been undertaken so that we might state to the shareholder 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 shareholder 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 Graeme Edwards.

For and on behalf of

KPMG
Auckland

22 August 2022