Bank of New Zealand

Disclosure Statement

For the year ended 30 September 2016

No. 83

Disclosure Statement

For the year ended 30 September 2016

This Disclosure Statement has been issued by Bank of New Zealand for the year ended 30 September 2016 in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the “Order”).

In this Disclosure Statement, unless the context otherwise requires:

a) “Banking Group” means Bank of New Zealand’s financial reporting group, which consists of Bank of New Zealand, all of its wholly owned entities and other entities consolidated for financial reporting purposes; and

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

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Bank of New Zealand Corporate Information

Address for Service
The name of the Registered Bank is Bank of New Zealand (referred to either by its full name or as the "Bank") and its address for service is Level 4, 80 Queen Street, Auckland 1010, New Zealand.

Nature of Business
The Bank was incorporated on 29 July 1861. The Banking Group provides a broad range of banking and financial products and services to retail, business, agribusiness, corporate and institutional clients.

Voting Securities and Power to Appoint Directors
National Australia Group (NZ) Limited, National Australia Bank Limited and National Equities Limited are the only holders of a direct or indirect qualifying interest in the 3,370,997,499 voting securities of the Bank. National Australia Group (NZ) Limited is the registered and beneficial holder of 3,370,997,499 voting securities and therefore holds 100% of the direct interest in the voting securities. Neither National Australia Bank Limited (the ultimate parent company) nor National Equities Limited (the immediate parent company of National Australia Group (NZ) Limited) is the registered or the beneficial holder of any of the voting securities of the Bank, but each has a relevant interest in all such securities by virtue of National Australia Group (NZ) Limited being related to them in terms of section 237(d) and 12(2) of the Financial Markets Conduct Act 2013 due to the fact that National Equities Limited owns 100% of the voting securities in National Australia Group (NZ) Limited and National Australia Bank Limited owns 100% of the voting securities in National Equities Limited.

The ultimate parent company has the power under the Bank's constitution to appoint any person as Director of the Bank or to remove any person from the office of Director, from time to time, by giving written notice to the Bank. Any appointment of a Director is subject to the Reserve Bank of New Zealand confirming it has no objection to that appointment.

Guarantees
Covered bond guarantee – Certain debt securities ("Covered Bonds") issued by the Bank, or its wholly owned controlled entity, BNZ International Funding Limited, acting through its London Branch ("BNZ-IF"), are guaranteed by CBG Trustee Company Limited, as trustee of the BNZ Covered Bond Trust (the "Covered Bond Guarantor"). The Covered Bond Guarantor has guaranteed the payment of interest and principal under the Covered Bonds pursuant to a guarantee which is secured over a pool of assets. The Covered Bond Guarantor's address for service is Level 9, 34 Shortland Street, Auckland 1010, New Zealand.

The Covered Bond Guarantor is not a member of the Banking Group and has no credit ratings applicable to any senior unsecured obligations payable in New Zealand dollars. The Covered Bonds have been assigned a long term credit rating of Aaa and AAA from Moody's Investors Service Pty Limited and Fitch Australia Pty Limited, respectively.

There are no material conditions applicable to the guarantee other than non-performance. There are no material legislative or regulatory restrictions in New Zealand which subordinate any claims under the guarantee of any creditors of the Bank on the assets of the Covered Bond Guarantor, to other claims on the Covered Bond Guarantor, in a winding up of the Covered Bond Guarantor.

Refer to note 11 for further information.

Other material obligations of the Bank are not guaranteed.

Ultimate Parent Bank
Ultimate Parent Bank and Address for Service
The ultimate parent bank, and ultimate holding company, of Bank of New Zealand is National Australia Bank Limited whose address for service is Level 1, 800 Bourke Street, Docklands, Victoria 3008, Australia.

References in this document to "NAB" are references to National Australia Bank Limited's financial reporting group, which consists of National Australia Bank Limited, all of its wholly owned entities and other entities consolidated for financial reporting purposes.

Legally Enforceable Restrictions that may Materially Inhibit National Australia Bank Limited's Legal Ability to Provide Material Financial Support to Bank of New Zealand
National Australia Bank Limited does not guarantee the obligations of Bank of New Zealand.

Australian Prudential Regulation Authority ("APRA") Prudential Standard APS 222 ("APS 222") restricts associations between an authorised deposit-taking institution ("ADI") (such as National Australia Bank Limited) and its related entities (such as the Bank). Any provision of material financial support to the Bank by National Australia Bank Limited would need to comply with the following pertinent requirements of APS 222:

1. National Australia Bank Limited should not undertake any third-party dealings with the prime purpose of supporting the business of the Bank. National Australia Bank Limited must avoid giving any impression of its support unless there are formal legal arrangements in place providing for such support.
2. National Australia Bank Limited should not hold unlimited exposures to the Bank.
3. National Australia Bank Limited should not enter into cross-default clauses whereby a default by the Bank on an obligation (whether financial or otherwise) is deemed to trigger a default of National Australia Bank Limited in its obligations.
4. In determining limits on acceptable levels of exposure to the Bank, the Board of Directors of National Australia Bank Limited should have regard to the level of exposures which would be approved for unrelated entities of broadly equivalent credit status, and the impact on National Australia Bank Limited's stand-alone capital and liquidity positions, as well as its ability to continue operating, in the event of a failure of any related entity to which National Australia Bank Limited is exposed.
5. National Australia Bank Limited's exposure to related entities that are overseas based ADIs, such as the Bank, cannot exceed 50% of National Australia Bank Limited's stand-alone capital base, and its aggregate exposure to all related authorised deposit-taking institutions cannot exceed 150% of that capital base. Exposures in excess of these limits require the prior approval of APRA.

Bank of New Zealand Corporate Information

Ultimate Parent Bank *continued*
In late 2014, APRA initiated a process to reduce Australian bank non-equity exposures to their respective New Zealand banking subsidiaries (which, in the case of National Australia Bank Limited, includes the Bank) and branches, so that these non-equity exposures are minimised during ordinary times. On 19 November 2015, APRA informed National Australia Bank Limited that its Extended Licensed Entity ("ELE") non-equity exposures to New Zealand banking subsidiaries, including the Bank, are to transition to be below a limit of 5% of National Australia Bank Limited's Level One Tier One Capital. The ELE consists of National Australia Bank Limited and any APRA approved subsidiary entities assessed effectively as part of a single "stand-alone" entity for the purposes of measuring capital. APRA has regard to a number of factors when approving subsidiary entities for inclusion in the ELE, including ownership, governance, funding arrangements and regulatory characteristics of the subsidiary. Exposures for the purposes of this limit include all committed, non-intraday, non-equity exposures, including derivatives and off-balance sheet exposures. For the purposes of assessing this exposure, the 5% limit excludes equity investments and holdings of capital instruments in New Zealand banking subsidiaries. As at 30 September 2016, National Australia Bank Limited's non-equity exposures to the Bank are below 5% of National Australia Bank Limited's Level One Tier One Capital.

APRA has also confirmed the terms on which National Australia Bank Limited may provide contingent funding support to a New Zealand banking subsidiary, including the Bank, during times of financial stress. APRA has confirmed that, at this time, only covered bonds meet its criteria for contingent funding arrangements. Such contingent funding support is proposed to be captured within an aggregate exposure limit (including debt, equity and any exposures held through a branch) of 50% of National Australia Bank Limited's Level One Tier One Capital.

Pending Proceedings or Arbitration
The Bank's Directors are of the opinion that there are no pending proceedings or arbitrations concerning any member of the Banking Group, whether in New Zealand or elsewhere, that may have a material adverse effect on the Registered Bank or the Banking Group.

In March 2013, a potential representative action against New Zealand banks was announced in relation to certain fees. Litigation Lending Services (NZ) Limited is funding the action. On 20 August 2014, representative proceedings were filed against the Bank. On 24 September 2014, 30 April 2015, 3 December 2015 and 4 May 2016, these proceedings were stayed. The potential outcome of these proceedings cannot be determined with any certainty at this stage.

On 16 August 2016, a class action complaint was filed in the United States District Court for the Southern District of New York regarding alleged conduct concerning the Bank Bill Swap Reference Rate, which is administered by the Australian Financial Markets Association. The complaint names a number of defendants, including the Bank. At this stage, the Bank has not been served with the complaint and the potential outcome of such proceeding cannot be determined with any certainty.

Other Material Matters
The Bank's Directors are of the opinion that there are no other matters relating to the business or affairs of the Registered Bank or the Banking Group which would, if disclosed in this Disclosure Statement, materially adversely affect the decision of a person to subscribe for debt securities of which the Registered Bank or any member of the Banking Group is the issuer.

During the reporting period, volatility persisted in global financial markets. The Banking Group considers that the volatility in global financial markets is now a normal factor in the operating environment and that the Bank has adequate liquidity, funding and capital to manage through these conditions.

The New Zealand dairy market has come under pressure due to a lower milk solid payout rate. More recent indicators suggest an improvement in the dairy sector; however, it is expected that pressure in this sector will continue for a period of time. This may impact land prices, security valuations and related parts of the New Zealand economy. At this stage, the Bank considers that it is well positioned to manage a period of lower dairy payouts.

Directorate and Auditor
Communications addressed to the Directors and responsible persons, or any of them, may be sent to Level 4, 80 Queen Street, Auckland 1010, New Zealand.

Directors
On 21 December 2015, Bruce Ronald Hassall was appointed as an independent Non-Executive Director of the Bank.

On 30 June 2016, Dr. Susan Carrel Macken and Dr. Andrew John Pearce retired as Directors of the Bank.

On 1 July 2016, Kevin John Kenrick was appointed as an independent Non-Executive Director of the Bank.

On 22 July 2016, Michaela Jane Healey and Gavin Robin Slater resigned as Non-Executive Directors of the Bank.

On 22 July 2016, the Bank announced that Philip Wayne Chronican was to be appointed as a Non-Executive Director of the Bank, effective 3 October 2016.

On 29 November 2016, the Bank announced that Angela Mentis will be appointed as a Non-Executive Director of the Bank, effective 19 December 2016.

Directors' details
The name, occupation, technical or professional qualifications, country of residence, and other directorships of each Director of the Bank as at the date of this Disclosure Statement are as follows:

Non-Executive Director, Chairman
Douglas Alexander McKay, ONZM
Company Director
B.A. (Auckland), A.M.P. (Harvard Business School)
New Zealand

Other Directorships:
Genesis Energy Limited, IAG New Zealand Limited, IAG (NZ) Holdings Limited, National Australia Bank Limited, Ryman Healthcare Limited, Tourism Transport Limited, Wymac Consulting Limited, Chairman of the Eden Park Trust Board.

Directorate and Auditor *continued*

Executive Director

Anthony John Healy
Managing Director and Chief Executive Officer
BSc., Grad Dip (Econ), Grad Dip (Fin)
New Zealand

Other Directorships:
Loyalty New Zealand Limited

Independent Non-Executive Directors

Mai Chen
Company Director
LL.B (Hons.) (Otago), LL.M (Harvard), FNZIM
New Zealand

Other Directorships:
ASIANZ CEO Limited, Chen & Palmer Office Services Limited, Chen Palmer Limited, Chen Palmer New Zealand Public Law Specialists Limited, Chen Palmer NZPLS Limited, Chen Palmer NZ Public Law Specialists Limited, CP New Zealand Public Law Specialists Limited, New Zealand Public Law Specialists Limited, NZPLS Limited, Public Law Toolbox Limited, Superdiverse Women Limited, Superdiversity Centre for Law, Policy and Business Limited.

Prudence Mary Flacks
Company Director
LL.B., LL.M.
New Zealand

Other Directorships:
BBull Family Trust Limited, Chorus Limited, Chorus LTI Trustee Limited, Mercury LTI Limited, Mercury NZ Limited, Planboe Limited.

Bruce Ronald Hassall
Company Director
B.Com., FCA
New Zealand

Other Directorships:
Marivan Holdings Limited, Prolife Foods Limited

Kevin John Kenrick
Company Director
BMS
New Zealand

Other Directorships:
Freeview Television Limited, NZOOM Limited, TVNZ International Limited, TVNZ Investments Limited, Chair of Good George Brewing Advisory Board.

Stephen John Moir
Company Director
New Zealand

Other Directorships:
Ijap Limited, Chair of BNZ Insurance Services Limited and BNZ Life Insurance Limited, Chair of the Advisory Board to BNZ Chair of Business in Asia at Victoria University, member of the board of the Guardians of New Zealand Superannuation.

Non-Executive Director

After 30 September 2016, Philip Wayne Chronican was appointed a Non-Executive Director effective 3 October 2016.

Philip Wayne Chronican
Company Director
B.Com (Hons.), MBA (Dist.), GAICD, SF Fin.
Australia

Other Directorships:
Banking + Finance Oath, Chronican SMSF No 2 Pty Limited, Juvenile Diabetes Research Foundation, Meribel Pty Limited, National Australia Bank Limited, Talloires Pty Limited, Chairman of NSW Treasury Corporation.

Diversity

As at 30 September 2016, the proportions of female Directors on the Board and female members as the Bank's Officers were 29% and 38%, respectively (30 September 2015: 44% and 33%).

For the purpose of this disclosure, the BNZ Executive Team has been treated as Officers.

The Bank has a Diversity Council to lead the BNZ diversity agenda, set strategic priorities and oversee performance related to diversity.

Bank of New Zealand Corporate Information

Directorate and Auditor *continued*

New Zealand Regional Audit Committee

Members of the New Zealand Regional Audit Committee as at the date of this Disclosure Statement were as follows:

Bruce Ronald Hassall (Chair)	Independent Non-Executive Director
Mai Chen	Independent Non-Executive Director
Stephen John Moir	Independent Non-Executive Director

Responsible Persons

Messrs. Douglas Alexander McKay, ONZM, Non-Executive Director, Chairman, and Anthony John Healy, Executive Director, have been authorised in writing to sign this Disclosure Statement in accordance with section 82 of the Reserve Bank of New Zealand Act 1989, on behalf of the other Directors, being:

Mai Chen
Philip Wayne Chronican*
Prudence Mary Flacks
Bruce Ronald Hassall
Kevin John Kenrick
Stephen John Moir

* Director appointment effective 3 October 2016.

Policy for Avoiding and Dealing with Conflicts of Interests

The policy and current practice of the Board of Directors of the Bank for avoiding or dealing with conflicts of interest which may arise from the personal, professional or business interests of the Directors, or any of them, are that, where a Director's judgement could potentially be impaired because a conflict of interest exists between the Director's business and personal affairs and the business affairs of the Bank, then that Director must declare that the conflict of interest exists and leave the meeting for the duration of the Board's discussion and voting on the relevant matter.

The Companies Act 1993 requires each Director to cause to be entered in the interests register and disclose to the Board of the Bank:

- the nature and monetary value of the Director's interest in a transaction or proposed transaction if its monetary value is able to be quantified; or
- the nature and extent of the Director's interest in a transaction or proposed transaction if its monetary value is not able to be quantified.

Directors' Benefits

There is no transaction which any Director or immediate relative or close business associate of any Director has with the Bank or any member of the Banking Group 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 otherwise be reasonably likely to influence materially the exercise of that Director's duties.

Information pertaining to loans to and other transactions with Directors is disclosed in note 30 of this Disclosure Statement.

Auditor

The auditor whose report is referred to in this Disclosure Statement is Ernst & Young. Their address for service is Level 9, Ernst & Young Building, 2 Takutai Square, Britomart, Auckland 1010, New Zealand.

Financial Statements

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Historical Summary of Financial Statements

Dollars in Millions	Consolidated 30/9/16	30/9/15	30/9/14	30/9/13	30/9/12
Income statement					
Interest income	**3,854**	4,247	3,926	3,716	3,693
Interest expense	**2,097**	2,512	2,302	2,151	2,190
Net interest income	**1,757**	1,735	1,624	1,565	1,503
Gains less losses on financial instruments	**106**	322	69	(94)	(233)
Other operating income	**406**	375	443	434	374
Total operating income	**2,269**	2,432	2,136	1,905	1,644
Operating expenses	**889**	865	901	843	794
Total operating profit before impairment losses on credit exposures and income tax expense	**1,380**	1,567	1,235	1,062	850
Impairment losses on credit exposures	**120**	128	74	113	61
Total operating profit before income tax expense	**1,260**	1,439	1,161	949	789
Income tax expense on operating profit	**347**	401	311	254	209
Net profit attributable to shareholders of Bank of New Zealand	**913**	1,038	850	695	580
Dividends					
Ordinary dividend	**500**	345	420	110	25
Perpetual preference dividend	**32**	32	44	55	63
Significant balance sheet items					
Total assets	**92,541**	86,787	79,685	75,310	73,111
Total liabilities	**85,536**	79,745	73,944	69,623	67,834
Ordinary shareholder's equity	**6,805**	6,392	5,091	4,777	4,367
Contributed equity - perpetual preference shareholders	**200**	650	650	910	910
Asset quality					
Individually impaired assets - at amortised cost	**246**	214	263	268	349
Individually impaired assets - at fair value through profit or loss	**7**	1	14	136	110
Impairment losses on credit exposures charged to income statement - at amortised cost	**120**	128	74	113	61
Credit risk adjustments on financial assets charged to income statement - at fair value through profit or loss (including derivatives)	**26**	1	39	4	78

The information presented in the above table has been extracted from audited financial statements that have been prepared in accordance with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS").

Basel III and Basel II regulatory capital ratios

The table below shows the capital adequacy ratios based on the Reserve Bank of New Zealand (“RBNZ”)'s Capital Adequacy Framework (Internal Models Based Approach) ("BS2B") expressed as a percentage of total risk-weighted exposures.

	Consolidated Basel III Unaudited 30/9/16	Basel III Unaudited 30/9/15	Basel III Unaudited 30/9/14	Basel III Unaudited 30/9/13	Basel II Unaudited 30/9/12
Common Equity Tier One capital ratio	**10.21%**	10.70%	9.36%	8.87%	N/A
Tier One capital ratio	**10.54%**	11.69%	10.64%	10.68%	11.26%
Total qualifying capital ratio	**12.04%**	12.67%	12.04%	12.61%	13.29%
Buffer ratio	**4.04%**	4.67%	4.04%	4.37%	N/A

The capital ratios as at 30 September 2016, 30 September 2015, 30 September 2014 and 30 September 2013 have been determined in accordance with the RBNZ’s Basel III capital adequacy framework effective from 1 January 2013. The capital ratios as at 30 September 2012 have been determined in accordance with the RBNZ’s Basel II capital adequacy framework effective prior to 1 January 2013.

Income Statement

For the year ended 30 September 2016

Dollars in Millions	Note	Consolidated 30/9/16	30/9/15
Interest income	2	**3,854**	4,247
Interest expense	2	**2,097**	2,512
Net interest income		**1,757**	1,735
Gains less losses on financial instruments	3	**106**	322
Other operating income	4	**406**	375
Total operating income		**2,269**	2,432
Operating expenses	5	**889**	865
Total operating profit before impairment losses on credit exposures and income tax expense		**1,380**	1,567
Impairment losses on credit exposures	12	**120**	128
Total operating profit before income tax expense		**1,260**	1,439
Income tax expense on operating profit	7	**347**	401
Net profit attributable to shareholders of Bank of New Zealand		**913**	1,038

The accounting policies and other notes form part of, and should be read in conjunction with, these financial statements.

Statement of Comprehensive Income

For the year ended 30 September 2016

Dollars in Millions	Note	Consolidated 30/9/16	30/9/15
Net profit attributable to shareholders of Bank of New Zealand		**913**	1,038
Other comprehensive income/(expense):			
Items that will not be reclassified to profit or loss			
Actuarial gain/(loss) on defined benefit plan	27	**(1)**	(2)
Credit risk adjustments on financial liabilities designated at fair value through profit or loss	27	**19**	125
Tax on items transferred directly to/(from) equity	27	**(5)**	(35)
		13	88
Items that may be reclassified subsequently to profit or loss			
Movement in cash flow hedge reserve	26	**19**	113
		19	113
Total other comprehensive income/(expense)		**32**	201
Total comprehensive income attributable to shareholders of Bank of New Zealand		**945**	1,239

The accounting policies and other notes form part of, and should be read in conjunction with, these financial statements.

Statement of Changes in Equity

For the year ended 30 September 2016

Dollars in Millions	Ordinary Capital	Perpetual Preference Capital	Retained Profits	Asset Revaluation Reserve	Cash Flow Hedge Reserve	Total Share-holders' Equity
			Consolidated (30/9/16)			
Balance at beginning of year	2,351	650	3,945	2	94	7,042
Comprehensive income/(expense)						
Net profit attributable to shareholders of Bank of New Zealand	-	-	913	-	-	913
Total other comprehensive income/(expense)	-	-	13	-	19	32
Total comprehensive income/(expense)	-	-	926	-	19	945
Buyback of shares	-	(450)	-	-	-	(450)
Ordinary dividend	-	-	(500)	-	-	(500)
Perpetual preference dividend	-	-	(32)	-	-	(32)
Balance at end of year	2,351	200	4,339	2	113	7,005
			Consolidated (30/9/15)			
Balance at beginning of year	1,851	650	3,257	2	(19)	5,741
Balance adjusted for adoption of accounting standard	-	-	(61)	-	-	(61)
Comprehensive income/(expense)						
Net profit attributable to shareholders of Bank of New Zealand	-	-	1,038	-	-	1,038
Total other comprehensive income/(expense)	-	-	88	-	113	201
Total comprehensive income/(expense)	-	-	1,126	-	113	1,239
Proceeds from shares issued	500	-	-	-	-	500
Ordinary dividend	-	-	(345)	-	-	(345)
Perpetual preference dividend	-	-	(32)	-	-	(32)
Balance at end of year	2,351	650	3,945	2	94	7,042

The accounting policies and other notes form part of, and should be read in conjunction with, these financial statements.

Balance Sheet

As at 30 September 2016

		Consolidated	
Dollars in Millions	Note	**30/9/16**	30/9/15
Assets			
Cash and liquid assets	8	**1,799**	1,634
Due from central banks and other institutions	9	**2,299**	2,009
Trading securities	10	**4,703**	4,918
Derivative financial instruments	14	**7,319**	7,895
Loans and advances to customers	11	**74,378**	68,216
Amounts due from related entities	30	**934**	1,259
Other assets	18	**549**	369
Deferred tax	17	**179**	153
Property, plant and equipment		**165**	176
Goodwill and other intangible assets		**216**	158
Total assets		**92,541**	86,787
Financed by:			
Liabilities			
Due to central banks and other institutions	19	**1,244**	1,439
Short term debt securities	20	**6,030**	5,027
Trading liabilities		**72**	51
Derivative financial instruments	14	**7,786**	8,310
Deposits from customers	21	**51,481**	46,729
Bonds and notes	22	**16,723**	16,156
Current tax liabilities		**35**	75
Amounts due to related entities	30	**434**	380
Other liabilities	23	**809**	863
Subordinated debt	24	**922**	715
Total liabilities		**85,536**	79,745
Net assets		**7,005**	7,042
Shareholders' equity			
Contributed equity – ordinary shareholder	25	**2,351**	2,351
Reserves	26	**115**	96
Retained profits	27	**4,339**	3,945
Ordinary shareholder's equity		**6,805**	6,392
Contributed equity – perpetual preference shareholders	25	**200**	650
Total shareholders' equity		**7,005**	7,042

The accounting policies and other notes form part of, and should be read in conjunction with, these financial statements.

Cash Flow Statement

For the year ended 30 September 2016

		Consolidated	
Dollars in Millions	Note	30/9/16	30/9/15
Cash flows from operating activities			
Cash was provided from:			
Dividend income		2	3
Interest income		3,877	4,257
Net trading income		-	46
Other income		401	367
Cash was applied to:			
Interest expense		(2,129)	(2,540)
Personnel expenses		(472)	(436)
Net trading income		(163)	-
Other operating expenses		(315)	(346)
Taxes and subvention payments		(417)	(353)
Net cash flows from operating activities before changes in operating assets and liabilities		784	998
Changes in operating assets and liabilities arising from cash flow movements			
Net movement in due from central banks and other institutions (term)*		34	21
Net movement in loans and advances to customers*		(6,351)	(3,623)
Net movement in other assets		(200)	(51)
Net movement in trading securities and trading liabilities*		231	(696)
Net movement in deposits from customers*		4,741	1,345
Net movement in due to central banks and other institutions (term)*		(26)	(91)
Net movement in other liabilities		(66)	36
Net change in operating assets and liabilities		(1,637)	(3,059)
Net cash flows from operating activities		(853)	(2,061)
Cash flows from investing activities			
Cash was provided from:			
Proceeds from sale of available for sale investments**		-	49
Proceeds from sale of property, plant and equipment		2	-
Cash was applied to:			
Acquisition of intangible assets		(101)	(38)
Purchase of property, plant and equipment		(32)	(30)
Net cash flows from investing activities		(131)	(19)
Cash flows from financing activities			
Net movement in bonds and notes*		686	1,531
Net movement in derivative financial instruments*		351	729
Net movement in short term debt securities*		1,001	63
Net movement in related entity funding*		(44)	(342)
Increase in contributed equity - ordinary shares	25	-	500
Decrease in contributed equity - perpetual preference shares	25	(450)	-
Net movement in subordinated debt*	24	207	-
Ordinary dividend	27	(500)	(345)
Perpetual preference dividend	27	(32)	(32)
Net cash flows from financing activities		1,219	2,104
Net movement in cash and cash equivalents		235	24
Cash and cash equivalents at beginning of year		1,292	1,268
Cash and cash equivalents at end of year		1,527	1,292
Cash and cash equivalents at end of year comprised:			
Cash and liquid assets	8	1,799	1,634
Due from central banks and other institutions classified as cash and cash equivalents	9	651	327
Due to central banks and other institutions classified as cash and cash equivalents	19	(758)	(927)
Amounts due from related entities classified as cash and cash equivalents	30	239	593
Amounts due to related entities classified as cash and cash equivalents	30	(404)	(335)
Total cash and cash equivalents		1,527	1,292

* The amounts shown represent the net cash flows for the financial year.
** Available for sale classification under NZ IAS 39 comprised of non-traded equity instruments which were sold in September 2014 and the proceeds were received in October 2014.

Cash Flow Statement

For the year ended 30 September 2016

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Reconciliation of net profit attributable to shareholders of Bank of New Zealand to net cash flows from operating activities		
Net profit attributable to shareholders of Bank of New Zealand	913	1,038
Decrease/(increase) in accrued interest receivable	19	10
Depreciation and amortisation expense	84	78
Impairment losses on credit exposures	120	128
Impairment losses and write offs on non-financial assets	-	8
(Decrease)/increase in provision for tax	(70)	48
Unrealised gains less losses on financial instruments	(269)	(276)
(Decrease)/increase in accrued interest payable	(32)	(28)
Increase/(decrease) in other liabilities	19	(3)
Gain on equity investments	-	(5)
Deduct operating cash flows not included in net profit:		
Net change in operating assets and liabilities	(1,637)	(3,059)
Net cash flows from operating activities	(853)	(2,061)

Netting of cash flows
Certain cash flows (as indicated by * on page 11) are shown net as these cash flows are either received and disbursed on behalf of customers and counterparties and therefore reflect the activities of these parties rather than those of the Bank, or are received and disbursed in transactions where the turnover is quick, the amounts large and the maturities short.

The accounting policies and other notes form part of, and should be read in conjunction with, these financial statements.

Note 1 Principal Accounting Policies

In these financial statements Bank of New Zealand is referred to as the "Bank". The "Banking Group" means Bank of New Zealand, all of its wholly owned entities listed in note 15 and entities consolidated for financial reporting purposes listed in note 16.

The financial statements are general purpose financial reports prepared in accordance with the requirements of the Financial Markets Conduct Act 2013 and the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended).

Basis for preparation

The financial statements have been prepared under the historical cost convention, modified by the application of fair value measurements required or allowed by relevant accounting standards. Accounting policies have been consistently applied to all periods presented, unless otherwise stated, throughout the Banking Group.

Assumptions and estimates

The preparation of the financial statements requires the use of certain critical accounting estimates and assumptions that affect the reported amount of assets, liabilities, revenues and expenses and the disclosed amount of contingent liabilities. It also requires management to exercise judgement in the process of applying accounting policies. The notes to the financial statements include areas involving a higher degree of judgement or complexity, or areas where assumptions are significant to the Banking Group. Refer to notes 6, 12, 31 and 32 for further information.

Assumptions made as at each reporting date (e.g. the calculation of the provision for doubtful debts and fair value adjustments), are based on best estimates at that date. Although the Banking Group has internal control systems in place to ensure that estimates can be reliably measured, actual amounts may differ from those estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the reporting period in which the estimates are revised and in any future periods affected.

Reclassification of financial information

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.

Statement of compliance

The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand ("NZ GAAP"). They comply with New Zealand Equivalents to International Financial Reporting Standards ("NZ IFRS") and other applicable Financial Reporting Standards as appropriate for profit-oriented entities. The financial statements comply with International Financial Reporting Standards ("IFRS").

Changes in accounting policies and disclosures

New and amended accounting standards and interpretations

All mandatory standards, amendments and interpretations have been adopted in the current year. None had a material impact on these financial statements.

The Banking Group early adopted NZ IFRS 9 (2014) Financial Instruments in the previous year and has elected to exercise an accounting policy choice under NZ IFRS 9 to continue to apply the hedge accounting requirements under NZ IAS 39 Financial Instruments: Recognition and Measurement.

New and amended accounting standards and interpretations not yet effective

The following new and amended accounting standards and interpretations relevant to the Banking Group are not yet effective and have not been applied in preparing these financial statements:

- NZ IFRS 15 Revenue from Contracts with Customers, applicable for annual periods beginning on or after 1 January 2018. The new revenue standard replaces the existing notion of risks and rewards and introduces a single, principles-based five step model to be applied to all contracts with customers. The Banking Group is in the process of evaluating the potential impact of this standard.
- NZ IFRS 16 Leases, applicable for annual reporting periods beginning on or after 1 January 2019. The new leases standard eliminates the distinction between operating and finance leases for lessees, and will result in lessees bringing most leases onto their balance sheet. The Banking Group has not yet assessed the impact of this new standard.

Other amendments to existing standards that are not yet effective are not expected to result in a material impact on the Banking Group's reported results or financial position.

Currency of presentation

All amounts are expressed in New Zealand dollars unless otherwise stated.

Rounding of amounts

All amounts have been rounded to the nearest million dollars except where indicated.

Principles of consolidation

NZ IFRS 10 Consolidated Financial Statements considers whether an entity has control of another entity for the purpose of consolidation where the entity is exposed, or has rights to, that other entity's (including Structured Entities) variable returns from its involvement with that entity and whether the entity has the ability to affect those returns through its power over the other entity. Entities are fully consolidated from the date on which control is transferred to the Bank. They are deconsolidated from the date that control ceases.

In assessing whether the Banking Group controls and should consolidate a structured entity, management uses their judgement when considering the requirements of NZ IFRS 10 and NZ IFRS 12 Disclosures of Interests in Other Entities. In applying their judgement management will make assessments on whether the entity has control of another entity, taking into account factors including the following:

- the power the Banking Group has from existing rights to direct the relevant activities of the entity;
- the exposure or rights the Banking Group has to variable returns from the entity; and
- the ability of the Banking Group to affect the amount of their returns from the entity.

Inter-company balances and transactions, including income, expenses and dividends, are eliminated in full.

Note 1 Principal Accounting Policies *continued*

The financial results of the Bank's consolidated entities have been prepared in accordance with the Bank's accounting policies, which have been consistently applied throughout the Banking Group.

Foreign currency translation

i) Functional and presentation currency

Items included in the financial statements of each of the Banking Group's foreign operations are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The Disclosure Statement is presented in New Zealand dollars, which is the Bank's functional and presentation currency.

ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when recognised in other comprehensive income as qualifying cash flow hedges. Non-monetary items are translated using the exchange rate at the date of the initial recognition of the asset or liability.

iii) Foreign operations

The results and financial position of all of the Banking Group's operations that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate as at the reporting date;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- all resulting exchange differences are recognised in other comprehensive income, in the foreign currency translation reserve.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and from borrowings and other foreign currency instruments designated as hedges of such investments, are recognised in other comprehensive income. To the extent that the hedge is ineffective, such differences are recognised in the income statement. When a foreign operation is sold, such exchange differences are transferred out of reserves and reclassified to the income statement as part of the gain or loss on sale.

Fair value measurement

Fair value is defined as the price 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.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Banking Group recognises the profit on initial recognition (i.e. on day one).

Where a financial asset or liability is subsequently measured at fair value, the best evidence is independently quoted market prices in an active market. Where such prices are unavailable, then depending on the circumstances, alternative evidence may be used, including the price of recent transactions, prices for similar instruments or prices obtained utilising component parts (which when aggregated form the price of the whole instrument).

Where no active market exists for a particular asset or liability, the Banking Group uses standard market valuation techniques to arrive at the estimated fair value, utilising observable market sourced inputs wherever possible. Depending on the circumstances, the same alternative evidence (as described above) may be used in the valuation techniques. The valuation techniques address factors such as interest rates, liquidity and credit risk.

Fair value asset or liability prices defined above generally represent the present value of all future cash flows including those relating to interest, dividends or other cash flows as appropriate.

Assets

Financial assets

Financial assets comprise items such as Cash and liquid assets, Due from central banks and other institutions, Trading securities, Derivative financial instruments, Loans and advances to customers and Amounts due from related entities.

Financial assets are classified into the following measurement categories:

- those to be measured at fair value through profit or loss; and
- those to be measured at amortised cost.

The classification depends on the Banking Group's business model for managing financial assets and the contractual terms of the financial assets cash flows.

i) Financial assets measured at fair value through profit or loss

Items at fair value through profit or loss include items held for trading, items specifically designated as fair value through profit or loss on initial recognition, and debt instruments with contractual terms that do not represent solely payments of principal and interest.

Financial assets held at fair value through profit or loss are initially recognised at fair value, with transaction costs being recognised in the income statement as incurred. Subsequently, they are measured at fair value with gains and losses recognised in the income statement as they arise.

Note 1 Principal Accounting Policies *continued*

Where a financial asset is held at fair value, the movement in fair value attributable to interest rate market movements is either an observable market value or calculated based on changes in observable market interest rates for swaps. The movement in fair value attributable to changes in credit risk is established through a statistical-based calculation to estimate expected losses attributable to adverse movements in credit risk.

Financial assets held for trading
A financial asset is classified as held for trading if it is acquired principally for the purpose of selling or repurchasing 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 it is a derivative (not in a qualifying hedge relationship). The Banking Group has classified certain public and other debt securities as held for trading.

Financial assets designated at fair value through profit or loss
Upon initial recognition, financial assets may be designated at fair value through profit or loss. For a financial asset, the fair value option is only applied if it eliminates an accounting mismatch that would otherwise arise from measuring items on a different basis.

ii) Financial assets measured at amortised cost
A financial asset is measured at amortised cost only if:

- it is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset represent contractual cash flows that are solely payments of principal and interest.

These assets are initially recognised at fair value plus direct attributable transaction costs and subsequently measured at amortised cost.

Derivative financial instruments and hedge accounting
All derivatives are recognised in the balance sheet at fair value on trade date and are classified as trading except where they are used as part of an effective hedge relationship. The carrying value of a derivative is remeasured at fair value throughout the life of the contract. Derivatives are carried as assets when the fair value is positive, and liabilities when the fair value is negative.

The method of recognising the fair value gain or loss on a derivative depends on whether the derivative is used as a hedging instrument and, if so, the nature of the item being hedged. The Banking Group designates certain derivatives as either hedges of movements in the fair value of recognised assets and liabilities or firm commitments (fair value hedge) or hedges of highly probable future cash flows attributable to a recognised asset or liability or a forecast transaction (cash flow hedge). Hedge accounting is generally used for derivatives designated in this way, provided certain criteria are met.

At inception of the transaction, the Banking Group documents the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Banking Group also documents how effectiveness will be measured throughout the life of the hedge relationship and 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 or cash flows of hedged items.

Any derivative that is de-designated as a hedging derivative will be accounted for as trading from the time that it is de-designated, with all subsequent movements in fair value recognised in the income statement.

i) Fair value hedge accounting
Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify for fair value hedge accounting are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used, is amortised to the income statement on an effective yield basis over the remaining period to maturity of the hedged item.

ii) Cash flow hedge accounting
The effective portion of changes in fair value of derivatives that are designated and qualify for cash flow hedge accounting are recognised in other comprehensive income, while the gain or loss relating to any ineffective portion is recognised immediately in the income statement. The carrying value of the hedged item is not adjusted.

Amounts accumulated in reserves are transferred to the income statement in the period in which the hedged item will affect profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in reserves at that time remains in reserves and is recognised in the income statement when the forecast transaction ultimately affects profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in reserves is immediately transferred to the income statement.

Loans and advances
Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Banking Group provides money or services directly to a customer and has no intention of trading the loan.

Loans and advances are either measured at fair value through profit or loss or at amortised cost using the effective interest method, net of any provision for doubtful debts. Under the effective interest method, fee income and costs directly related to the origination of the loan are deferred over the expected life of the assets or, where appropriate, a shorter period. When calculating the effective interest rate, the Banking Group estimates cash flows considering all contractual terms of the financial instrument and excluding future credit losses. Unearned future income on lease finance represents interest not yet earned on the Banking Group's lease finance assets and is calculated on an amortised cost basis. Loans and advances are derecognised when the rights to receive cash flows have expired or the Banking Group has transferred substantially all of the risks and rewards of ownership.

Notes to and Forming Part of the Financial Statements

Note 1 Principal Accounting Policies *continued*

Impairment of financial assets

The Banking Group applies a three stage approach to measuring expected credit losses ("ECL") on debt instruments accounted for at amortised cost and fair value through other comprehensive income. Assets migrate through the following three stages based on their change in credit quality since initial recognition:

i) Stage 1: 12-months ECL
For exposures where there has not been a significant increase in credit risk since initial recognition and that 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.

ii) Stage 2: Lifetime ECL–not credit impaired
For exposures where there has been a significant increase in credit risk since initial recognition but that are not credit impaired, a lifetime ECL (i.e. reflecting the remaining lifetime of the financial asset) is recognised.

iii) Stage 3: Lifetime ECL–credit impaired
Financial assets are assessed as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that asset have occurred. For financial assets that have become credit impaired, a lifetime ECL is recognised and interest revenue is calculated by applying the effective interest rate to the amortised cost (net of provision) rather than the gross carrying amount.

At each reporting date, the Banking Group assesses whether there has been a significant increase in credit risk since initial recognition by comparing the risk of default occurring over the expected life between that of the reporting date to that of the date of initial recognition. In determining whether credit risk has increased significantly since initial recognition, the Banking Group uses its internal credit risk grading system, external risk ratings and forecast information to assess deterioration in credit quality of a financial asset.

The Banking Group assesses whether the credit risk on a financial asset has increased significantly on an individual or collective basis. For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of shared credit risk characteristics, taking into account instrument type, credit risk ratings, date of initial recognition, remaining term to maturity, industry, geographical location of the borrower and other relevant factors.

The amount of ECL is measured as the probability-weighted present value of all cash shortfalls over the expected life of the financial asset discounted at its original effective interest rate. The cash shortfall is the difference between all contractual cash flows that are due to the Banking Group and all the cash flows that the Banking Group expects to receive. The amount of the loss is recognised as a provision for doubtful debt.

The Banking Group considers its historical loss experience and adjusts this for current observable data. In addition, 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 rates, gross domestic product, inflation and commercial property prices, 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 ECL.

If, in a subsequent reporting period, the credit quality improves and reverses any previously assessed significant increase in credit risk since origination, then the provision for doubtful debts reverts from lifetime ECL to 12-months ECL.

Asset quality

The Banking Group has disclosed in note 13 certain components of its loan portfolio as impaired assets according to the classifications below:

- **Impaired assets** means any credit exposure for which an impairment loss is required in accordance with NZ IFRS 9 paragraph 5.5.

The following categories are also disclosed in note 13 but are not considered to be impaired assets:

- **Other assets under administration** are those loans that are not impaired or past due, but where the customer is in receivership, liquidation, statutory management or any other form of administration in New Zealand, or is in an equivalent form of voluntary or involuntary administration overseas.
- **Past due assets** are those loans that are not impaired and for which payments of principal or interest are contractually past due and adequate security is held.

Repurchase and reverse repurchase agreements

Securities sold under agreements to repurchase are classified in the investment or trading portfolios and accounted for accordingly. They are not derecognised from the balance sheet as the Bank retains substantially all of the risks and rewards of ownership. The Bank's obligation to repurchase is classified under Due to central banks and other institutions. The difference between the sale and repurchase prices represents interest expense and is recognised in the income statement over the term of the repurchase agreements.

Securities purchased under agreements to resell are recorded as Due from central banks and other institutions and Due from related parties. The difference between the purchase and the resale prices is treated as interest and accrued over the life of the agreements using the effective interest method.

Where the Banking Group has accepted collateral arising from secured placements and reverse repurchase agreements, the Banking Group is obliged to return equivalent securities. Securities repledged by the Banking Group are strictly for the purposes of providing collateral for the counterparty. These transactions are conducted under terms that are usual for customary standard lending, and securities borrowing and lending activities.

Securities lent to counterparties are also disclosed in the financial statements.

Liabilities

Financial liabilities

Financial liabilities comprise items such as Due to central banks and other institutions, Short term debt securities, Trading liabilities, Derivative financial instruments, Deposits from customers, Bonds and notes, Amounts due to related entities and Subordinated debt.

Financial liabilities may be held at fair value through profit or loss or at amortised cost.

i) Financial liabilities held at fair value through profit or loss

Items held at fair value through profit or loss comprise both items held for trading and items specifically designated at fair value through profit or loss on initial recognition. A financial liability is classified as held for trading if it is incurred principally for the purpose of selling in the near term, it forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative (not in a qualifying hedge relationship). The Banking Group has classified short sales of securities as Trading liabilities.

Note 1 Principal Accounting Policies *continued*

Financial liabilities held at fair value through profit or loss are initially recognised at fair value with transaction costs being recognised immediately in the income statement. Subsequently, they are measured at fair value and any gains and losses are recognised in the income statement as they arise.

Liabilities may be designated at fair value through profit or loss if they meet the following criteria:

- where designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets and liabilities (not only financial assets and liabilities) or recognising the gains and losses on them on different bases. Where derivative financial instruments have been transacted to hedge these amounts, an accounting inconsistency would arise if such amounts were accounted for on an amortised cost basis, as the derivatives are measured at fair value with movements in fair value recognised in the income statement. By designating these amounts at fair value through profit or loss, any fair value movements on the instrument will offset the fair value movements on hedging derivatives in the income statement; or
- those that are part of a group of financial assets, financial liabilities or both, that are managed and their performance is evaluated by management on a fair value basis in accordance with the documented risk management or investment strategy; or
- those that contain one or more embedded derivatives, except if the embedded derivative does not modify significantly the associated cash flows or it is clear with little or no analysis that separation is prohibited.

Once a financial instrument has been designated at fair value through profit or loss upon initial recognition, the Banking Group cannot subsequently change the designation.

Where a financial liability is held at fair value, the movement in fair value attributable to changes in the Bank's own credit quality is calculated by determining the changes in credit spreads above observable market interest rates and recognised in other comprehensive income.

ii) Financial liabilities held at amortised cost

All other financial liabilities, Amounts due to related entities and certain amounts within Due to central banks and other institutions and Deposits from customers and Subordinated debt are measured at amortised cost using the effective interest method.

Financial guarantees

The Banking Group provides guarantees in its normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Banking Group to guarantee the performance or financial obligations of a customer to a third party.

The financial guarantee contract is initially recorded at fair value which is equal to the premium received, unless there is evidence to the contrary.

Subsequently, the Banking Group records and measures the financial guarantee contract at the higher of:

- the amount initially recognised less, when appropriate, amortisation of the fee that is recognised over the life of the guarantee; and
- where it is likely the Banking Group will incur a loss as a result of issuing the contract, a liability is recognised for the estimated amount of the loss payable.

Offsetting arrangements

Financial assets and financial liabilities are offset and the net amount presented in the balance sheet when there is a legally enforceable right to offset and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously. The Banking Group does not offset its financial assets and financial liabilities in the balance sheet. Refer to note 33 for further information.

Employee entitlements

Employee entitlements to long service leave are measured as the present value of expected future payments using an actuarial valuation method based on legal and contractual entitlements and assessments having regard to staff departures, leave utilisation and future salary levels. Expected future payments are discounted using relevant market yields at the reporting date.

Wages and salaries, annual leave and other employee entitlements expected to be paid or settled within 12 months of providing the service are measured at their nominal amounts using remuneration rates that the Banking Group expects to pay when the liabilities are settled.

All other employee entitlements that are not expected to be paid or settled within 12 months of the reporting date are measured at the present value of net future cash flows.

Contingent liabilities

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefits is not probable or cannot be reliably measured. Contingent liabilities are not recognised in the balance sheet, but are disclosed unless the likelihood of payment is remote.

Perpetual preference shares

The Bank has issued perpetual non-cumulative preference shares to subsidiaries of the Bank's ultimate parent, National Australia Bank Limited. The perpetual preference shares are non-redeemable and do not create any direct or indirect contractual obligation to deliver cash to the preference shareholders, and as such are classified as equity instruments.

Note 1 Principal Accounting Policies *continued*

Revenue and expense recognition

Net interest income

Net interest income is reflected in the income statement using the effective interest method.

The effective interest method is a method of calculating amortisation using the effective interest rate of a financial asset or financial liability. The effective interest rate is the rate that exactly discounts the estimated stream of future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or liability.

When calculating the effective interest rate, the cash flows are estimated considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) excluding future credit losses.

The calculation of the effective interest rate includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Where it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of financial instruments), the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments) are used.

Dividend income

Dividend income is recorded in the income statement on an accruals basis when the Banking Group obtains control of the right to receive the dividend.

Fees and commissions

Unless included in the effective interest calculation, fees and commissions are recognised on an accrual basis as the service is provided. Fees and commissions not integral to the effective interest rate arising from negotiating, or participating in the negotiation of a transaction with a third party, such as purchase or sale of businesses, are recognised on completion of the underlying transaction.

Funds management and other fiduciary activities

Fees and commissions earned through the marketing of funds management products and other fiduciary activities are included in the income statement as they are earned.

Gains less losses on financial instruments

Gains less losses on financial instruments recognised in the income statement comprises fair value gains and losses from three distinct activities:

- trading financial instruments;
- instruments designated in hedge accounting relationships; and
- other financial instruments designated at fair value through profit or loss.

Trading financial instruments include trading derivatives and trading securities. In general, gains less losses on trading derivatives recognises the full change in fair value of the derivatives inclusive of interest income and expense. However, in cases where the trading derivative is economically offsetting movements in the fair value of an asset or liability designated as being carried at fair value through profit or loss, the interest income and expense attributable to the derivative is recognised within net interest income and not part of the fair value movement of the trading derivative. Interest income and expenses on trading securities are reported within interest income.

Gains less losses on hedging assets, liabilities and derivatives designated in hedge accounting relationships recognises fair value movements on both the hedged item and hedging derivative in a fair value hedge accounting relationship, and hedge ineffectiveness for both fair value and cash flow hedge accounting relationships. Interest income and expenses on both hedging instruments and instruments designated at fair value through profit or loss at initial recognition are recognised in net interest income.

Gains less losses on financial assets and liabilities designated at fair value through profit or loss at inception recognises fair value movements excluding interest, which is reported within net interest income. Changes in the fair value of financial liabilities designated at fair value through profit or loss attributable to the Banking Group's own credit quality are presented separately in other comprehensive income.

Gains less losses on financial instruments includes gains and losses on the derecognition of financial instruments held at amortised cost.

Leasing

As lessee, the leases entered into by the Banking Group are primarily operating leases. Operating lease rentals are charged to the income statement on a straight-line basis over the term of the lease.

Income tax

Income tax expense is the income tax charge or benefit incurred on the current reporting period's profit or loss and is the aggregate of the movements in deferred tax taken through the income statement and the amount of income tax payable or recoverable in respect of taxable profit or loss for the period at the applicable tax rate.

Deferred tax assets are the amounts of income tax recoverable in future periods including unused tax losses and unused tax credits carried forward. Deferred tax liabilities are the amounts of income tax payable in future periods. Deferred tax assets and liabilities arise when there is a temporary difference between the tax bases (amount attributable to the asset or liability for tax purposes) of assets and liabilities and their carrying amounts in the balance sheet. Deferred tax assets and liabilities are determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax liabilities are recognised for all taxable temporary differences, except:

- for a deferred income tax liability arising from the initial recognition of goodwill;
- where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit or loss nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in wholly owned entities, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax credits and unused tax losses can be utilised:

Note 1 Principal Accounting Policies *continued*

- except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit or loss nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in wholly owned entities, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amounts of deferred income tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Income tax relating to items recognised directly in other comprehensive income is recognised in other comprehensive income and not in the income statement.

Goods and services tax

Revenues, expenses and assets are recognised net of the amount of value added tax such as goods and services tax, except where the tax incurred is not recoverable from the Inland Revenue Department. In these circumstances, the tax is recognised as part of the expense or the acquisition of the asset.

Receivables and payables are stated at an amount with tax included. The net amount of tax recoverable from, or payable to, Inland Revenue is included within either other assets or other liabilities.

Cash flows are included in the cash flow statement on a net basis. The tax component of cash flows for all activities is classified within operating activities.

Share-based payments

The Banking Group engages in equity settled share-based payment transactions via its ultimate parent, National Australia Bank Limited, in respect of services received from its employees. The fair value of the services received is measured by reference to the fair value of the shares or performance rights granted on the date of the grant. The cost of the employee services received in respect of the shares or performance rights granted is recognised in the income statement over the period in which the services are received, which is the vesting period.

The grant date fair value of each share is determined by the market value of the National Australia Bank Limited share, and is generally a five day weighted average price. Employee share plans and performance rights are linked to service conditions, and/or internal performance and market performance.

The fair value of the performance rights with market performance hurdles is determined using a simulated version of the Black-Scholes model. The key assumptions and inputs used in the valuation model are the exercise price of the performance rights, the expected volatility of the National Australia Bank Limited share price, the risk-free interest rate and the expected dividend yield on the National Australia Bank Limited shares for the life of the performance rights.

Except for those that include terms related to market conditions, vesting conditions included in the terms of the grant are not taken into account in estimating fair value.

Non-market vesting conditions are taken into account by adjusting the number of shares or performance rights included in the measurement of the cost of employee services so that ultimately, the amount recognised in the income statement reflects the number of vested shares or performance rights. Where vesting conditions are related to market conditions, the charges for the services received are recognised regardless of whether or not the market related vesting condition is met, provided that the non-market vesting conditions are met.

Income Statement Notes

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 2 Interest		
Interest income		
Central banks	**39**	59
Other financial institutions	**19**	21
Non-financial institutions	**4**	6
Trading securities	**133**	170
Loans and advances to customers	**3,617**	3,972
Individually impaired assets	**7**	7
Related entities	**35**	12
Total interest income	**3,854**	4,247
Total interest income was derived from financial assets:		
Not at fair value through profit or loss	**3,327**	3,635
At fair value through profit or loss	**527**	612
	3,854	4,247
Interest expense		
Central banks and other institutions	**20**	18
Short term debt securities*	**132**	145
Deposits from customers	**1,215**	1,486
Bonds and notes*	**672**	816
Related entities	**14**	15
Subordinated loans to related entities	**19**	29
Subordinated notes to external investors	**25**	-
Other*	**-**	3
Total interest expense	**2,097**	2,512
Total interest expense was incurred on financial liabilities:		
Not at fair value through profit or loss	**1,140**	1,397
At fair value through profit or loss	**957**	1,115
	2,097	2,512

* Certain prior year amounts for interest expense have been reclassified to align with changes in presentation made in the current year.

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 3 Gains Less Losses on Financial Instruments		
Trading gains less losses on financial instruments		
Foreign exchange trading gain	114	105
Interest rate related trading derivatives	(25)	65
Other derivatives	(1)	-
Net gain/(loss) in the fair value of financial assets and liabilities held for trading	48	58
Trading gains less losses on financial instruments	136	228
Other gains less losses on financial instruments		
Hedge accounting		
Net gain/(loss) arising from hedging instruments in fair value hedge accounting relationships	15	(212)
Net gain/(loss) arising from the hedged items attributable to the hedged risk in fair value hedge accounting relationships	(62)	209
Ineffectiveness arising from cash flow hedge accounting relationships	(1)	2
	(48)	(1)
Other		
Net gain/(loss) in the fair value of financial assets (refer to table below)	(8)	(7)
Net gain/(loss) in the fair value of financial liabilities (refer to table below)	(15)	76
Bid/offer adjustment	(1)	(1)
Net gain/(loss) attributable to other derivatives used for hedging purposes that no longer qualify for hedge accounting	42	27
	18	95
Other gains less losses on financial instruments	(30)	94
Total gains less losses on financial instruments	106	322
Net gain/(loss) in the fair value of financial assets comprised:		
Gain/(loss) in the fair value of financial assets designated at fair value through profit or loss	(3)	167
Credit risk adjustments on financial assets designated at fair value through profit or loss	(4)	(7)
Net gain/(loss) attributable to other derivatives used for hedging purposes where hedge accounting is not applied	(1)	(167)
	(8)	(7)
Net gain/(loss) in the fair value of financial liabilities comprised:*		
Gain/(loss) in the fair value of financial liabilities designated at fair value through profit or loss	62	(106)
Net gain/(loss) attributable to other derivatives used for hedging purposes where hedge accounting is not applied	(77)	182
	(15)	76

* All foreign currency gains/(losses) are excluded from this category. Due to the Banking Group's practice of managing all foreign exchange risk centrally, all foreign currency gains/(losses) are included within 'Foreign exchange trading gain' above.

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 4 Other Operating Income		
Dividends received from other investments	2	3
Money transfer fees	106	107
Fees earned on financial assets and liabilities at fair value through profit or loss	41	48
Fees earned on financial assets and liabilities at amortised cost	118	116
Fees earned on trust and other fiduciary activities	12	10
Other income, other fees and commissions income	127	91
Total other operating income	406	375

Dollars in Millions	Consolidated 30/9/16	Consolidated 30/9/15
Note 5 Operating Expenses		
Amortisation and depreciation		
Amortisation of intangible assets	43	37
Depreciation on property, plant and equipment	41	41
	84	78
Impairment losses and write offs		
Write offs and impairment losses on intangible assets	-	6
Write offs and impairment losses on furniture, fittings and other equipment	-	2
	-	8
Personnel expenses		
Share based payments (refer to note 6)	7	5
Defined contribution pension expense	17	17
Salaries and other staff expenses	452	427
	476	449
Other		
Rental on operating leases (refer to table below)	69	62
Related entity expenses	36	52
Other expenses	224	216
	329	330
Total operating expenses	889	865

Dollars in Millions	Consolidated 30/9/16	Consolidated 30/9/15
Rental on operating leases comprised:		
Lease payments		
Minimum lease payments	69	62
Total rental on operating leases	69	62
Personnel expenses include key management personnel remuneration paid or payable which comprised:		
Short term employee benefits	7	7
Equity compensation benefits	2	1
Total key management personnel remuneration paid or payable	9	8

Dollars in Thousands	Consolidated 30/9/16	Consolidated 30/9/15
Fees paid to auditors:		
Audit and review of financial statements	1,873	1,847
Other assurance and risk related services*	447	394

* Fees paid to auditors were for other assurance services provided in relation to funding activities, due diligence, benchmark remuneration services and cyber security assessment.

Note 6 Share Based Payments Expense

Shares and performance rights (subject to restrictions) are granted to employees of the Banking Group by the ultimate parent, National Australia Bank Limited, as part of NAB's short term and long term incentives ("STI" and "LTI") to employees. These incentives are an integral part of the Banking Group's remuneration strategy in rewarding an employee's current and future contribution to the Banking Group's performance.

The plans described below involve the provision of equity grants to employees of the Banking Group. The Banking Group reimburses National Australia Bank Limited for the cost of these grants. Details of the share based payments expense and the related entity payables are contained within notes 5 and 30 respectively.

As at 30 September 2016, share based payments expense of $14 million in relation to performance rights granted to employees of the Banking Group had not yet been charged by National Australia Bank Limited (30 September 2015: $16 million). This amount is required to be expensed in future periods under NZ IFRS 2 Share-based Payment.

a) NAB New Zealand Staff Share Allocation Plan

This plan provides for the National Australia Bank Limited Board to invite any employee of the Banking Group based in New Zealand to participate in an offer under this plan. Under this plan, funds are provided (if required) to National Australia Trustees Limited to subscribe for or purchase fully paid ordinary shares in National Australia Bank Limited on behalf of participating employees.

Year-end share offer

This programme is designed to offer up to approximately A$1,000 of ordinary shares to each employee when NAB's performance is on target, as measured against a scorecard of objectives for NAB for the financial year. These shares are held by the trustee for three years, or until the employee ceases his or her employment.

Under the New Zealand programme, each eligible employee is required to pay NZ$1.00 for the whole parcel of shares offered, or the market price of the parcel, whichever is less. Participating employees receive dividends and may exercise voting rights in respect of the shares, but otherwise cannot transact the shares until the restriction period concludes. If a participating employee leaves the Banking Group prior to the end of the three-year restriction period due to voluntary resignation or dismissal, the trustee will purchase the shares back for the lesser of the market price or the price paid by the employee for the shares.

b) NAB Executive Performance Rights Plan

STI Deferral

Each year, the Banking Group's senior executives participate in the STI Deferral offer and receive half of the value of their STI rewards in the form of National Australia Bank Limited performance rights. Employees become eligible for these rights based on their individual or business performance (or both). Deferred awards granted in respect of 2015 or earlier were granted in two equal tranches with half restricted for 12 months and the remaining half for 24 months. Deferred awards granted in respect of future awards will be granted in one tranche to be restricted for 12 months. Performance rights lapse during the restriction period if the employee resigns or fails to pass specific compliance expectations in respect of their performance review. The Board may also, in its discretion, lapse all or part of an employee's performance rights.

Long term incentives

National Australia Bank Limited operates an LTI programme primarily targeted at key executive positions. The programme delivers performance rights (instead of shares) aligned to National Australia Bank Limited's share price.

The plans provide for the National Australia Bank Limited Board to grant performance rights to selected senior executives of the Banking Group to subscribe for fully paid ordinary shares in National Australia Bank Limited. Each performance right entitles the holder to subscribe for one fully paid ordinary share in National Australia Bank Limited. The performance rights cannot be transferred and are not quoted on the Australian Securities Exchange. No payment is required from executives at the time of the grant. There are no voting or dividend rights attached to the performance rights.

The number and weighted average exercise prices of performance rights were as follows:

	Consolidated	
Number of Rights	**30/9/16**	30/9/15
Performance rights		
Outstanding at beginning of year	**334,790**	256,341
Add: Granted during the year	**188,395**	147,925
Add: Transferred in during the year	**14,818**	186
Deduct: Exercised during the year	**45,774**	40,954
Deduct: Forfeited during the year	**15,918**	28,336
Deduct: Transferred out during the year	**-**	372
Outstanding at end of year	**476,311**	334,790
Exercisable at end of year	**2,976**	3,632

Note 6 Share Based Payments Expense *continued*

The volume weighted average price of National Australia Bank Limited shares during the year ended 30 September 2016 was A$27.38 (year ended 30 September 2015: A$33.87).

Fair value of performance rights

The following table shows the significant assumptions used as inputs into the grant date fair value calculation of performance rights granted during the last two years. In the table, values have been presented as weighted averages, but the specific values for each grant are used for the fair value calculation. The table shows a 'no hurdle' value where the grant includes performance rights which have non-market based performance hurdles attached. For further details on the fair value methodology, refer to note 1.

	Consolidated	
	30/9/16	30/9/15
Weighted average values		
Contractual life (years)	3.0	4.8
Risk-free interest rate (per annum)	2.10%	2.41%
Expected volatility of share price	18.00%	17.00%
Closing share price on grant date	A$28.30	A$33.34
Dividend yield (per annum)	5.90%	5.80%
Fair value of performance rights	A$9.63	A$14.01
'No hurdle' value of performance rights	A$23.84	A$30.15
Expected time to vesting (years)	2.72	3.69

	Consolidated	
Dollars in Millions	30/9/16	30/9/15

Note 7 Income Tax Expense on Operating Profit

Income tax on operating profit charged to income statement		
Current tax	373	396
Deferred tax	(26)	5
Total income tax on operating profit charged to income statement	347	401
Reconciliation of income tax expense on operating profit shown in the income statement with prima facie tax payable on the pre-tax accounting profit		
Total operating profit before income tax expense	1,260	1,439
Prima facie income tax at 28%	353	403
Add/(deduct): Tax effect of amounts which are non-deductible or non-assessable:		
Non-assessable and tax paid income	-	(2)
Other accounting movements	(6)	-
Total income tax expense on operating profit	347	401
Effective tax rate	27.5%	27.9%
Income tax charged to other comprehensive income		
Current tax	5	35
Total income tax charged to other comprehensive income	5	35

Asset Notes

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 8 Cash and Liquid Assets		
Notes and coins	135	153
Transaction balances with central banks	1,432	1,219
Transaction balances with other institutions	232	262
Total cash and liquid assets	1,799	1,634

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 9 Due from Central Banks and Other Institutions		
Loans and advances due from other institutions	1,648	1,682
Securities purchased under agreements to resell with other financial institutions*	172	128
Securities purchased under agreements to resell with non-financial institutions*	479	199
Total due from central banks and other institutions	2,299	2,009

* Classified as cash and cash equivalents in the cash flow statement.

The Banking Group has accepted collateral of New Zealand government securities with a fair value of $800 million as at 30 September 2016 arising from reverse repurchase agreements included in due from central banks and other institutions and due from related entities (refer to note 30), which it is permitted to sell or repledge (30 September 2015: $874 million).

Government securities with a fair value of $87 million were repledged as at 30 September 2016 (30 September 2015: $113 million). Securities were repledged for periods of less than three months. The Bank's obligation to repurchase government securities is classified under due to central banks and other institutions (refer to note 19).

Included in due from central banks and other institutions as at 30 September 2016 was $1,412 million of collateral posted with counterparties to meet standard derivative trading obligations (30 September 2015: $1,148 million).

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 10 Trading Securities		
Government bonds, notes and securities	3,241	2,656
Semi-government bonds, notes and securities	510	749
Corporate and other institutions bonds, notes and securities	952	1,513
Total trading securities	4,703	4,918

Included in trading securities as at 30 September 2016 were $152 million encumbered through repurchase agreements (30 September 2015: $159 million). These trading securities have not been derecognised from the Bank as the Bank retains substantially all the risks and rewards of ownership. Counterparties have the right to sell or repledge these encumbered securities. The Bank's obligation to repurchase trading securities is classified under due to central banks and other institutions (refer to note 19) and due to related entities (refer to note 30).

Dollars in Millions	Consolidated 30/9/16	Consolidated 30/9/15
Note 11 Loans and Advances to Customers		
Overdrafts	**2,387**	2,400
Credit card outstandings	**1,131**	1,160
Housing loans	**34,914**	31,830
Other term lending	**35,354**	32,003
Other lending	**907**	1,037
Total gross loans and advances to customers	**74,693**	68,430
Deduct:		
Specific provision for doubtful debts and credit risk adjustments on individual financial assets (refer to note 12)	**100**	92
Collective provision for doubtful debts and credit risk adjustments on groups of financial assets (refer to note 12)	**445**	374
Deferred and other unearned future income/(expenses)	**(84)**	(45)
Fair value hedge adjustments	**(146)**	(207)
Total deductions	**315**	214
Total net loans and advances to customers	**74,378**	68,216

The BNZ RMBS Trust Series 2008-1 (the "RMBS Trust") provides an internal residential mortgage-backed securities ("RMBS") programme to issue securities as collateral for borrowing from the RBNZ. As at 30 September 2016, included within the Banking Group's loans and advances to customers were housing loans with a carrying amount of $4,472 million held by the RMBS Trust (30 September 2015: $4,467 million). These housing loans have not been derecognised by the Bank for financial reporting purposes as the Bank retains substantially all of the risks and rewards of ownership. These housing loans and other assets (including cash) of the RMBS Trust secure debt instruments issued to the Bank as detailed in the Liquidity portfolio management section in Note 41. The Banking Group had not entered into any repurchase agreements for residential mortgage-backed securities with the RBNZ as at 30 September 2016 (30 September 2015: nil). The RBNZ had not accepted any residential mortgage-backed securities as collateral from the Banking Group as at 30 September 2016 (30 September 2015: nil) and, as a result, the securities issued by the RMBS Trust remain unencumbered.

The BNZ Covered Bond Trust (the "Covered Bond Trust") holds certain Bank of New Zealand housing loans and its trustee guarantees the payment of interest and principal under the covered bonds issued by the Bank and BNZ-IF. The assets of the Covered Bond Trust are not available to the Bank unless and until all prior ranking creditors of the Covered Bond Trust have been satisfied. As at 30 September 2016, included within the Banking Group's loans and advances to customers were housing loans with a carrying amount of $4,956 million held by the Covered Bond Trust (30 September 2015: $4,204 million). These housing loans have not been derecognised by the Bank for financial reporting purposes as the Bank retains substantially all of the risks and rewards of ownership. The Banking Group had issued debt securities with a face value of $3,901 million that were guaranteed by the Covered Bond Trust as at 30 September 2016 (30 September 2015: $3,436 million). The underlying collateral that supports the guarantee provided by the Covered Bond Trust comprised housing loans and other assets (including cash) with a carrying amount of $5,003 million as at 30 September 2016 (30 September 2015: $4,293 million).

Further details on the transactions with the RMBS Trust and the Covered Bond Trust are provided in notes 16, 22, 30, 34, 39 and 41.

	Consolidated			
Dollars in Millions	Residential Mortgage Lending 30/9/16	Other Retail Exposures 30/9/16	Corporate Exposures 30/9/16	Total 30/9/16
Note 12 Provision for Doubtful Debts				
Loans and advances to customers				
Collective provision for doubtful debts measured on a 12-months expected credit loss ("ECL")	**1**	**13**	**46**	**60**
Provision for doubtful debts measured on a lifetime ECL				
Collective provision for doubtful debts for assets not credit impaired	**12**	**10**	**213**	**235**
Collective provision for doubtful debts for credit impaired assets	**4**	**8**	**91**	**103**
Specific provision for doubtful debts for credit impaired assets	**11**	**8**	**80**	**99**
Total provision for doubtful debts measured on a lifetime ECL	**27**	**26**	**384**	**437**
Total provision for doubtful debts	**28**	**39**	**430**	**497**
	Consolidated (30/9/15)			
Loans and advances to customers				
Collective provision for doubtful debts measured on a 12-months ECL	2	9	65	76
Provision for doubtful debts measured on a lifetime ECL				
Collective provision for doubtful debts for assets not credit impaired	5	7	192	204
Collective provision for doubtful debts for credit impaired assets	7	9	34	50
Specific provision for doubtful debts for credit impaired assets	14	6	72	92
Total provision for doubtful debts measured on a lifetime ECL	26	22	298	346
Total provision for doubtful debts	28	31	363	422

Note 12 Provision for Doubtful Debts *continued*

The following table provides a reconciliation from the opening balance to the closing balance of provision for doubtful debts and shows the movement in opening balance where financial assets have transferred between provision stages during the year.

	Consolidated				
Dollars in Millions	Collective Provision 12-months ECL 30/9/16	Collective Provision Lifetime ECL Not Credit Impaired 30/9/16	Collective Provision Lifetime ECL Credit Impaired 30/9/16	Specific Provision Lifetime ECL Credit Impaired 30/9/16	Total 30/9/16
Movement in provision for doubtful debts					
Residential mortgage lending					
Balance at beginning of year	2	5	7	14	28
Changes to the opening balance due to transfer between ECL stages:					
Transferred to collective provision 12-months ECL	4	(2)	(2)	-	-
Transferred to collective provision lifetime ECL not credit impaired	-	1	(1)	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(1)	1	-	-
Transferred to specific provision lifetime ECL credit impaired	-	-	(1)	1	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(5)	9	-	3	7
Amounts written off	-	-	-	(7)	(7)
Recovery of amounts written off	-	-	-	-	-
Balance at end of year - Residential mortgage lending	1	12	4	11	28
Other retail exposures					
Balance at beginning of year	9	7	9	6	31
Changes to the opening balance due to transfer between ECL stages:					
Transferred to collective provision 12-months ECL	5	(4)	(1)	-	-
Transferred to collective provision lifetime ECL not credit impaired	(1)	2	(1)	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(1)	1	-	-
Transferred to specific provision lifetime ECL credit impaired	-	(1)	(5)	6	-
Charge / (credit) to income statement excluding transfer between ECL stages*	-	7	5	19	31
Amounts written off	-	-	-	(34)	(34)
Recovery of amounts written off	-	-	-	11	11
Balance at end of year - Other retail exposures	13	10	8	8	39
Corporate exposures					
Balance at beginning of year	65	192	34	72	363
Changes to the opening balance due to transfer between ECL stages:					
Transferred to collective provision 12-months ECL	48	(48)	-	-	-
Transferred to collective provision lifetime ECL not credit impaired	(6)	11	(5)	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(24)	24	-	-
Transferred to specific provision lifetime ECL credit impaired	-	(5)	(2)	7	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(61)	87	40	16	82
Amounts written off	-	-	-	(18)	(18)
Recovery of amounts written off	-	-	-	3	3
Balance at end of year - Corporate exposures	46	213	91	80	430
Total					
Balance at beginning of year	76	204	50	92	422
Changes to the opening balance due to transfer between ECL stages:					
Transferred to collective provision 12-months ECL	57	(54)	(3)	-	-
Transferred to collective provision lifetime ECL not credit impaired	(7)	14	(7)	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(26)	26	-	-
Transferred to specific provision lifetime ECL credit impaired	-	(6)	(8)	14	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(66)	103	45	38	120
Amounts written off	-	-	-	(59)	(59)
Recovery of amounts written off	-	-	-	14	14
Total provision for doubtful debt balance at end of year	60	235	103	99	497

* Classified as impairment losses on credit exposures in the income statement.

Note 12 Provision for Doubtful Debts *continued*

	Consolidated					
Dollars in Millions	Collective Provision 12-months ECL 30/9/15	Collective Provision Lifetime ECL Not Credit Impaired 30/9/15	Collective Provision Lifetime ECL Credit Impaired 30/9/15	Collective Provision* 30/9/15	Specific Provision Lifetime ECL Credit Impaired 30/9/15	Total 30/9/15
Movement in provision for doubtful debts						
Residential mortgage lending						
Balance at beginning of year	-	-	-	6	21	27
Restated for adoption of new accounting standard	1	4	4	(6)	-	3
Changes to the opening balance due to transfer between ECL stages:						
Transferred to collective provision 12-months ECL	2	(1)	(1)	-	-	-
Transferred to collective provision lifetime ECL not credit impaired	-	-	-	-	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(1)	1	-	-	-
Transferred to specific provision lifetime ECL credit impaired	-	-	(1)	-	1	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(1)	3	4	-	-	6
Amounts written off	-	-	-	-	(8)	(8)
Recovery of amounts written off	-	-	-	-	-	-
Balance at end of year - Residential mortgage lending	2	5	7	-	14	28
Other retail exposures						
Balance at beginning of year	-	-	-	31	7	38
Restated for adoption of new accounting standard	9	6	9	(31)	-	(7)
Changes to the opening balance due to transfer between ECL stages:						
Transferred to collective provision 12-months ECL	5	(4)	(1)	-	-	-
Transferred to collective provision lifetime ECL not credit impaired	(2)	3	(1)	-	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(2)	2	-	-	-
Transferred to specific provision lifetime ECL credit impaired	-	(1)	(5)	-	6	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(3)	5	5	-	16	23
Amounts written off	-	-	-	-	(33)	(33)
Recovery of amounts written off	-	-	-	-	10	10
Balance at end of year - Other retail exposures	9	7	9	-	6	31
Corporate exposures						
Balance at beginning of year	-	-	-	91	88	179
Restated for adoption of new accounting standard	69	142	46	(91)	4	170
Changes to the opening balance due to transfer between ECL stages:						
Transferred to collective provision 12-months ECL	24	(24)	-	-	-	-
Transferred to collective provision lifetime ECL not credit impaired	(9)	10	(1)	-	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(1)	1	-	-	-
Transferred to specific provision lifetime ECL credit impaired	-	(20)	(3)	-	23	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(19)	85	(9)	-	42	99
Amounts written off	-	-	-	-	(85)	(85)
Recovery of amounts written off	-	-	-	-	-	-
Balance at end of year - Corporate exposures	65	192	34	-	72	363
Total						
Balance at beginning of year	-	-	-	128	116	244
Restated for adoption of new accounting standard	79	152	59	(128)	4	166
Changes to the opening balance due to transfer between ECL stages:						
Transferred to collective provision 12-months ECL	31	(29)	(2)	-	-	-
Transferred to collective provision lifetime ECL not credit impaired	(11)	13	(2)	-	-	-
Transferred to collective provision lifetime ECL credit impaired	-	(4)	4	-	-	-
Transferred to specific provision lifetime ECL credit impaired	-	(21)	(9)	-	30	-
Charge / (credit) to income statement excluding transfer between ECL stages*	(23)	93	-	-	58	128
Amounts written off	-	-	-	-	(126)	(126)
Recovery of amounts written off	-	-	-	-	10	10
Total provision for doubtful debt balance at end of year	76	204	50	-	92	422

* Classified as impairment losses on credit exposures in the income statement.

Note 12 Provision for Doubtful Debts *continued*

Impact of changes in gross carrying amount on ECL

The following explains how significant changes in the gross carrying amount of financial assets during the year have contributed to the changes in the provision for doubtful debts. Provision for doubtful debts reflects ECL measured using the three-stage approach under NZ IFRS 9. Refer to note 1 for a detailed description of these stages.

Overall, the net increase in the total provision for doubtful debts of $75 million was driven by increased specific provisioning for credit impaired assets and collective provisioning, offset by write-offs during the year. The outlook for the dairy industry largely contributed to the increase in collective provision in Stage 2 and Stage 3. Across all stages, the increase was mainly attributed to an increase in the corporate segment of $67 million and an increase in the other retail segment of $8 million.

- Collective provision 12-months ECL (Stage 1) decreased by $16 million, reflecting the net movement in originated and repaid loans. This decrease was offset by loans that returned to Stage 1 due to improvement in credit quality.
- Collective provision lifetime ECL – not credit impaired (Stage 2) increased by $31 million, mainly due to increase in collective provision reflecting the outlook in dairy industry. This increase was offset by loans that returned to Stage 1 due to improvement in credit quality as described above, and loans that became credit impaired as a result of reduced asset quality, moving to Stage 3.
- Collective provision lifetime ECL – credit impaired (Stage 3) increased by $53 million, mainly due to increase in collective provision reflecting the outlook in dairy industry and migration of loans to Stage 3 reflecting the deterioration in credit quality. The increases were partially offset by loans that migrated from Stage 3 to Stage 2 and to individually assessed credit impaired assets.
- Specific provision lifetime ECL - credit impaired (Stage 3) increased by $7 million, reflecting the migration of loans previously assessed collectively, partially offset by net write-offs during the year.

Gross carrying amounts written off during the year still subject to enforcement activity

As at 30 September 2016, the contractual amount outstanding on loans and advances to customers written off during the year, and that are still subject to enforcement activity was $14 million for the Banking Group (30 September 2015: $42 million).

Information about the nature and effect of modifications on the measurement of doubtful debts

A loan that is renegotiated is derecognised from the Banking Group's balance sheet if the existing agreement is cancelled and a new agreement made on substantially different terms or if the terms of an existing agreement are modified such that the renegotiated loan is a substantially different instrument. Where such loans are derecognised, the renegotiated contract is a new loan and impairment is assessed in accordance with the Banking Group's accounting policy.

Where the renegotiation of such loans does not result in derecognition, impairment continues to be assessed for significant increases in credit risk compared to the initial origination credit risk rating.

The following table shows information on loans and advances that were modified but not derecognised during the year, for which the provision for doubtful debts was measured at a lifetime ECL at the beginning of the year, and at the end of the year had changed to a 12-months ECL:

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15*
Amortised cost before the modification	**114**	81
Gross carrying amount at end of year	**114**	73

* The 2015 comparative information has been restated due to change in methodology to exclude off balance sheet and include facility balances.

Notes to and Forming Part of the Financial Statements

Note 12 Provision for Doubtful Debts *continued*

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

The changes in value of financial assets designated at fair value through profit or loss that are attributable to changes in credit risk have been calculated using a statistical-based calculation that estimates expected losses attributable to adverse movement in credit risks.

Credit risk adjustments on financial assets designated at fair value through profit or loss are analysed in the following table.

	Consolidated			
Dollars in Millions	Residential Mortgage Lending 30/9/16	Other Retail Exposures 30/9/16	Corporate Exposures 30/9/16	Total 30/9/16
Credit risk adjustment on individual financial assets				
Loans and advances to customers				
Balance at beginning of year	-	-	-	-
Charge/(credit) to income statement	-	-	1	1
Amounts written off	-	-	-	-
Balance at end of year	-	-	1	1
Credit risk adjustment on groups of financial assets				
Loans and advances to customers				
Balance at beginning of year	-	1	43	44
Charge / (credit) to income statement	-	-	3	3
Balance at end of year	-	1	46	47
Total credit risk adjustments on loans and advances designated at fair value through profit or loss	-	1	47	48
Trading derivative financial instruments				
Balance at beginning of year	-	-	(2)	(2)
Charge / (credit) to income statement	-	-	22	22
Balance at end of year	-	-	20	20
Total credit risk adjustments on trading derivative financial instruments	-	-	20	20
	Consolidated (30/9/15)			
Credit risk adjustment on individual financial assets				
Loans and advances to customers				
Balance at beginning of year	-	-	4	4
Restated for adoption of new accounting standard	-	-	(4)	(4)
Charge / (credit) to income statement	-	-	-	-
Amounts written off	-	-	-	-
Balance at end of year	-	-	-	-
Credit risk adjustment on groups of financial assets				
Loans and advances to customers				
Balance at beginning of year	-	3	147	150
Restated for adoption of new accounting standard	-	(2)	(111)	(113)
Charge / (credit) to income statement	-	-	7	7
Balance at end of year	-	1	43	44
Total credit risk adjustments on loans and advances designated at fair value through profit or loss	-	1	43	44
Trading derivative financial instruments				
Balance at beginning of year	-	-	4	4
Charge / (credit) to income statement	-	-	(6)	(6)
Balance at end of year	-	-	(2)	(2)
Total credit risk adjustments on trading derivative financial instruments	-	-	(2)	(2)

Note 13 Asset Quality

The Banking Group provides for doubtful debts as disclosed in note 12. Accordingly, when management determines that recovery of a loan is doubtful, the principal amount and accrued interest on the obligation are written down to estimated net realisable value.

	Consolidated			
	Residential Mortgage Lending	Other Retail Exposures	Corporate Exposures	Total
Dollars in Millions	30/9/16	30/9/16	30/9/16	30/9/16
Movements in pre-allowance balances				
Individually impaired assets - at amortised cost				
Balance at beginning of year	40	14	160	214
Amounts written off	(7)	(34)	(18)	(59)
Additions	47	47	213	307
Deletions	(49)	(13)	(154)	(216)
Balance at end of year	31	14	201	246
Specific provision for doubtful debt	11	8	80	99
Individually impaired assets - at fair value through profit or loss				
Balance at beginning of year	-	-	1	1
Amounts written off	-	-	-	-
Additions	-	-	7	7
Deletions	-	-	(1)	(1)
Balance at end of year	-	-	7	7
Credit risk adjustments on individual financial assets designated at fair value through profit or loss	-	-	1	1
Total impaired assets at end of year	31	14	208	253
Individually impaired assets - undrawn lending commitments				
At amortised cost	-	-	2	2
At fair value through profit or loss	-	-	-	-
Other assets under administration	12	1	7	20

	Consolidated (30/9/15)			
Movements in pre-allowance balances				
Individually impaired assets - at amortised cost				
Balance at beginning of year	63	13	187	263
Restated for adoption of new accounting standards	-	-	13	13
Amounts written off	(8)	(33)	(85)	(126)
Additions	54	51	170	275
Deletions	(69)	(17)	(125)	(211)
Balance at end of year	40	14	160	214
Specific provision for doubtful debt	14	6	72	92
Individually impaired assets - at fair value through profit or loss				
Balance at beginning of year	-	1	13	14
Restated for adoption of new accounting standards	-	-	(13)	(13)
Amounts written off	-	-	-	-
Additions	-	-	1	1
Deletions	-	(1)	-	(1)
Balance at end of year	-	-	1	1
Credit risk adjustments on individual financial assets designated at fair value through profit or loss	-	-	-	-
Total impaired assets at end of year	40	14	161	215
Individually impaired assets - undrawn lending commitments				
At amortised cost	-	-	-	-
At fair value through profit or loss	-	-	-	-
Other assets under administration	13	2	3	18

* In the NAB 2016 Annual Financial Report, the NAB 2016 Full Year Results and the NAB 2016 Full Year Pillar 3 Report, NZD$823 million of Bank of New Zealand's dairy exposures were classified as impaired with no loss, some of which were not past due as at 30 September 2016. The definition of Individually Impaired Assets applied in the table above aligns to New Zealand regulatory requirements. It differs to the definition of Impaired Assets as set out in Prudential Standard APS 220 by APRA. This APRA definition is used for reporting purposes by the Bank's ultimate parent, NAB in its Pillar 3 report. Under the APRA definition, Impaired Assets include Individually Impaired Assets and also certain exposures that are in default (but for which no loss is expected) where recovery timeframes are expected to be longer than usual.

Note 13 Asset Quality *continued*

Included in contingent liabilities in note 36 are $1 million of off-balance sheet facilities to counterparties for whom drawn balances were classified as individually impaired as at 30 September 2016 (30 September 2015: $2 million). No specific provision for doubtful debt on individual off-balance sheet credit related commitments had been made as at 30 September 2016 (30 September 2015: nil).

	Consolidated			
	Residential Mortgage Lending	Other Retail Exposures	Corporate Exposures	Total
Dollars in Millions	30/9/16	30/9/16	30/9/16	30/9/16
Past due assets not impaired				
Loans and advances to customers				
1 - 7 days past due	102	43	201	346
8 - 29 days past due	68	46	60	174
1 - 29 days past due	170	89	261	520
30 - 59 days past due	52	14	32	98
60 - 89 days past due	23	6	28	57
90+ days past due	33	17	123	173
Total past due assets not impaired	278	126	444	848
	Consolidated (30/9/15)			
Past due assets not impaired				
Loans and advances to customers				
1 - 7 days past due	131	50	273	454
8 - 29 days past due	87	65	63	215
1 - 29 days past due	218	115	336	669
30 - 59 days past due	58	18	46	122
60 - 89 days past due	35	10	16	61
90+ days past due	45	23	128	196
Total past due assets not impaired	356	166	526	1,048

The credit quality of assets that are neither past due nor impaired has been classified using the Banking Group's internal customer rating system and credit monitoring procedures required under internal policies, and in accordance with the RBNZ's Basel III capital adequacy framework. Refer to note 41 for further information on the Banking Group's credit policies.

Note 14 Derivative Financial Instruments

Derivative financial instruments are financial instruments whose value is dependent on the value of an underlying financial asset or a combination of assets. The fair value of derivative financial instruments are obtained from quoted market prices, discounted cash flow models or option pricing models as appropriate.

Derivative financial instruments held or issued for trading purposes

The Banking Group maintains trading positions in a variety of derivative financial instruments and acts primarily in the market by satisfying the needs of its customers through foreign exchange, interest rate related services and other market related contracts. In addition, the Banking Group takes positions on its own account within a prescribed limit framework, to manage its exposure to market and credit risks relating to trading activities. It satisfies customer needs and maintains access to market liquidity by quoting bid and offer prices on those instruments and trading with other market makers. All positions held for trading purposes are revalued on a daily basis to reflect market movements and any revaluation profit or loss is recognised immediately in the income statement.

Derivative financial instruments held or issued for purposes other than trading

Fair value hedges

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.

Cash flow hedges

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.

There were no transactions for which cash flow hedge accounting had to be ceased during the year ended 30 September 2016 (year ended 30 September 2015: nil) as a result of the highly probable cash flows no longer being expected to occur.

The following tables reflect the periods when the hedged cash flows are expected to occur and affect the income statement.

			Consolidated (30/9/16)			
Dollars in Millions	Less than 1 Year	1 to 2 Years	2 to 3 Years	3 to 4 Years	4 to 5 Years	Over 5 Years
Cash flow hedges						
Cash inflows - assets	119	89	62	43	12	3
Cash outflows - liabilities	(53)	(43)	(28)	(16)	(8)	(6)
Net cash inflows/(outflows)	66	46	34	27	4	(3)
			Consolidated (30/9/15)			
Cash flow hedges						
Cash inflows - assets	143	102	63	28	8	-
Cash outflows - liabilities	(13)	(3)	(1)	-	-	-
Net cash inflows	130	99	62	28	8	-

Note 14 Derivative Financial Instruments *continued*

	Consolidated		
Dollars in Millions	Notional Principal 30/9/16	Fair Value Assets 30/9/16	Fair Value Liabilities 30/9/16
Held for trading - at fair value *			
Foreign exchange rate related contracts			
Spot and forward contracts to purchase foreign exchange	64,487	641	646
Cross currency swaps	49,047	587	1,624
Options	6,004	107	106
	119,538	1,335	2,376
Interest rate related contracts			
Forward rate agreements	14,351	2	-
Swaps	395,083	5,766	5,101
Futures**	224,541	-	-
Options	322	-	-
	634,297	5,768	5,101
Other market related contracts			
Commodity derivatives	304	14	14
Credit derivatives	355	3	3
	659	17	17
Total held for trading – at fair value	754,494	7,120	7,494
Held for hedging – fair value hedges			
Interest rate related contracts			
Swaps	19,098	30	255
Total held for hedging – fair value hedges	19,098	30	255
Held for hedging – cash flow hedges			
Interest rate related contracts			
Forward rate agreements	660	1	-
Swaps	7,982	168	37
Total held for hedging – cash flow hedges	8,642	169	37
Total derivative contracts	782,234	7,319	7,786

* Held for trading derivative financial instruments include some derivatives that are used for hedging purposes that are not in designated hedge accounting relationships.
** The calculation of the notional amount reflects the gross volume of transactions outstanding at the reporting period end and is not indicative of either the market risk or credit risk.

Note 14 Derivative Financial Instruments *continued*

	Consolidated		
Dollars in Millions	Notional Principal 30/9/15	Fair Value Assets 30/9/15	Fair Value Liabilities 30/9/15
Held for trading - at fair value*			
Foreign exchange rate related contracts			
Spot and forward contracts to purchase foreign exchange	81,395	1,157	1,119
Cross currency swaps	47,818	1,378	2,036
Options	6,456	133	133
	135,669	2,668	3,288
Interest rate related contracts			
Forward rate agreements	3,560	3	-
Swaps	442,045	5,070	4,990
Futures**	242,715	-	-
Options	183	-	-
Swaptions	350	1	-
	688,853	5,074	4,990
Other market related contracts			
Commodity derivatives	640	22	22
Credit derivatives	115	-	-
	755	22	22
Total held for trading – at fair value	825,277	7,764	8,300
Held for hedging – fair value hedges ***			
Interest rate related contracts			
Swaps	-	-	-
Total held for hedging – fair value hedges	-	-	-
Held for hedging – cash flow hedges			
Interest rate related contracts			
Swaps	5,708	131	10
Total held for hedging – cash flow hedges	5,708	131	10
Total derivative contracts	830,985	7,895	8,310

* Held for trading derivative financial instruments include some derivatives that are used for hedging purposes that are not in designated hedge accounting relationships.
** The calculation of the notional amount reflects the gross volume of transactions outstanding at the reporting period end and is not indicative of either the market risk or credit risk.
*** Fair value hedges that are held for hedging but ineffective at balance date are included in the Held for trading - at fair value category.

Credit risk

The maximum exposure to credit risk at any one time is limited to the current fair value of instruments that are favourable to the Banking Group (assets where their fair value is positive), which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding. For information on the Banking Group's risk management policies, refer to note 41.

Notes to and Forming Part of the Financial Statements

Note 15 Investments in Wholly Owned Entities

Wholly owned entities of the Bank as at 30 September 2016 were:

Name	Country of Incorporation	Principal Activities
BNZ Agricapital Limited	New Zealand	Investment company
BNZ Equity Investments No.2 Limited	New Zealand	Investment company
BNZ Facilities Management Limited	New Zealand	Facilities management
BNZ International Funding Limited	New Zealand	Funding company
BNZ Investments Limited	New Zealand	Investment company
BNZ Property Investments Limited	New Zealand	Property company
BNZ Branch Properties Limited	New Zealand	Property company
BNZ Investment Services Limited	New Zealand	Investment administration and management

All wholly owned entities listed above have the same reporting date as the Bank.

Note 16 Consolidated Structured Entities

The following structured entities are consolidated for financial reporting purposes:

Name	Country of Domicile	Principal Activities
BNZ Term PIE	New Zealand	Portfolio investment entity
BNZ Cash PIE	New Zealand	Portfolio investment entity
BNZ Covered Bond Trust	New Zealand	Funding structure vehicle
BNZ RMBS Trust Series 2008-1	New Zealand	Funding structure vehicle

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
Note 17 Deferred Tax		
Deferred tax assets		
Balance at beginning of year	**153**	138
Restated for adoption of new accounting standard	**-**	20
Tax expense recognised in income statement	**26**	(5)
Balance at end of year	**179**	153
Deferred tax assets were attributable to the following items:		
Employee entitlements	**12**	17
Credit risk adjustments on financial assets designated at fair value through profit or loss	**19**	11
Provision for doubtful debts on credit exposures	**144**	124
Depreciation and amortisation	**(6)**	(12)
Operating expense provisions	**9**	8
Prepaid pension assets	**(1)**	(1)
Other	**2**	6
Total deferred tax assets	**179**	153

The recognition of the deferred tax assets relies on management's judgements about the probability and sufficiency of future taxable profits and future reversals of existing taxable temporary differences.

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
Note 18 Other Assets		
Accrued interest receivable	**127**	146
Prepaid pension assets	**5**	6
Securities sold – not yet settled	**244**	94
Other assets*	**173**	123
Total other assets	**549**	369

* Other assets includes receivables relating to prepayments and settlements clearing.

Liability Notes

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 19 Due to Central Banks and Other Institutions		
Transaction balances with other institutions*	**550**	645
Deposits from central banks	**130**	199
Deposits from other institutions**	**382**	323
Securities sold under agreements to repurchase from other institutions*	**182**	272
Total due to central banks and other institutions	**1,244**	1,439

* Classified as cash and cash equivalents in the cash flow statement.
** Included in deposits from other institutions as at 30 September 2016 was $26 million classified as cash and cash equivalents in the cash flow statement (30 September 2015: $10 million).

Included in due to central banks and other institutions as at 30 September 2016 was $284 million of collateral posted by counterparties to meet standard derivative trading obligations (30 September 2015: $331 million). The Bank held no secured deposits from central banks and other institutions as at 30 September 2016 (30 September 2015: nil).

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 20 Short Term Debt Securities		
Certificates of deposit	**2,357**	1,709
Commercial paper	**3,673**	3,318
Total short term debt securities	**6,030**	5,027

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 21 Deposits from Customers		
Demand deposits not bearing interest	**4,616**	3,688
Demand deposits bearing interest	**19,123**	18,242
Term deposits	**27,742**	24,799
Total deposits from customers	**51,481**	46,729

Included in term deposits as at 30 September 2016 was $2 million of collateral posted by counterparties to meet standard derivative trading obligations (30 September 2015: $3 million).

Dollars in Millions	Consolidated 30/9/16	Consolidated 30/9/15
Note 22 Bonds and Notes		
Domestic medium term notes	**4,084**	4,057
Offshore medium term notes	**12,639**	12,099
Total bonds and notes	**16,723**	16,156

Details of the terms and conditions of these notes as at 30 September 2016 were as follows:

Issue Currency	Coupon Rate %	Maturity Date	Face Value Issue Currency Millions* 30/9/16	Fair Value NZ $Millions 30/9/16	Face Value Issue Currency Millions* 30/9/15	Fair Value NZ $Millions 30/9/15
Medium term notes issued by Bank of New Zealand:						
New Zealand dollar	3 month NZD BKBM + 32bp	26 February 2016	-	-	200	201
New Zealand dollar	7.465 (fixed)	27 May 2016	-	-	50	53
New Zealand dollar	3 month NZD BKBM + 35bp	27 May 2016	-	-	228	229
New Zealand dollar	5.730 (fixed)	15 July 2016	-	-	180	185
New Zealand dollar	6.905 (fixed)	15 September 2016	-	-	100	104
New Zealand dollar	6.425 (fixed)	30 June 2017**	**250**	**262**	248	266
New Zealand dollar	5.773 (fixed)	19 January 2018**	**350**	**368**	350	374
New Zealand dollar	3 month NZD BKBM + 75bp	26 February 2018	**100**	**100**	-	-
New Zealand dollar	4.680 (fixed)	28 March 2018	**94**	**97**	100	103
New Zealand dollar	3 month NZD BKBM + 121bp	28 March 2018	**250**	**252**	250	254
New Zealand dollar	3 month NZD BKBM + 77bp	26 April 2018	**100**	**101**	-	-
New Zealand dollar	3 month NZD BKBM	17 December 2018	**117**	**117**	106	105
New Zealand dollar	6.100 (fixed)	20 December 2018	**500**	**544**	500	548
New Zealand dollar	3 month NZD BKBM + 127bp	31 March 2019**	**300**	**304**	300	308
New Zealand dollar	5.570 (fixed)	25 June 2019	**694**	**753**	691	747
New Zealand dollar	4.426 (fixed)	18 June 2020	**575**	**609**	562	580
New Zealand dollar	4.261 (fixed)	3 February 2023**	**300**	**318**	-	-
New Zealand dollar	4.102 (fixed)	15 June 2023	**249**	**259**	-	-
				4,084		4,057

* Face value represents current value on issue held by the market.

** These notes are guaranteed by the trustee of the Covered Bond Trust. Refer to the Guarantees section on page 2 and note 11 for further information.

Note 22 Bonds and Notes *continued*

Issue Currency	Coupon Rate %	Maturity Date	Face Value Issue Currency Millions* 30/9/16	Fair Value NZ $Millions 30/9/16	Face Value Issue Currency Millions* 30/9/15	Fair Value NZ $Millions 30/9/15
Medium term notes issued by BNZ-IF						
US Dollar	3 month USD LIBOR + 130bp	17 November 2015	-	-	10	16
British Pound	3 month GBP LIBOR + 70bp	29 January 2016	-	-	250	598
US Dollar	3 month USD LIBOR + 65bp	22 April 2016	-	-	80	126
US Dollar	1.0725 (fixed)	30 April 2016	-	-	20	31
Australian Dollar	6.250 (fixed)	14 June 2016**	-	-	700	805
Hong Kong Dollar	3 month HIBOR + 51.6bp	12 July 2016	-	-	775	157
Euro	4.000 (fixed)	8 March 2017	750	1,205	750	1,427
Japanese Yen	1.150 (fixed)	23 March 2017	1,000	14	1,000	13
US Dollar	3 month USD LIBOR + 150bp	24 May 2017	15	21	15	24
Japanese Yen	3 month JPY LIBOR + 100bp	26 July 2017	11,400	157	11,400	153
Japanese Yen	1.260 (fixed)	26 July 2017	14,100	194	14,100	190
Euro	3.125 (fixed)	23 November 2017**	1,000	1,641	1,000	1,933
Swiss Franc	1.500 (fixed)	22 January 2018	225	332	225	381
Hong Kong Dollar	1.375 (fixed)	26 January 2018	780	139	780	157
US Dollar	1.900 (fixed)	26 February 2018	600	832	600	947
Japanese Yen	3 month JPY LIBOR + 27bp	13 March 2018	2,000	27	2,000	26
US Dollar	3 month USD LIBOR + 80bp	23 April 2018	10	14	10	16
Euro	1.250 (fixed)	23 May 2018	500	794	500	907
US Dollar	3 month USD LIBOR + 45bp	20 August 2018	10	14	10	16
US Dollar	3 month USD LIBOR + 82bp	26 November 2018	10	14	10	16
Japanese Yen	0.4700 (fixed)	27 November 2018	2,000	27	2,000	26
US Dollar	3 month USD LIBOR + 75bp	13 December 2018	10	14	10	15
US Dollar	2.2825 (fixed)	13 December 2018	10	14	10	16
US Dollar	2.350 (fixed)	4 March 2019	1,000	1,400	1,000	1,584
US Dollar	3 month USD LIBOR + 32bp	20 March 2019	100	137	100	155
Swiss Franc	1.125 (fixed)	20 September 2019	275	407	275	464
US Dollar	3 month USD LIBOR + 72bp	24 October 2019	100	138	100	157
Euro	3 month EURIBOR + 50bp	2 December 2019	550	854	550	971
Hong Kong Dollar	3.480 (fixed)	8 September 2020	53	9	53	11
New Zealand Dollar	6.590 (fixed)	30 September 2020	50	56	50	56
Swiss Franc	1.375 (fixed)	3 February 2021	200	307	200	349
Japanese Yen	0.1775 (fixed)	12 February 2021	17,000	230	-	-
Hong Kong Dollar	2.500 (fixed)	1 March 2021	233	40	-	-
US Dollar	2.750 (fixed)	2 March 2021	500	710	-	-
Hong Kong Dollar	2.320 (fixed)	31 March 2021	180	32	-	-
Hong Kong Dollar	2.350 (fixed)	31 March 2021	169	27	-	-
Hong Kong Dollar	2.560 (fixed)	31 March 2021	125	22	-	-
US Dollar	3 month USD LIBOR + 114bp	19 May 2021	30	42	-	-
US Dollar	3 month USD LIBOR + 105bp	15 June 2021	10	14	-	-
Euro	0.125 (fixed)	17 June 2021**	750	1,174	-	-
Hong Kong Dollar	2.060 (fixed)	22 June 2021	160	27	-	-
US Dollar	3 month USD LIBOR + 100bp	28 June 2021	10	14	-	-
US Dollar	3 month USD LIBOR + 100bp	22 July 2021	20	28	-	-
US Dollar	2.100 (fixed)	14 September 2021	600	826	-	-
US Dollar	3 month USD LIBOR + 98bp	14 September 2021	250	344	-	-
Swiss Franc	0.250 (fixed)	24 June 2022	200	290	200	323
Euro	0.685 (fixed)	28 July 2025	20	30	-	-
Australian Dollar	4.000 (fixed)	30 September 2025	30	28	30	33
				12,639		12,099

* Face value represents current value on issue held by the market.
** These notes are guaranteed by the trustee of the Covered Bond Trust. Refer to the Guarantees section on page 2 and note 11 for further information.

Dollars in Millions	Consolidated 30/9/16	30/9/15
Note 23 Other Liabilities		
Accrued interest payable	**282**	289
Payables and accrued expenses	**95**	81
Securities purchased – not yet settled	**232**	277
Employee entitlements	**115**	111
Other liabilities*	**85**	105
Total other liabilities	**809**	863

* Other liabilities includes payables relating to settlements clearing.

Note 24 Subordinated Debt

The following subordinated debt is subordinated to all other indebtedness of the Bank. The subordinated debt constitutes Tier Two capital for RBNZ capital adequacy purposes as follows:

Dollars in Millions	Consolidated 30/9/16	30/9/15
Subordinated loans due to related entities		
NAB Capital LLC	**150**	230
National Equities Limited	**230**	485
Total subordinated loans due to related entities	**380**	715
Other subordinated debt		
Subordinated notes due to external investors	**542**	-
Total other subordinated debt	**542**	-
Total subordinated debt	**922**	715

Subordinated loans due to related entities of $380 million as at 30 September 2016 have no fixed maturity and are repayable on five years and one day's notice by the holder. These are also repayable at the Bank's option, subject to certain conditions at any time on seven days' notice. The interest rate is reset every three months based on a margin over the prevailing rate for New Zealand 90-day bank bills. Subordinated loans due to related entities of $335 million were repaid in June 2016.

On 17 December 2015, the Bank issued $550 million of subordinated unsecured notes ("Subordinated Notes"), which are currently quoted on the NZX Debt Market under the ticker code BNZ090. The Subordinated Notes are treated as Tier Two capital under the Bank's and National Australia Bank Limited's regulatory capital requirements. The Subordinated Notes will mature on 17 December 2025 ("Maturity Date"), subject to the Bank's option repay some or all of the Subordinated Notes on any scheduled interest payment date on or after 17 December 2020 ("Optional Redemption Date"). At any time, the Bank may repay all (but not some only) of the Subordinated Notes if a regulatory or tax event occurs. The initial interest rate for the Subordinated Notes was 5.314% per annum, which was fixed for five years and will be reset on the Optional Redemption Date. From the Optional Redemption Date to the Maturity Date, the interest rate will be the sum of the Five Year Swap Rate (a benchmark interest rate for a term of five years) on the Optional Redemption Date plus 2.250% per annum. Interest is scheduled to be paid quarterly in arrear subject to the Bank being solvent (by satisfying the solvency test in section 4 of the Companies Act 1993) on the relevant payment date and remaining solvent immediately after making the payment. If the Bank does not pay an amount on the Subordinated Notes because it has not satisfied the solvency test, the Bank must pay that amount on the first date on which it is able to make the payment and satisfy the solvency test. Interest will accrue daily (at the interest rate then applicable to the Subordinated Notes) on any interest that is not paid when scheduled as a result of the Bank not satisfying the solvency test on the relevant payment date. If some or all of the Subordinated Notes are converted or written off, any rights to receive interest on those Subordinated Notes (including any accrued but unpaid interest) are also terminated and written off.

If a non-viability trigger event ("NVTE") occurs, some or all of the Subordinated Notes will automatically and immediately be converted to National Australia Bank Limited ordinary shares or written off. A NVTE will occur if: (i) the RBNZ gives the Bank a direction under the Reserve Bank of New Zealand Act 1989 ("RBNZ Act") requiring the Bank to exercise its right of conversion or write off of its Tier Two capital instruments; (ii) the Bank is made subject to statutory management under the RBNZ Act and the New Zealand statutory manager announces his or her decision to convert or write off the Bank's Tier Two capital instruments; or (iii) APRA has provided a written determination to National Australia Bank Limited that without the conversion or write off of a class of capital instruments of National Australia Bank Limited which includes the Subordinated Notes, or a public sector injection of capital into, or equivalent capital support with respect to, National Australia Bank Limited, APRA considers that National Australia Bank Limited would become non-viable. The RBNZ may give the Bank a direction that affects the Subordinated Notes under the RBNZ Act if the RBNZ has reasonable grounds to believe, based on the Bank's financial position, that: (a) the Bank is insolvent or is likely to become insolvent; (b) the Bank is about to suspend payment or is unable to meet its obligations as and when they fall due; (c) the affairs of the Bank are being conducted in a manner prejudicial to the soundness of the financial system; (d) the circumstances of the Bank are such as to be prejudicial to the soundness of the financial system; or (e) the business of the Bank has not been, or is not being, conducted in a prudent manner.

If the Subordinated Notes are not converted or written off, in a liquidation of the Bank, the holder's right to claim payment on the Subordinated Notes will rank: (a) ahead of claims of holders of ordinary shares of the Bank and securities that rank below the Subordinated Notes; (b) equally with claims of other holders of the Subordinated Notes and holders of other securities that rank equally with the Subordinated Notes with respect to priority of payment in a liquidation; and (c) behind all other claims (such as those of the Bank's secured creditors, depositors and holders of unsecured unsubordinated bonds issued by the Bank from time to time).

In connection with the Subordinated Notes, a Coordination Agreement dated 11 November 2015 between the Bank, National Australia Group (NZ) Limited ("NAGNZ"), National Equities Limited and National Australia Bank Limited sets out intragroup transactions that are intended to occur on conversion of the Subordinated Notes. Under this agreement, the Bank is required to issue a variable number of ordinary shares to NAGNZ for an amount equivalent to the Subordinated Notes converted into National Australia Bank Limited ordinary shares.

Shareholders' Equity Notes

Number of shares in Millions	Consolidated 30/9/16	30/9/15
Note 25 Contributed Equity		
Issued and paid-up shares		
Ordinary shares, fully paid – balance at beginning of year	**3,371**	2,871
Ordinary shares issued during the year	**-**	500
Ordinary shares, fully paid – balance at end of year	**3,371**	3,371
Perpetual preference shares, fully paid – balance at beginning of year	**650**	650
Buyback of shares	**(450)**	-
Perpetual preference shares, fully paid – balance at end of year	**200**	650
Total issued and paid-up shares	**3,571**	4,021

The issued and paid-up capital is included in Tier One capital of the Banking Group and the Registered Bank (refer to note 40).

Ordinary shares

The authorised ordinary share capital of the Bank comprises 3,370,997,499 shares with a balance of $2,351 million (30 September 2015: 3,370,997,499 shares; $2,351 million), which do not have a par value. All issued shares were fully paid as at the reporting date. Each of the 3,370,997,499 ordinary shares entitles the shareholder to one vote at any meeting of shareholders.

Dividends on ordinary shares for the year ended 30 September 2016 were 14.83 cents per share (year ended 30 September 2015: 11.01 cents per share).

Perpetual non-cumulative preference shares

The perpetual non-cumulative preference share capital of the Bank comprises 200,000,000 shares (30 September 2015: 649,730,000 shares), which do not have a par value. All issued shares were fully paid as at the reporting date.

Each of the 200,000,000 perpetual non-cumulative preference shares is non-redeemable and carries no voting rights other than in relation to amendments of the rights, privileges, limitations and conditions attaching to these shares.

March 2008 issue

On 28 September 2016, the Bank bought back the $450 million of perpetual non-cumulative preference shares ("2008 BNZ PPS") issued to BNZ Income Management Limited ("BNZIM") on 28 March 2008.

Dividends on the 2008 BNZ PPS for the year ended 30 September 2016 were 4.05 cents per share (year ended 30 September 2015: 4.05 cents per share).

December 2009 issue

On 29 December 2009, the Bank issued 200,000,000 perpetual non-cumulative preference shares ("2009A BNZ PPS") to NAGNZ, the Bank's immediate parent and a subsidiary of the Bank's ultimate parent, National Australia Bank Limited.

The 2009A BNZ PPS were issued in conjunction with the making of a loan by National Australia Bank Limited, acting through its New York branch, to NAGNZ. NAGNZ invested the proceeds of the loan in the 2009A BNZ PPS.

The 2009A BNZ PPS are non-redeemable and carry no voting rights other than in relation to amendments of the rights, privileges, limitations and conditions attaching to the 2009A BNZ PPS. Dividends are payable quarterly in arrears, but are non-cumulative if dividends are not paid for the reasons set out below.

The dividend payable on the 2009A BNZ PPS is determined by reference to the seven-year mid-market swap rate plus a margin of 3.50% per annum. The initial rate was set at 9.25% per annum on 23 December 2009, applicable for the period from (and including) 29 December 2009 to (but excluding) 28 December 2016. Dividend rates are to be reset seven-yearly on the business day falling two business days before 28 December (or the applicable business day if 28 December is not a business day) in the relevant year. The first dividend reset date is 22 December 2016.

Dividends will not be paid on the 2009A BNZ PPS if any of the following conditions apply: (a) the Directors of the Bank in their sole discretion do not resolve to pay the dividend on the relevant dividend payment date; (b) such a payment would result in the Bank's Tier One capital ratio ceasing to comply with the RBNZ's then current capital adequacy requirements; or (c) the Directors of the Bank are not satisfied that the Bank will be solvent (under the solvency test set out in section 4 of the Companies Act 1993) immediately after payment of the dividend.

If the Bank does not pay a dividend on the 2009A BNZ PPS on a scheduled dividend payment date (for whatever reason), then the Bank must not make any other distribution or payment on or with respect to its other shares that rank equally with or junior to the 2009A BNZ PPS (other than pro-rata distributions or payments on shares that rank equally with the 2009A BNZ PPS) unless and until it has paid two consecutive dividends in full on the 2009A BNZ PPS.

Dividends on the 2009A BNZ PPS rank for payment:

- before the Bank's ordinary shareholder;
- equally with any other shares issued by the Bank that, by their terms, are expressed to rank equally with the 2009A BNZ PPS; and
- after all other shareholders and creditors of the Bank.

Dividends on the 2009A BNZ PPS for the year ended 30 September 2016 were 6.66 cents per share (year ended 30 September 2015: 6.66 cents per share).

In the event of liquidation of the Bank, the 2009A BNZ PPS rank:

- before the Bank's ordinary shareholder;
- equally with any other shares issued by the Bank that, by their terms, are expressed to rank equally with the 2009A BNZ PPS; and
- after all other shareholders and creditors of the Bank.

Refer to note 42 for further information.

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Note 26 Reserves		
Asset revaluation reserve	2	2
Cash flow hedge reserve	113	94
Total reserves	115	96
Total reserves comprised:		
Asset revaluation reserve		
Balance at beginning of year	2	2
Balance at end of year	2	2
Cash flow hedge reserve		
Balance at beginning of year	94	(19)
Transferred to interest income in the income statement	(262)	(260)
Transferred to interest expense in the income statement	224	242
Net gains from changes in fair value	57	131
Balance at end of year	113	94
Total reserves	115	96

The asset revaluation reserve includes gross revaluation increments and any subsequent decrements arising from the revaluation of property, plant and equipment.

The cash flow hedge reserve records the effective portion of fair value revaluations of derivatives designated as cash flow hedge accounting relationships.

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Note 27 Retained Profits		
Balance at beginning of year	3,945	3,257
Balance adjusted for adoption of accounting standard	-	(61)
Net profit attributable to shareholders of Bank of New Zealand	913	1,038
Actuarial gain/(loss) on defined benefit plan	(1)	(2)
Credit risk adjustments on financial liabilities designated at fair value through profit or loss	19	125
Current tax on credit risk adjustments on financial liabilities designated at fair value through profit or loss	(5)	(35)
Ordinary dividend	(500)	(345)
Perpetual preference dividend	(32)	(32)
Balance at end of year	4,339	3,945

Other Notes

Note 28 Imputation Credit Account

The amount of imputation credits available to the Banking Group as at 30 September 2016 was $1,712 million (30 September 2015: $1,529 million).

Note 29 Interest Earning and Discount Bearing Assets and Liabilities and Ranking of Liabilities

Ranking of liabilities

The Bank held no secured deposits from central banks as at 30 September 2016 (30 September 2015: nil). All deposits reported in these financial statements by the Banking Group are unsecured and rank equally with the Banking Group's other unsecured liabilities. Included in liabilities are obligations of the Bank under repurchase agreements where the Bank has agreed to repurchase $182 million of government stock (30 September 2015: $272 million).

As at 30 September 2016, $139 million (30 September 2015: $150 million) of certain unsecured liabilities rank in priority to general creditors' claims in a winding up of the Bank. Certain debt securities are guaranteed by the trustee of the Covered Bond Trust. Further details on the Covered Bond Trust are provided on page 2 and in note 11. Subordinated debt with a carrying value totalling $922 million as at 30 September 2016 (30 September 2015: $715 million) ranks behind the claims of all other creditors in a winding up. No residential mortgage-backed securities were used as collateral securities as at 30 September 2016 (30 September 2015: nil).

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Interest earning and discount bearing assets*	82,439	76,456
Interest and discount bearing liabilities	72,230	66,746

* September 2015 restated due to change in methodology of interest earning assets to exclude mortgage offset accounts.

Note 30 Related Entity Transactions

The Bank is a wholly owned controlled entity of NAGNZ. The ultimate parent bank of Bank of New Zealand is National Australia Bank Limited. During the year ended 30 September 2016, there were dealings between the Bank and its related entities (including NAB) as well as other related parties (including key management personnel, their close family members and their controlled entities). Details of these transactions are outlined on pages 43 to 45.

Dealings with NAB included on-balance sheet activities such as funding and accepting deposits and other activities such as foreign exchange transactions.

Related entities

Total balances with related entities

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Amounts due from ultimate parent	707	1,009
Amounts due from controlled entities of ultimate parent	227	250
Total amounts due from related entities	934	1,259
Derivative financial assets with related entities	1,739	2,135
Amounts due to ultimate parent	69	36
Amounts due to controlled entities of ultimate parent	365	344
Total amounts due to related entities	434	380
Subordinated loans due to related entities (refer to note 24)	380	715
Derivative financial liabilities with related entities	2,227	2,562

No provisions have been recognised in respect of loans provided to related entities (year ended 30 September 2015: nil). There were no debts with any of the above parties written off or forgiven during the year ended 30 September 2016 (year ended 30 September 2015: nil).

Note 30 Related Entity Transactions *continued*

Related entities *continued*

Included within the amounts due from and due to related entities were the following balances:

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Amounts due from related entities		
Collateral loan posted to ultimate parent to meet standard derivative trading obligations	483	451
Securities purchased under agreements to resell to ultimate parent	135	545
Amounts due to related entities		
Intercompany payable in respect of share based payments included in amounts due to ultimate parent	7	5
Securities sold under agreements to repurchase from ultimate parent	54	-

Included within the amounts classified as cash and cash equivalents in the cash flow statement were the following balances with related entities:

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Amounts due from related entities	239	593
Amounts due to related entities	404	335

Transactions with related entities

The Banking Group provides banking and other administrative services to members of NAB operating in New Zealand at arm's length and on normal terms and conditions.

During the financial year, there have been dealings between the Bank and its controlled entities, and the Banking Group and its related entities. The Bank provides a range of services to related entities including the provision of banking facilities. These transactions are normally subject to commercial terms and conditions. The Bank provides some accounting administration and banking services to controlled entities for which fees may not be charged.

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Interest income on amounts due from related entities		
Ultimate parent	28	2
Controlled entities of ultimate parent	7	10
Total interest income on amounts due from related entities	35	12
Interest expense on amounts due to related entities		
Ultimate parent	7	7
Controlled entities of ultimate parent	26	37
Total interest expense on amounts due to related entities	33	44
Other operating income		
Collection services income from ultimate parent	-	2
Unrealised gains on derivative contracts with ultimate parent	1,739	2,135
Unrealised losses on derivatives contracts with ultimate parent	(2,227)	(2,562)
Commissions received from controlled entities of ultimate parent for sale of insurance	21	19
Operating expenses		
Intercompany recharges paid to ultimate parent	31	47
Other service charges paid to ultimate parent	5	5
Other transactions		
Payments for the use of tax losses to controlled entities of ultimate parent	32	31

Dividends paid to the shareholders are disclosed in note 27.

For the year ended 30 September 2016, $12 million of imputation credits from the group imputation credit account (year ended 30 September 2015: $11 million) were attached to dividends paid by National Wealth Management New Zealand Holdings Limited, a controlled entity of the Bank's ultimate parent.

Note 30 Related Entity Transactions *continued*

Related entities *continued*

The BNZ KiwiSaver Scheme (the "Scheme") is a voluntary retirement savings scheme. BNZ Investment Services Limited ("BNZISL"), a wholly owned controlled entity of the Bank, is the Manager and Issuer of the Scheme. The Scheme's banking arrangements are provided by the Bank. The Scheme currently invests in, among other things, bank deposits with the Bank. As at 30 September 2016, the Scheme held $11 million in the transactional bank accounts (30 September 2015: $185 million). Further information is included in note 39.

The RMBS Trust provides an internal residential mortgage-backed securities programme. As at 30 September 2016, included in the Bank's financial statements is an intercompany payable and an intercompany receivable which are eliminated on consolidation. Further details on the RMBS Trust are provided in notes 11, 16, 34, 39 and 41.

The Covered Bond Trust holds certain Bank of New Zealand housing loans and its trustee guarantees covered bonds issued by the Bank and BNZ-IF. As at 30 September 2016, included in the Bank's financial statements is an intercompany payable and an intercompany receivable of equal amount which are eliminated on consolidation. Further details on the Covered Bond Trust are provided in notes 11, 16, 22, 34 and 39.

The Bank guarantees the obligations of BNZ-IF, in respect of securities issued by BNZ-IF to wholesale investors. Refer to note 36 for further information.

As at 30 September 2016, there was an A$1,000 million standby liquidity facility (30 September 2015: A$1,250 million) provided from National Australia Bank Limited for the Banking Group's liquidity management. Fees for the provision of this facility are charged at 0.40% per annum. From 1 October 2016, this standby liquidity facility was reduced to A$500 million. Funds will be made available for a term not exceeding 90 days, or at a term to be agreed with National Australia Bank Limited at the time of usage.

Key management personnel

Key management personnel are defined as being Directors and the executive team of the Banking Group. The information relating to key management personnel disclosed below includes transactions with those individuals, their close family members and their controlled entities.

Loans and deposits with non-executive key management personnel of the Banking Group are made in the ordinary course of business on commercial terms and conditions. Loans and deposits with executive key management personnel of the Banking Group are made either:

- on normal terms and conditions; or
- on terms and conditions which apply to other employees in the Banking Group.

All loans made to key management personnel have been made in accordance with the Banking Group's lending policies.

Amounts due from key management personnel

Included in loans and advances to customers were the following amounts due from key management personnel:

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
Loans outstanding at end of year	**10**	10
Interest income on amounts due from key management personnel	**-**	1

Interest income on amounts due from key management personnel for the year ended 30 September 2016 is shown as nil in the table above as a result of rounding to the nearest million.

No provisions have been recognised in respect of loans provided to key management personnel. There were no debts written off or forgiven during the year ended 30 September 2016 (year ended 30 September 2015: nil).

Amounts due to key management personnel

Included in deposits from customers were the following amounts due to key management personnel:

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
Deposits at end of year	**7**	8
Interest expense on amounts due to key management personnel	**-**	-

Interest expense on amounts due to key management personnel is shown as nil in the table above as a result of rounding to the nearest million.

Other transactions with key management personnel

The remuneration paid or payable to the Directors and other key management personnel is outlined in note 5.

Note 31 Categories of Financial Assets and Financial Liabilities

Fair value is the price 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 under current market conditions. For the purposes of this note, carrying amount refers to amounts reflected in the balance sheet. The methodologies and assumptions used in the fair value estimates are described in note 32.

Dollars in Millions	**Consolidated (30/9/16)** Fair Value Through Profit or Loss	At Amortised Cost	Total Carrying Amount
Financial assets			
Cash and liquid assets	**-**	**1,799**	**1,799**
Due from central banks and other institutions	**1,412**	**887**	**2,299**
Trading securities	**4,703**	**-**	**4,703**
Derivative financial instruments	**7,319**	**-**	**7,319**
Loans and advances to customers	**5,562**	**68,816**	**74,378**
Amounts due from related entities	**-**	**934**	**934**
Other financial assets	**-**	**371**	**371**
Total financial assets	**18,996**	**72,807**	**91,803**

	Consolidated (30/9/15) Fair Value Through Profit or Loss	At Amortised Cost	Total Carrying Amount
Financial assets			
Cash and liquid assets	-	1,634	1,634
Due from central banks and other institutions	1,682	327	2,009
Trading securities	4,918	-	4,918
Derivative financial instruments	7,895	-	7,895
Loans and advances to customers	7,133	61,083	68,216
Amounts due from related entities	-	1,259	1,259
Other financial assets	-	240	240
Total financial assets	21,628	64,543	86,171

Dollars in Millions	**Consolidated (30/9/16)** Fair Value Through Profit or Loss	At Amortised Cost	Total Carrying Amount
Financial liabilities			
Due to central banks and other institutions	**512**	**732**	**1,244**
Short term debt securities	**6,030**	**-**	**6,030**
Trading liabilities	**72**	**-**	**72**
Derivative financial instruments	**7,786**	**-**	**7,786**
Deposits from customers	**6,193**	**45,288**	**51,481**
Bonds and notes	**16,723**	**-**	**16,723**
Amounts due to related entities	**-**	**434**	**434**
Other financial liabilities	**-**	**599**	**599**
Subordinated debt	**-**	**922**	**922**
Total financial liabilities	**37,316**	**47,975**	**85,291**

	Consolidated (30/9/15) Fair Value Through Profit or Loss	At Amortised Cost	Total Carrying Amount
Financial liabilities			
Due to central banks and other institutions	522	917	1,439
Short term debt securities	5,027	-	5,027
Trading liabilities	51	-	51
Derivative financial instruments	8,310	-	8,310
Deposits from customers	3,875	42,854	46,729
Bonds and notes	16,156	-	16,156
Amounts due to related entities	-	380	380
Other financial liabilities	-	566	566
Subordinated debt	-	715	715
Total financial liabilities	33,941	45,432	79,373

Note 32 Fair Value of Financial Assets and Financial Liabilities

Difference between carrying amount and contractual amount on financial liabilities designated at fair value through profit or loss on initial recognition

	Consolidated (30/9/16)		
Dollars in Millions	Carrying Amount	Contractual Amount	Higher/ (Lower)
Due to central banks and other institutions	**512**	**511**	**1**
Short term debt securities	**6,030**	**6,036**	**(6)**
Deposits from customers	**6,193**	**6,169**	**24**
Bonds and notes	**16,723**	**16,222**	**501**
	29,458	**28,938**	**520**
	Consolidated (30/9/15)		
Due to central banks and other institutions	522	521	1
Short term debt securities	5,027	5,035	(8)
Deposits from customers	3,875	3,863	12
Bonds and notes	16,156	15,536	620
	25,580	24,955	625

Movements in fair value of financial liabilities designated at fair value through profit or loss on initial recognition attributable to changes in credit risk

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Bonds and notes		
Balance at beginning of year	**89**	211
Movement during the year	**(19)**	(122)
Balance at end of year	**70**	89

The movement in fair value attributable to changes in the credit risk of financial liabilities designated at fair value through profit or loss is determined as the amount of change in fair value that is not attributable to changes in market conditions that give rise to market risk.

Hierarchy for fair value measurements

The tables on page 48 present a three level fair value hierarchy of the Banking Group's financial assets and financial liabilities which are measured at fair value or amortised cost. The fair value of the financial assets and financial liabilities are considered to approximate the carrying value disclosed in the balance sheet with the exception of loans and advances to customers, deposits from customers and subordinated debt. Financial assets and financial liabilities are measured at amortised cost where the carrying value does not equal fair value.

The three levels in the hierarchy are based on the valuation methods and assumptions used in determining the fair values of financial assets and financial liabilities. The levels are as follows:

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 (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3. Inputs for the asset or liability that are not based on observable market data (unobservable inputs). The Banking Group did not have any financial assets or financial liabilities measured at fair value that met the criteria of Level 3 classification.

Management uses its judgement in selecting an appropriate valuation technique for financial instruments which are not quoted in an active market.

The Banking Group considers transfers between levels of the fair value hierarchy, if any, to have occurred at the beginning of the respective reporting period.

In the current reporting period listed subordinated debt, previously classified as Level 2, has now been classified as Level 1. There were no transfers between any of the levels for the year ended 30 September 2015.

Note 32 Fair Value of Financial Assets and Financial Liabilities *continued*

Dollars in Millions	Carrying Value	Total	Level 1	Level 2	Level 3
		Consolidated (30/9/16)			
Financial assets at fair value					
Due from central banks and other institutions		1,412	-	1,412	-
Trading securities		4,703	3,241	1,462	-
Derivative financial instruments		7,319	-	7,319	-
Loans and advances to customers		5,562	-	5,562	-
Financial assets at amortised cost					
Loans and advances to customers	68,816	69,093	-	2,387	66,706
Financial liabilities at fair value					
Due to central banks and other institutions		512	-	512	-
Short term debt securities		6,030	-	6,030	-
Trading liabilities		72	72	-	-
Derivative financial instruments		7,786	-	7,786	-
Deposits from customers		6,193	-	6,193	-
Bonds and notes		16,723	-	16,723	-
Financial liabilities at amortised cost					
Deposits from customers	45,288	45,507	-	45,507	-
Subordinated debt*	542	564	564	-	-
		Consolidated (30/9/15)			
Financial assets at fair value					
Due from central banks and other institutions		1,682	-	1,682	-
Trading securities		4,918	2,656	2,262	-
Derivative financial instruments		7,895	-	7,895	-
Loans and advances to customers		7,133	-	7,133	-
Financial assets at amortised cost					
Loans and advances to customers	61,083	61,432	-	2,400	59,032
Financial liabilities at fair value					
Due to central banks and other institutions		522	-	522	-
Short term debt securities		5,027	-	5,027	-
Trading liabilities		51	51	-	-
Derivative financial instruments		8,310	-	8,310	-
Deposits from customers		3,875	-	3,875	-
Bonds and notes		16,156	-	16,156	-
Financial liabilities at amortised cost					
Deposits from customers	42,854	43,122	-	43,122	-

* This amount represents subordinated notes due to external investors.

Note 32 Fair Value of Financial Assets and Financial Liabilities *continued*

The fair value estimates are based on the following methodologies and assumptions:

Due from central banks and other institutions, Due to central banks and other institutions and Short term debt securities

These assets and liabilities are primarily short term in nature or are receivable or payable on demand. In such cases the carrying amounts approximate their fair value or have been determined using discounted cash flow models based on observable market prices as appropriate.

Trading securities and Trading liabilities

Trading securities include treasury bills, bank bills and bonds, promissory notes, and government and other securities. Trading liabilities include short sales of securities. Where quoted market prices are not available, the Banking Group obtains the fair value by means of discounted cash flows and other valuation techniques based on observable market prices. These techniques have accounted for factors such as interest rates, credit risk and liquidity.

Derivative financial instruments

The fair values of trading and hedging derivatives, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from observable market prices as at the reporting date, discounted cash flow models or option pricing models as appropriate.

Loans and advances to customers

The carrying value of loans and advances is net of allowance for impairment losses, credit risk adjustments, unearned and deferred income. Floating rate loans to customers generally reprice within six months, therefore, their fair value is assumed to equate to their carrying value. For fixed rate loans, the fair value is estimated by discounting the expected future cash flows based on the maturity of the loans and advances, using current market interest rates of similar types of loans and advances or interest rate swap rates. The differences between estimated fair values of loans and advances and carrying value reflect the difference between observable market interest rates and customer rates on day one and changes in interest rates and creditworthiness of borrowers since loan or advance origination.

Deposits from customers

With respect to deposits from customers, the fair value of non-interest-bearing, call and variable rate deposits and fixed rate deposits repricing within six months is approximated as the carrying value as at the reporting date. For other fixed rate term deposits, the fair value is estimated by discounting the cash flows based on the maturity of the deposit, using current market interest rates.

Bonds and notes

Bonds and notes are recorded at fair value based on a discounted cash flow model using a yield curve appropriate to the remaining maturity of the instruments. This is based on observable market prices as at the reporting date where available, otherwise alternative observable market source data is used. The fair value includes a calculation of the Banking Group's own credit risk based on observable market data.

Subordinated debt

Subordinated loans due to related entities reprice every 90 days, therefore, their fair value is considered to approximate their carrying value. The fair value of subordinated notes due to external investors is based on quoted closing market prices as at the reporting date.

Other financial assets/liabilities

These include securities sold/purchased but not yet settled and accrued interest. Securities sold/purchased but not yet settled and the fair value of accrued interest is approximately equal to the carrying amounts on the balance sheet due to the short term nature of the amounts.

Note 33 Offsetting Financial Assets and Financial Liabilities

Under NZ IAS 32, financial assets and financial liabilities shall be offset in the balance sheet only when two requirements are met: there is a legally enforceable right to offset the recognised amounts and an intention to either settle on a net basis or realise the asset and settle the liability simultaneously. The legal enforceable right to offset effectively settles all or partial corresponding amounts of financial assets and financial liabilities by counterparty.

The Banking Group does not offset its financial assets and financial liabilities in the balance sheet as both requirements are not met.

The table below illustrates the amounts of financial instruments that could be offset in the balance sheet and also those amounts that are subject to enforceable master netting arrangements or similar agreements (i.e. offsetting agreements and any related financial collateral). The table excludes financial instruments not subject to offset and that are only subject to collateral arrangements (e.g. Loans and Advances).

The 'Net amounts' presented in the table are not intended to represent the Banking Group's actual exposure to credit risk, as the Banking Group utilises a wide range of strategies to mitigate credit risk in addition to netting and collateral arrangements. The 'Carrying amount' is comprised of the sum of the 'Net amounts reported in balance sheet' and 'Amounts not subject to enforceable netting arrangements' included in the table below.

	Consolidated (30/9/16)								
	Amounts Subject to Enforceable Netting Arrangements								
	Effect of Offsetting on Balance Sheet			Related Amounts not Offset					
Dollars in Millions	Gross Amounts	Amounts Offset	Net Amounts Reported in Balance Sheet	Financial Instru-ments*	Non-Cash Collateral**	Cash Collateral**	Net Amount	Amounts not Subject to Enforceable Netting Arrange-ments*****	Carrying Amount
Derivative financial assets	**6,107**	**-**	**6,107**	**5,401**	**-**	**283**	**423**	**1,212**	**7,319**
Reverse repurchase agreements***	**786**	**-**	**786**	**-**	**786**	**-**	**-**	**-**	**786**
Total assets	**6,893**	**-**	**6,893**	**5,401**	**786**	**283**	**423**	**1,212**	**8,105**
Derivative financial liabilities	**7,195**	**-**	**7,195**	**5,401**	**-**	**1,757**	**37**	**591**	**7,786**
Repurchase agreements****	**236**	**-**	**236**	**-**	**236**	**-**	**-**	**-**	**236**
Total liabilities	**7,431**	**-**	**7,431**	**5,401**	**236**	**1,757**	**37**	**591**	**8,022**
	Consolidated (30/9/15)								
Derivative financial assets	6,891	-	6,891	6,030	-	290	571	1,004	7,895
Reverse repurchase agreements***	872	-	872	-	872	-	-	-	872
Total assets	7,763	-	7,763	6,030	872	290	571	1,004	8,767
Derivative financial liabilities	7,674	-	7,674	6,030	-	1,536	108	636	8,310
Repurchase agreements****	272	-	272	-	272	-	-	-	272
Total liabilities	7,946	-	7,946	6,030	272	1,536	108	636	8,582

* Financial instruments include recognised financial instruments on the balance sheet.

** Collateral amounts (cash and non-cash financial collateral) included are reflected at their fair value; however, this amount is limited to the net balance sheet exposure in order to not include any overcollateralisation.

*** Reverse Repurchase Agreements are reported in the balance sheet within Due from central banks and other institutions of $651 million (30 September 2015: $327 million) and Amounts due from related entities of $135 million (30 September 2015: $545 million) respectively, refer to notes 9 and 30 for further information.

**** Repurchase Agreements are reported in the balance sheet within Due to central banks and other institutions of $182 million (30 September 2015: $272 million) and Amounts due to related entities of $54 million (30 September 2015: nil) respectively, refer to notes 19 and 30 for further information.

***** Relate to items which do not have an enforceable netting arrangement in place or there is uncertainty as to the legal enforceability of a close out netting arrangement in a default or liquidation under the laws of a specific jurisdiction.

Derivative assets and liabilities

Derivative financial instrument contracts are typically subject to International Swaps and Derivatives Association ("ISDA") master netting agreements, as well as relevant Credit Support Annexes ("CSA") around collateral arrangements attached to those ISDA agreements, or derivative exchange or clearing counterparty agreements if contracts are settled via an exchange or clearing house.

Derivative amounts offset in the balance sheet, if any, may typically relate to some exchange and central clearing counterparty settled contracts where the Banking Group has a legal right to offset for both payments netting (i.e. in the ordinary course of business) and close out netting (i.e. upon default or insolvency). As at 30 September 2016 the Banking Group has not offset any derivative amounts in the balance sheet (30 September 2015: nil).

Financial instruments refer to amounts that are subject to relevant close out netting arrangements under a relevant ISDA agreement. Cash collateral and Non-cash collateral include amounts of cash and non-cash collateral respectively, which are either obtained or pledged, to cover the net exposure between the counterparty in the event of default or insolvency.

Reverse repurchase and repurchase agreements

Reverse repurchase and repurchase agreements will typically be subject to Global Master Repurchase Agreements ("GMRAs") or similar agreements whereby all outstanding transactions with the same counterparty can be offset and closed out upon a default or insolvency event.

When, under the relevant agreement, the Banking Group has a legal right to offset both for payments and default netting, the Banking Group will offset amounts with that counterparty in the balance sheet. As at 30 September 2016 the Banking Group has not offset any amounts relating to reverse repurchase or repurchase agreements in the balance sheet (30 September 2015: nil).

Where the Banking Group has a right of offset on default or insolvency only, the related financial instrument amounts represents highly liquid securities either obtained or pledged, which can be realised in the event of a default or insolvency by one of the counterparties. The value of such securities obtained or pledged must at least equate to the value of the exposure to the counterparty, therefore, the net exposure is considered to be nil.

Note 34 Transfers of Financial Assets

A financial asset is considered to be transferred when the Bank transfers the contractual rights to receive the cash flows of the asset, or retains the contractual rights to receive the cash flows with a contractual obligation to pay the cash flows to another party.

Transfers of financial assets that have not been derecognised in their entirety

The RMBS Trust provides an internal residential mortgage-backed securities programme to issue securities as collateral for borrowing from the RBNZ. The Bank has transferred housing loans to the RMBS Trust which secure these securities. These housing loans have not been derecognised by the Bank for financial reporting purposes as the Bank retains substantially all of the risks and rewards of ownership. As these housing loans have been legally transferred, the Bank does not retain the legal rights of ownership, but retains a security interest in these assets.

The Covered Bond Trust holds certain Bank of New Zealand housing loans and its trustee guarantees the payment of interest and principal under the covered bonds issued by the Bank and BNZ-IF. The assets of the Covered Bond Trust are not available to the Bank unless and until all prior ranking creditors of the Covered Bond Trust have been satisfied. The housing loans held by the Covered Bond Trust have not been derecognised by the Bank for financial reporting purposes as the Bank retains substantially all of the risks and rewards of ownership. As these housing loans have been legally transferred, the Bank does not retain the legal rights of ownership, but retains a security interest in these assets which is secondary to the guarantee provided by the trustee.

Further details on the transactions with the RMBS Trust and the Covered Bond Trust are provided in notes 11, 16, 22, 30, 39 and 41.

Government bonds and securities transferred under the agreements to repurchase have not been derecognised from the balance sheet as the Bank retains substantially all the risks and rewards of ownership. The Bank's obligation to repurchase is classified under Due to central banks and other institutions. Further detail on securities sold under agreements to repurchase are provided in notes 9, 10 and 19. The fair value of these agreements is approximately equal to the carrying amount on the balance sheet due to their short term nature.

The table below presents the carrying value of the transferred assets and the associated liabilities.

	Consolidated			
Dollars in Millions	**Carrying Amount of Assets 30/9/16**	Carrying Amount of Assets 30/9/15	**Carrying Amount of Associated Liabilities 30/9/16**	Carrying Amount of Associated Liabilities 30/9/15
Housing loans held by RMBS Trust	**4,472**	4,467	**-**	-
Housing loans held by Covered Bond Trust	**4,956**	4,204	**4,067**	3,686
Government bonds and securities	**152**	159	**152**	159
	9,580	8,830	**4,219**	3,845

Transfers of financial assets that have been derecognised in their entirety, but the Bank has continuing involvement

The Banking Group has no financial assets which have been derecognised in their entirety, but the Banking Group has continuing involvement.

Note 35 Segment Analysis

Operating segments

An operating segment is a component of an entity engaging in business activities and whose operating results are regularly reviewed by the entity's chief operating decision maker. For each operating segment identified by the Banking Group, financial information is regularly reported to the New Zealand Executive Team for the purposes of performance evaluation and resource allocation.

The Banking Group's business is organised into two major operating and reportable segments: Retail and Marketing, and BNZ Partners. The Retail and Marketing function provides transactional banking, savings and investments, home loans, credit cards and personal loans to individual and small business customers and, for management reporting purposes, includes insurance activities carried out by a controlled entity of National Australia Bank Limited that is not part of the Banking Group. BNZ Partners provides financial products and services to medium-sized business, agribusiness, private banking, institutional and corporate customers.

Revenues and expenses directly associated with each operating segment are included in determining their result. Transactions between operating segments are based on agreed recharges between segments. Segment revenue represents revenue directly attributable to a segment and a portion of the Banking Group's revenue that can be allocated to a segment on a reasonable basis. Segment revenue includes Net interest income and Other operating income, and includes transfer pricing adjustments to reflect inter-segment funding arrangements.

Segment profit represents operating profit before unrealised fair value gains or losses on financial instruments and income or expenses which are one-off in nature and are not part of the Banking Group's core business operations.

Included within the 'Other' categories in the following table are business activities that do not constitute a separately reportable segment; elimination entries on consolidation of the results and of the Banking Group's controlled entities in the preparation of the consolidated financial statements of the Banking Group; results of an entity included for management reporting purposes, but excluded from the consolidated financial statements of the Banking Group for statutory financial reporting purposes; and other balances excluded for management reporting purposes, but included in the consolidated financial statements of the Banking Group for statutory financial reporting purposes.

Note 35 Segment Analysis *continued*

Operating segments *continued*

Dollars in Millions	Retail and Marketing	BNZ Partners	Total Reportable Segments	All Other Segments	Other Adjustments	Total Banking Group
	Consolidated (30/9/16)					
Net interest income	**591**	**987**	**1,578**	**180**	**(1)**	**1,757**
Other income	**228**	**243**	**471**	**137**	**(96)**	**512**
Total operating income*	**819**	**1,230**	**2,049**	**317**	**(97)**	**2,269**
Operating expenses	**387**	**320**	**707**	**198**	**(16)**	**889**
Operating profit before impairment losses on credit exposures and income tax expense	**432**	**910**	**1,342**	**119**	**(81)**	**1,380**
Impairment losses / (gains) on credit exposures	**27**	**126**	**153**	**(28)**	**(5)**	**120**
Operating profit before income tax expense	**405**	**784**	**1,189**	**147**	**(76)**	**1,260**
Total income tax expense	**112**	**219**	**331**	**36**	**(20)**	**347**
Net profit attributable to shareholders of Bank of New Zealand	**293**	**565**	**858**	**111**	**(56)**	**913**
Lending assets	**27,614**	**45,865**	**73,479**	**899**	**-**	**74,378**
Deposit liabilities	**27,320**	**21,986**	**49,306**	**2,175**	**-**	**51,481**

* For the year ended 30 September 2016, there were no revenues deriving from transactions with a single external customer that amounted to 10% or more of the Banking Group's revenues.

Dollars in Millions	Retail and Marketing	BNZ Partners	Total Reportable Segments	All Other Segments	Other Adjustments	Total Banking Group
	Consolidated (30/9/15)					
Net interest income	649	901	1,550	185	-	1,735
Other income	229	265	494	165	38	697
Total operating income**	878	1,166	2,044	350	38	2,432
Operating expenses	459	332	791	90	(16)	865
Operating profit before impairment losses on credit exposures and income tax expense	419	834	1,253	260	54	1,567
Impairment losses / (gains) on credit exposures	16	87	103	31	(6)	128
Operating profit before income tax expense	403	747	1,150	229	60	1,439
Total income tax expense	107	209	316	59	26	401
Net profit attributable to shareholders of Bank of New Zealand	296	538	834	170	34	1,038
Lending assets	25,221	42,315	67,536	680	-	68,216
Deposit liabilities	25,241	19,356	44,597	2,132	-	46,729

** For the year ended 30 September 2015, there were no revenues deriving from transactions with a single external customer that amounted to 10% or more of the Banking Group's revenues.

Note 35 Segment Analysis *continued*

Other adjustments

The tables below detail reconciling items comprising Other adjustments in the segment analysis tables presented above.

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Other adjustments comprised:		
Total segment revenue		
Eliminations and consolidation adjustments	(63)	(57)
Fair value credit risk adjustment	(5)	(5)
Fair value gains or losses on financial instruments	(29)	100
	(97)	38
Operating profit before income tax expense		
Eliminations and consolidation adjustments	(47)	(40)
Fair value gains or losses on financial instruments	(29)	100
	(76)	60
Income tax expense		
Eliminations and consolidation adjustments	(12)	(2)
Fair value gains or losses on financial instruments	(8)	28
	(20)	26

Geographical information

The Banking Group has operations primarily in New Zealand. Geographical revenue information is based on the location of the office in which the transactions were booked, whereas for assets, it is based on the location of the assets.

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
Revenue from external customers		
New Zealand	2,269	2,432
Total revenue	2,269	2,432
Non-current assets*		
New Zealand	379	334
Overseas	2	-
Total non-current assets	381	334

* In accordance with NZ IFRS 8 Operating Segments, Non-current assets do not include financial instruments, deferred tax assets or post-employment benefit assets.

Note 36 Contingent Liabilities and Other Commitments

Bank of New Zealand and other income tax group members have a joint and several liability for the income tax liability of the income tax group. Bank of New Zealand is not expected to incur any additional tax liability as a result of this joint and several liability.

Contingent liabilities and credit related commitments exist in respect of commitments to extend credit, letters of credit and financial guarantees, as well as claims, potential claims and court proceedings against entities in the Banking Group. Any potential liability arising in respect of these claims cannot be accurately assessed with certainty. Where some loss is probable provisions have been made.

In March 2013, a potential representative action against New Zealand banks was announced in relation to certain fees. Litigation Lending Services (NZ) Limited is funding the action. On 20 August 2014, representative proceedings were filed against the Bank. On 24 September 2014, 30 April 2015, 3 December 2015 and 4 May 2016, these proceedings were stayed. The potential outcome of these proceedings cannot be determined with any certainty at this stage.

On 16 August 2016, a class action complaint was filed in the United States District Court for the Southern District of New York regarding alleged conduct concerning the Bank Bill Swap Reference Rate, which is administered by the Australian Financial Markets Association. The complaint names a number of defendants, including the Bank. At this stage, the Bank has not been served with the complaint and the potential outcome of such proceeding cannot be determined with any certainty.

The Labour Inspectorate of the Ministry of Business, Innovation and Employment is currently undertaking a programme of compliance audits of a number of New Zealand organisations in respect of the Holidays Act 2003 (the "Holidays Act"). The Bank requested early participation in this programme in May 2016 and received the Labour Inspectorate's preliminary findings of the Bank's compliance with the Holidays Act on 30 November 2016. The findings suggested that the Bank had not complied with certain requirements of the Holidays Act, including in respect of annual and public holiday payments to certain employees. The Bank is reviewing the findings and intends to work with the Labour Inspectorate to reach an appropriate resolution. At this stage, the potential outcome of the audit, including possible remediation, cannot be determined with any certainty.

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

	Consolidated	
Dollars in Millions	Notional Amount 30/9/16	Notional Amount 30/9/15
Contingent liabilities		
Bank guarantees	**65**	68
Standby letters of credit	**349**	404
Documentary letters of credit	**126**	215
Performance related contingencies	**466**	440
Total contingent liabilities	**1,006**	1,127
Credit related commitments		
Revocable commitments to extend credit	**8,012**	7,416
Irrevocable commitments to extend credit	**9,839**	8,924
Total credit related commitments	**17,851**	16,340
Total contingent liabilities and credit related commitments	**18,857**	17,467
Total contingent liabilities and credit related commitments comprised:		
New Zealand		
Agriculture	**364**	524
Forestry and fishing	**251**	170
Mining	**279**	273
Manufacturing	**1,416**	1,517
Electricity, gas and water	**1,061**	769
Construction	**381**	289
Wholesale and retail trade	**1,008**	1,204
Accommodation, restaurants, culture and recreation	**311**	264
Transport and storage	**522**	414
Communications	**262**	188
Financial, investment and insurance	**668**	681
Property, business and personal services	**1,527**	1,122
Government, education, health and community services	**1,102**	1,040
Real estate - mortgage	**1,643**	1,539
Personal lending	**50**	57
Total New Zealand	**10,845**	10,051
Revocable commitments to extend credit	**8,012**	7,416
Total contingent liabilities and credit related commitments	**18,857**	17,467

Contingent liabilities and credit related commitments by geographical location presented in the table above are based on the geographical location of the office in which the exposures are recognised. Contingent liabilities and credit related commitments by industry sector are based on the RBNZ M3 Institutions Standard Statistical Return.

The full notional amount of contingent liabilities and credit related commitments have been disclosed as "on-demand" as they could be payable on demand. The Banking Group expects that not all of the contingent liabilities or commitments will be drawn before their contractual expiry.

Note 36 Contingent Liabilities and Other Commitments *continued*

Contingent liabilities

The Banking Group's maximum exposure to credit risk for contingent exposures is the notional amount which represents the amount that the Banking Group would have to pay if the contingent liability is called upon.

The Banking Group uses the same credit policies and assessment criteria in making commitments and conditional obligations for off-balance sheet risk as it does for on-balance sheet loan assets.

The Bank has recourse arrangements with customers and others in respect of almost all of the contingent liabilities.

Guarantees

The Banking Group provides guarantees in its normal course of business on behalf of its customers. Guarantees are conditional commitments issued by the Banking Group to guarantee the performance or financial obligations of a customer to a third party.

The Banking Group has four principal types of guarantees:

- Bank guarantees - a guarantee that is an agreement by which the Bank agrees to pay an amount of money on demand on behalf of a customer to a third party during the life of the guarantee;
- Standby letters of credit - an obligation of the Bank on behalf of a customer to make payment to a third party in the event that the customer fails to meet an outstanding financial obligation;
- Documentary letters of credit - a guarantee that is established to indemnify exporters and importers in their trade transactions where the Bank agrees to make certain trade payments on behalf of a specified customer under specific conditions; and
- Performance related contingencies - a guarantee given by the Bank that undertakes to pay a sum of money to a third party where the customer fails to carry out certain terms and conditions of a contract.

The credit risk involved in issuing letters of credit and financial guarantees is essentially the same as that involved in extending loan facilities to customers. Apart from the normal documentation for a facility of this type, the customer must also provide the Banking Group with a written indemnity, undertaking that, in the event the Banking Group is called upon to pay, the Banking Group will be fully reimbursed by the customer.

Fees in relation to guarantees are collected over the life of the contract.

Credit related commitments

For commitments to extend credit, the maximum credit exposure to the Banking Group is the full amount of the commitment. Irrevocable commitments to extend credit are agreements to lend to a customer which can be drawn down at any time before the commitments expire as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiry dates or other termination clauses and may require payment of a fee by the customer. Since many of the commitments are expected to expire without being drawn down, the total commitment amounts do not necessarily represent future cash requirements.

Revocable commitments to extend credit represent those facilities which can be cancelled at any time at the Bank's discretion without the risk of incurring significant penalty or expense. These facilities are generally on-demand.

For information on the Banking Group's risk management policies, refer to note 41.

Guarantees to wholly owned controlled entities

The Bank guarantees the obligations of BNZ-IF in respect of securities issued by BNZ-IF to wholesale investors.

The constitution of BNZ-IF requires funds raised by its London Branch to be on-lent to the Bank on terms and conditions which match the terms and conditions of the original funding, including the same principal amount, currency, term and interest rate basis, and with corresponding redemption events and status (except that funds on-lent to the Bank will not be guaranteed).

Other commitments

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
Capital expenditure commitments *	**2**	1
Land and building operating lease commitments (refer to table below) **	**224**	263
Fleet vehicles operating lease commitments	**4**	7
Total other commitments	**230**	271
Land and buildings operating lease commitments comprised:		
Non-cancellable future minimum lease payments:		
Due within one year	**49**	49
Due within one to five years	**136**	153
Due after five years	**39**	61
Total land and buildings lease commitments	**224**	263

* These capital expenditure commitments have been entered into but not provided for in these financial statements.

** Figures include liabilities taken up for surplus leased space.

Note 37 Credit Exposures to Connected Persons and Non-bank Connected Persons

The RBNZ defines Connected Persons to be other members of NAB and Directors of the Bank. Controlled entities of the Bank are not connected persons. Credit exposures to connected persons have been derived in accordance with the Bank's conditions of registration and RBNZ's Connected Exposures Policy (BS8). The amounts are net of specific provision for doubtful debts and exclude advances of a capital nature.

Credit exposures to connected persons have been calculated on a partial bilateral net basis, netting derivative balances. Certain term loans from NAB have also been netted against derivative exposures. There is a limit of 125% of the Banking Group's Tier One capital in respect of the gross amount of aggregate credit exposure to connected persons that can be netted off in determining the net exposure.

	Consolidated	
	$ in Millions	% of Tier One Capital As At
	30/9/16	30/9/16
As at end of year		
Credit exposure to connected persons (on gross basis, before netting)	3,666	57.3%
Credit exposure to connected persons (amount netted)	2,227	34.8%
Credit exposure to connected persons (on partial bilateral net basis)	1,439	22.5%
Credit exposure to non-bank connected persons	-	-
Peak for the year ended		
Credit exposure to connected persons (on gross basis, before netting)	5,658	88.5%
Credit exposure to connected persons (amount netted)	2,197	34.4%
Credit exposure to connected persons (on partial bilateral net basis)	3,461	54.1%
Credit exposure to non-bank connected persons	-	-

As at 30 September 2016, the Banking Group's rating-contingent limit was 70% of the Banking Group's Tier One capital. This limit has not changed during the year. Within the overall rating-contingent limit, there is a sublimit of 15% of Tier One capital that applies to aggregate credit exposures to non-bank connected persons. The rating-contingent limit on credit exposures to connected persons as set out in the Bank's conditions of registration has been complied with at all times during the year ended 30 September 2016. Aggregate gross exposures to connected persons must not exceed 125% of the Banking Group's Tier One capital. The peak for the year ended credit exposure to connected persons and non-bank connected persons are calculated by determining the maximum end-of-day aggregated amount of actual credit exposure over Banking Group's Tier One Capital as at 30 September 2016.

Where a bank is funding a large loan it is common practice to share the risk of a customer default with other connected banks. These arrangements are called risk lay-off arrangements. As at 30 September 2016, the Banking Group had no contingent credit exposures arising from risk lay-off arrangements with connected persons. There were no credit exposures to connected persons that were credit-impaired, and no allowances for doubtful debts on individual financial assets for connected person credit exposures as at 30 September 2016.

Note 38 Concentrations of Credit Exposures to Individual Counterparties and Groups of Closely Related Counterparties

The Banking Group's disclosure of concentrations of credit exposures to individual counterparties and groups of closely related counterparties is based on actual credit exposures and excludes credit exposures to connected persons, the central government of any country with a long term credit rating of A- or A3 or above, or its equivalent, and banks with a long term credit rating of A- or A3 or above, or its equivalent. Peak credit exposures to individual counterparties are calculated using the Banking Group's end of period shareholders' equity.

	Consolidated (30/9/16) Credit Exposures to Individual Counterparties and Groups of Closely Related Counterparties* Long Term Credit Rating			
	Peak End-of-Day Number of Non-banks		Balance Sheet Date Number of Non-banks	
Percentage of Shareholders' Equity %	No Long Term Credit Rating	Total	No Long Term Credit Rating	Total
10-14	2	2	1	1
15 -19	-	-	-	-
20+	-	-	-	-

* The Banking Group has revised its methodology to calculate credit exposures based on maximum exposure to credit risk, which includes financial guarantees and undrawn loan commitments. This table reflects the change in methodology. Under the previous methodology, the Banking Group had no non-bank counterparties that met the disclosure thresholds.

Where the Banking Group is funding large loans, it is common practice to share the risk of a customer default with other connected banks or enter into other risk lay-off arrangements. The above table has been compiled using gross exposures before risk lay-offs. No account is taken of collateral, security and/or netting agreements which the Banking Group may hold in respect of the various counterparty exposures.

As at 30 September 2016 and for the three months ended 30 September 2016, the Banking Group had no bank counterparties that equalled or exceeded 10% of the Banking Group's equity and met the disclosure thresholds described above.

Note 39 Insurance Business, Securitisation, Funds Management, Other Fiduciary Activities, and the Marketing and Distribution of Insurance Products

Funds management

The Bank markets and distributes funds management products to a range of customers which are issued by its wholly owned subsidiary BNZISL. The Bank provides banking services for funds management products administered by BNZISL. The Bank also provides services to a number of customers which include advice on, administration, and management of, investment portfolios.

BNZ Cash PIE (the "Fund") is a Portfolio Investment Entity. BNZISL is the Manager and Issuer of the Fund. The Fund is consolidated as part of the Banking Group for financial reporting purposes. The Fund transitioned into the Financial Markets Conduct Act 2013 (the "FMCA") regime on 5 September 2016.

BNZ Term PIE (the "Term Fund") is a Portfolio Investment Entity. BNZISL is the Manager and Issuer of the Term Fund. The Term Fund is consolidated as part of the Banking Group for financial reporting purposes. The Term Fund transitioned into the FMCA regime on 5 September 2016.

BNZISL established the BNZ KiwiSaver Scheme by a Trust Deed dated 8 January 2013 between it and The New Zealand Guardian Trust Company Limited. The Scheme was registered under the KiwiSaver Act 2006 on 16 January 2013. The Scheme was launched to the public on 25 February 2013. The BNZ Kiwisaver Scheme transitioned into the FMCA regime on 5 September 2016.

BNZISL is the Manager and Issuer of the BNZ KiwiSaver Scheme. The BNZ KiwiSaver Scheme invested in the BNZ Cash PIE issued by BNZISL until 26 March 2015. The BNZ KiwiSaver Scheme currently invests (among other things) in bank deposits with BNZ. The Scheme's banking arrangements are provided by the Bank. All arrangements are conducted on arms' length commercial terms.

Investments made in the BNZ KiwiSaver Scheme do not represent deposits or other liabilities of the Bank or any other member of NAB, and are subject to investment risk, including possible delays in repayment and loss of income and principal invested. None of the Bank, or any other member of NAB, the Supervisor (The New Zealand Guardian Trust Company Limited), any Director of any of them, the Crown or any other person guarantees (either fully or in part) the performance or returns of the BNZ KiwiSaver Scheme or the repayment of capital.

During the year ended 30 September 2016, the Bank held deposits on behalf of customers of JBWere (NZ) Pty Limited and JBWere (NZ) Nominees Limited. JBWere (NZ) Pty Limited and JBWere (NZ) Nominees Limited, as controlled entities of the ultimate parent, are related parties of the Banking Group, but are not a part of the Banking Group.

The outstanding value of assets related to fund management activities is set out in the table below. The assets shown below for portfolios managed on behalf of customers are not owned by the Banking Group and are, therefore, not included as part of the Banking Group's assets on the balance sheet. The Fund and Term Fund invest solely in debt securities issued by the Banking Group and on consolidation their assets are eliminated against liabilities recorded by the Bank. Unitholders' interests are included as part of the Banking Group's liabilities.

Dollars in Millions	**30/9/16**	30/9/15
Portfolios managed on behalf of customers	**3,590**	2,718
BNZ Cash PIE	**115**	206
BNZ Term PIE	**1,017**	976

Insurance business

The Banking Group does not conduct any Insurance Business, as defined in clause 3 of Bank of New Zealand's conditions of registration set out on page 84.

Marketing and distribution of insurance products

The Banking Group is involved in marketing insurance products for the following entities: BNZ Life Insurance Limited, Union Medical Benefits Society Limited, The National Mutual Life Association of Australasia Limited, IAG New Zealand Limited, Cigna Life Insurance New Zealand Limited, Partners Life Limited and QBE Insurance (International) Limited. In addition, the Banking Group refers all commercial non life insurance product queries to AON New Zealand and all trade credit queries are referred to National Credit Insurance (Brokers) Pty Limited.

All of these entities are unrelated to the Banking Group, with the exception of BNZ Life Insurance Limited, a controlled entity of National Australia Bank Limited. BNZ Life Insurance Limited is an Affiliated Insurance Entity as defined in BS2B.

Structured entities

A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity. Structured entities generally have restricted activities and a narrow and well defined objective which are both created through contractual arrangements.

Depending on the Banking Group's power over the relevant activities of the structured entity and its exposure to and ability to influence its own returns, it may or may not consolidate the entity.

The Banking Group's involvement in structured entities is subject to internal credit, compliance and legal approval processes to ensure that any difficulties arising from the structured entities do not impact adversely on the Banking Group, beyond that which is normal for arm's length commercial relationships.

Consolidated structured entities

The Banking Group has interests in the RMBS Trust and Covered Bond Trust consolidated structured entities.

RMBS Trust and Covered Bond Trust

The RMBS Trust provides an internal residential mortgage-backed securities programme. As at 30 September 2016, included within the Banking Group's loans and advances to customers were housing loans with a carrying amount of $4,472 million held by the RMBS Trust (30 September 2015: $4,467 million). These housing loans have not been derecognised by the Bank for financial reporting purposes as the Bank retains substantially all of the risks and rewards of ownership.

Note 39 Insurance Business, Securitisation, Funds Management, Other Fiduciary Activities, and the Marketing and Distribution of Insurance Products *continued*

Consolidated structured entities *continued*

The Covered Bond Trust holds certain Bank of New Zealand housing loans and its trustee guarantees the payment of interest and principal under the covered bonds issued by the Bank and BNZ-IF. The assets of the Covered Bond Trust are not available to the Bank unless and until all prior ranking creditors of the Covered Bond Trust have been satisfied. As at 30 September 2016, included within the Banking Group's loans and advances to customers were housing loans with a carrying amount of $4,956 million held by the Covered Bond Trust (30 September 2015: $4,204 million). These housing loans have not been derecognised by the Bank for financial reporting purposes as the Bank retains substantially all of the risks and rewards of ownership.

Further details on the transactions with the RMBS Trust and the Covered Bond Trust are provided in notes 11, 16, 22, 30, 34 and 41.

Cash and Term PIE Investment Entity

The Banking Group has interests in consolidated investment entities. The Banking Group's interests are noted in the funds management section on page 57.

Unconsolidated structured entities

Unconsolidated structured entities refer to all structured entities that are not controlled by the Banking Group. The Banking Group enters into transactions with unconsolidated structured entities in the normal course of business to facilitate customer transactions and for specific investment opportunities.

The Banking Group engages with third party (client) securitisations by providing funding, liquidity support and derivatives.

Interests in unconsolidated structured entities include, but are not limited to, debt investments, guarantees, liquidity arrangements, and commitments that expose the Banking Group to the risks of the unconsolidated structured entity. Interests do not include plain vanilla derivatives (e.g. interest rate swaps and currency swaps).

The table below shows the carrying value and maximum exposure to loss and credit quality of the Banking Group's interests in unconsolidated securitisation entities as at 30 September 2016.

	Consolidated (30/9/16)			Consolidated (30/9/15)		
Dollars in Millions	**Senior Investment Grade**	**Investment Grade**	**Total**	Senior Investment Grade	Investment Grade	Total
Carrying value of loans and advances	**365**	**203***	**568**	135	204*	339
Commitments and guarantees	**177**	**3**	**180**	255	4	259
Total maximum exposure to credit loss	**542**	**206**	**748**	390	208	598

* Included in investment grade loans and advances is $195 million lent to a securitisation vehicle included in "Peak aggregate funding provided to entities" table on page 59. The Banking Group markets the products of, and seconds staff and leases premises to this securitisation vehicle. All transactions have taken place on arm's length terms and conditions.

The total assets of unconsolidated structured entities are not considered meaningful for the purpose of understanding the Banking Group's financial risks associated with these entities and so have not been presented. Unless specified otherwise, the Banking Group's maximum exposure to loss is the total of its on-balance sheet positions and its off-balance sheet arrangements, being loan commitments, financial guarantees, and liquidity support. Exposure to loss is managed as part of the Banking Group-wide risk management framework. Refer to note 41 for further information.

Income earned from interests in unconsolidated structured entities primarily resulted from interest income, fees and commission income.

Risk management

The Banking Group has in place policies and procedures to ensure that the activities identified above are conducted in an appropriate manner. Should adverse investment or liquidity conditions arise it is considered that the Banking Group's policies and procedures, combined with those of BNZ Life Insurance Limited and BNZ Insurance Services Limited, will minimise the possibility that those conditions will adversely impact the Banking Group. The policies and procedures referred to include comprehensive and prominent disclosure of information regarding products, formal and regular review of operations and policies by internal auditors and management, appropriate contractual agreements and compliance with contractual obligations and regulatory requirements.

The Banking Group's risk review and risk management systems are equally applicable to the marketing and distribution of products issued by the third party entities identified in the marketing and distribution of insurance products and funds management sections discussed on page 57.

In addition, the following measures are also taken to manage any risk to the Banking Group of marketing and distributing insurance products:

- disclaimers on policies, application forms and other collateral relating to insurance products expressly state that the policy is not an obligation of the Bank and that the Bank does not guarantee the obligations of the insurer;
- the risks under policies issued by BNZ Life Insurance Limited are substantially reinsured; and
- the introduction of new policies and changes to existing policies marketed or distributed by the Banking Group are subject to the Banking Group's standard risk management policies and procedures.

The Bank does not guarantee the capital, income or return of any of the products referred to above.

Transactions with Banking Group entities

Financial services provided by any member of the Banking Group to entities which are involved in trust, custodial, funds management and other fiduciary activities and securitisation arrangements, and to affiliated insurance entities which conduct marketing and distribution of insurance products, or on whose behalf the marketing and distribution of insurance products are conducted, have been provided on arm's length terms and conditions and at fair value. Assets purchased from any such entities by any member of the Banking Group have been purchased on arm's length terms and conditions and at fair value.

Note 39 Insurance Business, Securitisation, Funds Management, Other Fiduciary Activities, and the Marketing and Distribution of Insurance Products *continued*

Peak aggregate funding provided to entities

The Bank does not provide any funding to individual unit trusts which the Banking Group distributes on behalf of third parties.

Peak end-of-day aggregate funding (including funding provided by the purchase of securities) provided by the Banking Group to individual affiliated insurance entities and entities involved in securitisation activities, where the Banking Group is involved in the origination of securitised assets, and the marketing of securitisation schemes, is disclosed in the table below:

	Consolidated					
	Peak End-of-Day Aggregate Amount of Funding during the Year		Peak End-of-Day Aggregate Amount of Funding during the Year expressed as a Percentage of the Amount of the Entity's Assets at end of Year		Peak End-of-Day Aggregate Amount of Funding during the Year expressed as a Percentage of the Banking Group's Tier One Capital at end of Year	
Dollars in Thousands	**For the Year Ended 30/9/16**	For the Year Ended 30/9/15	**For the Year Ended 30/9/16**	For the Year Ended 30/9/15	**For The Year Ended 30/9/16**	For The Year Ended 30/9/15
Covenant Trustee Services Limited	**195,000**	195,000	**100.0%**	100.0%	**3.0%**	3.0%

The above table has been compiled using gross exposures before risk lay-offs.

Note 40 Capital Adequacy*

The RBNZ minimum regulatory capital requirements for banks have been established under BS2B and Capital Adequacy Framework (Standardised Approach) ("BS2A") based on the international framework developed by the Bank for International Settlements, Committee on Banking Supervision, commonly known as Basel III. These requirements outline how minimum regulatory capital is to be calculated and provide methods for measuring risks incurred by the banks in New Zealand.

The Basel III Framework's objective is to develop capital adequacy guidelines that are more accurately aligned with the individual risk profile of banks. Basel III consists of three pillars – Pillar One covers the capital requirements for banks for credit, operational, and market risks. Pillar Two covers all other material risks that are not already included in Pillar One. Pillar Three relates to market disclosure.

RBNZ Capital Adequacy Framework (Internal Models Based Approach) ("BS2B")

The Banking Group has calculated its implied Risk-Weighted Exposure and minimum regulatory capital requirements based on BS2B for operational risk and the majority of credit risk portfolios.

Under BS2B, banks use their own models for estimating risk and minimum capital requirements. Under the Internal Ratings Based Approach for credit risk, the level of risk associated with customers' exposures is determined by way of the primary components of Probability of Default, Loss Given Default and Exposure at Default. These components and associated processes are subject to regular review. For exposures in the Specialised Lending asset category (including Project Finance, Object Finance, Commodity Finance and Income Producing Real Estate) the Banking Group uses supervisory slotting estimates provided by the RBNZ.

The exceptions to the Internal Ratings Based Approach for credit risk are portfolios of relatively low materiality which are subject to the standardised treatment as set out in BS2A.

Capital for market risk has been calculated in accordance with the approach specified in BS2B.

Capital management policies

The Banking Group's primary objectives in relation to the management of capital adequacy are to comply with the requirements set out by the RBNZ, the Banking Group's primary prudential supervisor, to provide a sufficient capital base to cover risks faced by the Bank and to maintain a credit rating to support future business development.

The Bank's conditions of registration require capital adequacy ratios to be calculated in accordance with BS2B. Total regulatory capital is defined as the sum of Common Equity Tier One capital, Additional Tier One capital and Tier Two capital. Tier One capital is defined as the sum of Common Equity Tier One capital and Additional Tier One capital. The Banking Group's Common Equity Tier One capital includes paid up ordinary shares and retained profits less certain deductions, Additional Tier One capital includes perpetual non-cumulative preference shares and Tier Two capital includes revaluation reserves and subordinated loans and notes.

The Banking Group is required under its conditions of registration to maintain a minimum ratio of total eligible or qualifying capital to total risk-weighted assets of 8%, of which a minimum of 4.5% must be held in Common Equity Tier One capital and a minimum of 6% must be held in Tier One capital. The Banking Group must maintain a minimum common equity buffer ratio of 2.5% above these minimum ratios or it will face restrictions on the distribution of earnings and be required to prepare a capital plan that restores the Banking Group's buffer ratio and have that capital plan approved by the RBNZ.

The Banking Group has an Internal Capital Adequacy Assessment Process ("ICAAP") in place which complies with the requirements set out in the RBNZ's "Guidelines on a Bank's Internal Capital Adequacy Assessment Process" ("BS12") as specified under the Bank's conditions of registration. The Banking Group's ICAAP outlines the approach to maintaining capital adequacy, risk appetite and stress testing. The ICAAP considers all material risks consistent with the Banking Group's risk appetite and outlines the capital requirements.

* Note 40 is subject to review procedures which do not constitute an audit. Refer to page 82 of the Independent Auditor's Report for further information.

Note 40 Capital Adequacy *continued*

Capital requirements, as detailed in the Banking Group's ICAAP document, are managed by the Bank's Risk Return Management Committee and Asset, Liability and Capital Committee under delegated authority from the Board of Directors.

Information on the capital structure of the Banking Group is detailed in notes 24 to 27.

The tables included below and on the following pages detail the capital calculation, capital ratios and capital requirements as at 30 September 2016. During the financial period the Banking Group fully complied with all RBNZ's capital requirements as set out in the Bank's conditions of registration, except as disclosed on page 88 of this Disclosure Statement.

Regulatory capital

The following table shows the qualifying capital for the Banking Group.

Dollars in Millions	**Consolidated** Unaudited 30/9/16
Qualifying capital	
Common Equity Tier One capital	
Contributed equity - ordinary shareholder	2,351
Retained profits	4,339
Deductions from Common Equity Tier One capital:	
Intangible assets	216
Credit value adjustment on liabilities designated at fair value through profit or loss	(53)
Prepaid pension assets (net of deferred tax)	4
Deferred tax asset	179
Total expected loss less total eligible allowances for impairment	148
Total Common Equity Tier One capital	6,196
Additional Tier One capital	
Contributed equity - perpetual preference shareholders*	200
Total Additional Tier One capital	200
Total Tier One capital	6,396
Tier Two capital	
Revaluation reserves	2
Subordinated loans due to related entities**	362
Subordinated notes due to external investors	550
Total Tier Two capital	914
Total Tier One and Tier Two qualifying capital	7,310

* Contributed equity (comprising perpetual preference shares) in Additional Tier One capital is subject to phase-out in accordance with BS2B. The phase-out, which commenced on 1 January 2014, takes place over five years, with the maximum eligible amount of Additional Tier One capital for these instruments declining by 20% each year. The base amount for phase-out was fixed at the nominal amount outstanding as at 1 January 2013 and amounted to $910 million. Perpetual preference shares of $260 million and $450 million were repurchased in June 2014 and September 2016 respectively.

** Subordinated loans due to related entities in Tier Two capital are subject to phase-out in accordance with BS2B. The phase-out, which commenced on 1 January 2014, takes place over five years, with the maximum eligible amount of Tier Two capital for these instruments declining by 20% each year. The base amount for phase-out was fixed at the nominal amount outstanding as at 1 January 2013 and amounted to $905 million. Subordinated loans of $190 million and $335 million were repaid in February 2014 and June 2016 respectively.

Banking Group Basel III regulatory capital ratios

The table below shows the capital adequacy ratios for the Banking Group based on BS2B, expressed as a percentage of total risk-weighted exposures.

		Consolidated		
	Regulatory Minima 30/9/16	**Unaudited 30/9/16**	Regulatory Minima 30/9/15	Unaudited 30/9/15
Common Equity Tier One capital ratio	4.50%	10.21%	4.50%	10.70%
Tier One capital ratio	6.00%	10.54%	6.00%	11.69%
Total qualifying capital ratio	8.00%	12.04%	8.00%	12.67%
Buffer ratio	2.50%	4.04%	2.50%	4.67%

Note 40 Capital Adequacy *continued*

Registered Bank Basel III regulatory capital ratios

The tables below show the capital adequacy ratios based on BS2B, expressed as a percentage of total risk-weighted exposures.

	The Registered Bank Unaudited 30/9/16	Unaudited 30/9/15
Common Equity Tier One capital ratio	**10.23%**	10.76%
Tier One capital ratio	**10.56%**	11.74%
Total qualifying capital ratio	**12.06%**	12.73%

For the purpose of calculating capital adequacy ratios for the Registered Bank under BS2B, subsidiaries which are both funded exclusively and wholly owned by the Registered Bank are consolidated within the Registered Bank.

Total regulatory capital requirements

Dollars in Millions	Consolidated Total Exposure at Default Unaudited 30/9/16	Risk-Weighted Exposure or Implied Risk-Weighted Exposure Unaudited 30/9/16	Total Capital Require-ment* Unaudited 30/9/16
Credit risk			
Exposures subject to the internal ratings based approach	92,426	43,397	3,472
Equity exposures	12	49	4
Specialised lending subject to the slotting approach	8,002	7,623	610
Exposures subject to the standardised approach	2,441	1,015	81
Credit value adjustment subject to BS2B	N/A	1,360	109
Total credit risk	102,881	53,444	4,276
Operational risk	N/A	4,375	350
Market risk	N/A	2,890	231
Total	102,881	60,709	4,857

* In calculating the total capital requirement, a scalar of 1.06 has been applied to the risk-weighted assets, as required by the RBNZ in accordance with the Bank's conditions of registration.

Advanced Internal Ratings Based approach to credit risk management

The Banking Group's quantitative credit risk measurement is based on the Internal Ratings Based ("IRB") approach (IRB for Retail Credit portfolios and Advanced IRB for Non-retail Credit portfolios) and uses a series of models, to calculate loss estimates for the credit portfolio. This includes consideration of:

- probability of default ("PD") which estimates the probability that a customer will default over the next 12 months;
- exposure at time of default ("EAD") which estimates the amount of outstanding principal, fees and interest owed at the time of default; and
- loss given default ("LGD") which estimates the expected loss in the event of default. It is the percentage of exposure which will be lost after all recovery efforts, including legal expenses, time value of money and recovery expenses.

The above three elements (PD, EAD, and LGD) are important inputs in determining the risk-weighted exposure calculations for both on and off-balance sheet exposures, including undrawn portions of credit facilities, committed and contingent exposures. These ratings are also an important input into the credit approval, risk management, internal capital allocation and corporate governance functions of the Banking Group.

Methodologies used to calculate credit risk estimates (PD, EAD and LGD) are in accordance with BS2B and the Bank's conditions of registration. For credit risk estimates on some portfolios, the RBNZ has set prescribed risk estimates required to be used when calculating risk-weighted assets and capital under BS2B. The RBNZ prescribed risk estimates will continue to be used until the Banking Group develops its own internal models for these portfolios.

Controls surrounding credit risk rating systems

The credit risk rating systems cover all methods, processes, controls, data collection and technology that support the assessment of credit risk, the assignment of internal credit risk ratings and the quantification of associated default and loss estimates.

The credit risk rating systems and risk estimate processes are governed by the Banking Group's Credit Risk Committee and are an integral part of reporting to senior management. Management and staff of the credit risk function regularly assess the performance of the rating systems, monitor progress on changes being made to systems and identify any areas for improvement. These systems are subject to rigorous internal review and approval and regular independent review. The annual validation of models is undertaken by specialists who are responsible for overseeing the design, implementation and performance of all rating models across the Banking Group.

The risk-weighted asset amounts presented in the following tables include a scalar of 1.06 as required by the RBNZ in accordance with the Bank's conditions of registration.

Note 40 Capital Adequacy *continued*

Credit risk subject to the Internal Ratings Based ("IRB") approach

The following tables analyse credit risk exposures by asset class split into PD bandings. The lower the PD banding the less the probability of default over the next 12 months.

	Consolidated					
Dollars in Millions	Weighted Average PD (%) Unaudited 30/9/16	Exposure at Default Unaudited 30/9/16	Exposure-Weighted LGD used for the Capital Calculation (%) Unaudited 30/9/16	Exposure-Weighted Risk Weight (%) Unaudited 30/9/16	Risk-Weighted Assets Unaudited 30/9/16	Minimum Capital Requirement Unaudited 30/9/16
Corporate						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.07	3,626	45	24	866	69
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.30	13,940	37	44	6,173	494
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.95	11,597	34	67	7,752	620
Exposure-weighted PD grade > 1.5 ≤ 5.0%	2.58	8,194	36	97	7,931	635
Exposure-weighted PD grade > 5.0 ≤ 99.99%	10.82	1,262	40	163	2,061	165
Default PD grade = 100%	100.00	1,186	44	340	4,037	323
Total corporate exposures	4.24	39,805	37	72	28,820	2,306
Sovereign						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.03	5,250	9	2	86	7
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.43	17	45	59	10	1
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.67	20	45	72	14	1
Exposure-weighted PD grade > 1.5 ≤ 5.0%	1.85	2	45	107	2	-
Exposure-weighted PD grade > 5.0 ≤ 99.99%	5.72	-	45	147	-	-
Default PD grade = 100%	-	-	-	-	-	-
Total sovereign exposures	0.03	5,289	9	2	112	9
Bank						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.03	4,063	36	14	549	44
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.17	447	51	48	213	17
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.78	10	60	92	10	1
Exposure-weighted PD grade > 1.5 ≤ 5.0%	2.63	7	60	147	10	1
Exposure-weighted PD grade > 5.0 ≤ 99.99%	5.72	-	60	195	-	-
Default PD grade = 100%	-	-	-	-	-	-
Total bank exposures	0.05	4,527	37	17	782	63
Residential mortgage						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.03	25	25	4	1	-
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.40	1,737	18	14	243	19
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.91	34,527	21	28	9,560	765
Exposure-weighted PD grade > 1.5 ≤ 5.0%	4.92	2,161	20	72	1,545	124
Exposure-weighted PD grade > 5.0 ≤ 99.99%	-	-	-	-	-	-
Default PD grade = 100%	100.00	170	24	239	407	32
Total residential mortgage exposures	1.54	38,620	21	30	11,756	940
Other retail*						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.05	802	85	13	103	8
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.25	616	83	40	243	19
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.95	389	83	86	333	27
Exposure-weighted PD grade > 1.5 ≤ 5.0%	2.83	320	83	120	384	31
Exposure-weighted PD grade > 5.0 ≤ 99.99%	11.74	117	81	150	176	14
Default PD grade = 100%	100.00	11	77	501	53	4
Total other retail exposures	1.73	2,255	84	57	1,292	103

* Other retail includes credit cards, current accounts and personal overdrafts.

Notes to and Forming Part of the Financial Statements

Note 40 Capital Adequacy *continued*

Credit risk subject to the Internal Ratings Based ("IRB") approach *continued*

Dollars in Millions	Consolidated					
	Weighted Average PD (%) Unaudited 30/9/16	Exposure at Default Unaudited 30/9/16	Exposure-Weighted LGD used for the Capital Calculation (%) Unaudited 30/9/16	Exposure-Weighted Risk Weight (%) Unaudited 30/9/16	Risk-Weighted Assets Unaudited 30/9/16	Minimum Capital Requirement Unaudited 30/9/16
Retail small to medium enterprises						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.07	135	34	7	9	1
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.30	595	28	15	92	8
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.97	548	31	32	175	14
Exposure-weighted PD grade > 1.5 ≤ 5.0%	2.58	561	34	48	268	21
Exposure-weighted PD grade > 5.0 ≤ 99.99%	11.06	57	37	65	37	3
Default PD grade = 100%	100.00	34	44	160	54	4
Total retail SME exposures	3.20	1,930	31	33	635	51
Total*						
Exposure-weighted PD grade > 0 ≤ 0.1%	0.04	13,901	31	12	1,614	129
Exposure-weighted PD grade > 0.1 ≤ 0.5%	0.30	17,352	37	40	6,974	558
Exposure-weighted PD grade > 0.5 ≤ 1.5%	0.92	47,091	25	38	17,844	1,428
Exposure-weighted PD grade > 1.5 ≤ 5.0%	3.04	11,245	34	90	10,140	812
Exposure-weighted PD grade > 5.0 ≤ 99.99%	10.91	1,436	43	158	2,274	182
Default PD grade = 100%	100.00	1,401	42	325	4,551	363
Total exposures	2.59	92,426	30	47	43,397	3,472

* The BS2B credit value adjustment has not been included in the above exposures.

The following table analyses the value and exposure at default of on-balance sheet exposures, off-balance sheet exposures and market related contracts under the IRB approach by asset class:

Dollars in Millions	Consolidated			
	Total Exposure Unaudited 30/9/16	Exposure at Default Unaudited 30/9/16	Risk-Weighted Assets Unaudited 30/9/16	Minimum Capital Requirement Unaudited 30/9/16
On-balance sheet exposures				
Corporate	29,674	29,674	23,070	1,846
Sovereign	4,981	4,981	85	7
Bank	2,201	2,201	341	28
Residential mortgage	34,919	34,919	10,778	862
Other retail	1,273	1,273	942	75
Retail small to medium enterprises	1,555	1,555	527	42
Total on-balance sheet exposures	74,603	74,603	35,743	2,860
Off-balance sheet exposures				
Corporate	9,388	8,476	4,803	384
Sovereign	83	49	14	1
Bank	881	868	53	4
Residential mortgage	3,480	3,701	978	78
Other retail	2,858	982	350	28
Retail small to medium enterprises	416	375	108	9
Total off-balance sheet exposures	17,106	14,451	6,306	504
Market related contracts				
Corporate	193,477	1,655	947	76
Sovereign	10,777	259	13	1
Bank	153,537	1,458	388	31
Total market related contracts	357,791	3,372	1,348	108

Note 40 Capital Adequacy *continued*

Credit risk subject to the Internal Ratings Based ("IRB") approach *continued*

	Consolidated			
Dollars in Millions	Total Exposure Unaudited 30/9/16	Exposure at Default Unaudited 30/9/16	Risk-Weighted Assets Unaudited 30/9/16	Minimum Capital Requirement Unaudited 30/9/16
Summary*				
Corporate	232,539	39,805	28,820	2,306
Sovereign	15,841	5,289	112	9
Bank	156,619	4,527	782	63
Residential mortgage	38,399	38,620	11,756	940
Other retail	4,131	2,255	1,292	103
Retail small to medium enterprises	1,971	1,930	635	51
Total credit risk exposures subject to the IRB approach	449,500	92,426	43,397	3,472

* The BS2B credit value adjustment and agribusiness supervisory adjustment have not been included in the above exposures.

Equity exposures

The table below shows the capital required to be held as a result of equities held.

	Consolidated			
Dollars in Millions	Exposure at Default Unaudited 30/9/16	Risk Weight (%) Unaudited 30/9/16	Risk-Weighted Exposures Unaudited 30/9/16	Minimum Pillar One Capital Requirement Unaudited 30/9/16
Equity holdings (not deducted from capital) that are publicly traded	-	300	-	-
All other equity holdings (not deducted from capital)	12	400	49	4
Total equity exposures	12	400	49	4

Specialised lending subject to the slotting approach

The tables below show specialised lending exposures for which the supervisory slotting approach has been used and includes Project Finance, Object Finance, Commodity Finance and Income Producing Real Estate exposures.

On-balance sheet exposures subject to the slotting approach

	Consolidated			
Dollars in Millions	Total Exposure at Default after Credit Risk Mitigation Unaudited 30/9/16	Risk Weight (%) Unaudited 30/9/16	Risk-Weighted Assets Unaudited 30/9/16	Minimum Pillar One Capital Requirement Unaudited 30/9/16
Strong	1,358	70	1,007	81
Good	4,350	90	4,146	332
Satisfactory	1,329	115	1,615	129
Weak	37	250	97	8
Default	116	-	-	-
Total on-balance sheet exposures subject to the slotting approach	7,190	90	6,865	550

The categories of specialised lending above are associated with the risk weight shown. These categories broadly correspond to external credit assessments from Standard & Poor's rating scale: BBB- or better (Strong); BB+ or BB (Good); BB- or B+ (Satisfactory); B to C- (Weak).

The calculated risk-weighted assets reflected above include the required scalar of 1.06, specified in the Bank's conditions of registration, which is not reflected in the risk weight shown.

Off-balance sheet exposures subject to the slotting approach

	Consolidated				
Dollars in Millions	Total Exposure Unaudited 30/9/16	Exposure At Default Unaudited 30/9/16	Average Risk Weight (%) Unaudited 30/9/16	Risk-Weighted Assets Unaudited 30/9/16	Minimum Pillar One Capital Requirement Unaudited 30/9/16
Off-balance sheet exposures	153	41	90	36	3
Undrawn commitments	1,369	685	95	653	52
Market related contracts	1,496	86	80	69	5
Total off-balance sheet exposures subject to the slotting approach	3,018	812	93	758	60
Total exposures subject to the slotting approach		8,002	90	7,623	610

Note 40 Capital Adequacy *continued*

Credit risk exposures subject to the standardised approach

The tables below show credit risk exposures, for which the standardised approach has been used.

On-balance sheet exposures subject to the standardised approach

	Consolidated			
	Total Exposure at Default after Credit Risk Mitigation Unaudited	Average Risk Weight (%) Unaudited	Risk-Weighted Assets Unaudited	Minimum Pillar One Capital Requirement Unaudited
Dollars in Millions	30/9/16	30/9/16	30/9/16	30/9/16
Corporate	376	61	230	18
Residential mortgages	106	84	88	7
Past due assets	1	106	1	-
Other assets*	1,676	39	662	53
Total on-balance sheet exposures subject to the standardised approach	2,159	45	981	78

* Other assets relate to all other non-lending assets (including interest receivables, account receivables, intangibles and cash accounts) that are not included in the other categories in the table.

Off-balance sheet exposures subject to the standardised approach

	Consolidated					
	Total Exposure or Principal Amount Unaudited	Average Credit Conversion Factor (%) Unaudited	Credit Equivalent Amount Unaudited	Average Risk Weight (%) Unaudited	Risk-Weighted Assets Unaudited	Minimum Pillar One Capital Requirement Unaudited
Dollars in Millions	30/9/16	30/9/16	30/9/16	30/9/16	30/9/16	30/9/16
Total off-balance sheet exposures subject to the standardised approach	88	29	26	90	23	2
Market related contracts subject to the standardised approach						
Foreign exchange contracts	13	N/A	-	106	-	-
Interest rate contracts**	184,346	N/A	256	4	11	1
Other	1	N/A	-	4	-	-
Total market related contracts subject to the standardised approach	184,360	N/A	256	4	11	1
Total exposures subject to the standardised approach		N/A	2,441	42	1,015	81

** The total exposure or principal amount reflects the gross notional value of contracts transacted through a qualifying central counterparty ("QCCP"). The application of a risk weight for exposures to central counterparties was enacted by the RBNZ as part of its Basel III reforms. Capital requirements have been calculated in accordance with BS2B.

Credit risk mitigation

The Banking Group assesses the integrity and ability of counterparties to meet their contractual financial obligations for repayment. Collateral security in the form of property or a security interest in personal property is generally taken for business credit except for major government, bank and corporate counterparties of strong financial standing. Longer term consumer finance (e.g. housing loans) is generally secured against real estate while short term revolving consumer credit is generally unsecured.

The table below shows the total value of exposures covered by eligible financial collateral (after haircutting) for portfolios subject to the standardised approach and total value of exposures covered by credit derivatives and guarantees for all portfolios.

	Consolidated
	Corporate (Including Specialised Lending) Unaudited
Dollars in Millions	30/9/16
For portfolios subject to the standardised approach:	
Total value of exposures covered by eligible financial or IRB collateral (after haircutting)	9
For all portfolios:	
Total value of exposures covered by credit derivatives or guarantees	-

Note 40 Capital Adequacy *continued*

Residential mortgages by loan-to-valuation ratio

The table below sets out residential mortgages (including loans to businesses) wholly or partly secured by mortgages over residential properties as used to calculate the Banking Group's Pillar One capital requirement by the loan-to-valuation ratio ("LVR").

The LVRs are calculated as the greater of the customer's current loan limit or balance, divided by the Banking Group's valuation of the security at the last credit event for the customer. Where no LVR is available, the exposure is included in the over 90% category.

	Consolidated		
	On-balance Sheet Exposures at Default Unaudited	Off-balance Sheet Exposures at Default* Unaudited	Total Exposures at Default Unaudited
Dollars in Millions	30/9/16	30/9/16	30/9/16
LVR Range			
0-59%	12,553	1,455	14,008
60-69%	7,371	730	8,101
70-79%	12,133	1,114	13,247
80-89%	1,520	56	1,576
Over 90%	1,342	346	1,688
Total exposures at default secured by residential mortgages	34,919	3,701	38,620

* Off-balance sheet items include unutilised limits and loans approved, but not yet drawn.

	Consolidated
	On-balance Sheet Exposures at Default Unaudited
Dollars in Millions	30/9/16
Reconciliation of exposures secured by residential mortgages to housing loans in note 11 Loans and advances to customers	
Loans and advances to customers - housing loans	34,914
Add: Partial write offs excluded under the IRB approach	7
Deduct: Interest accrued	(2)
Total exposures secured by residential mortgages	34,919

Operational risk

	Consolidated	
	Implied Risk-Weighted Exposure Unaudited	Total Operational Risk Capital Requirement Unaudited
Dollars in Millions	30/9/16	30/9/16
Operational risk	4,375	350

The operational risk capital requirement above has been calculated under the Advanced Measurement Approach which the Banking Group uses for determining its regulatory capital for operational risk together with any required regulatory adjustments. The Advanced Measurement Approach is in accordance with BS2B.

Note 40 Capital Adequacy *continued*

Market risk

The table below shows market risk end of period and peak end-of-day capital charges.

	Consolidated 30/9/16 Unaudited			
	Implied Risk-Weighted Exposure	Peak	Aggregate Capital Charge	Peak
Dollars in Millions	End of Period	End-of-Day	End of Period	End-of-Day
Interest rate risk	2,836	3,581	227	286
Foreign exchange risk	42	97	3	8
Equity risk	12	12	1	1
Total market risk	2,890	3,690	231	295

The aggregate market risk exposure above is derived in accordance with BS2B and the Bank's conditions of registration.

For each category of market risk, the Banking Group's end of period aggregate capital charge is the charge as at the end of period reported. The peak end-of-day aggregate capital charge is the maximum over the half year accounting period at the close of each business day.

Equity risk subject to a market risk capital charge as shown above relates to equities owned by the Bank.

Capital for other material risks

The Banking Group actively manages and measures all material risks affecting its operations. These risks go beyond the traditional banking risks of credit, operational and market risk. The measurement and management of all material risks is determined under the Banking Group's ICAAP and includes consideration of all other material risks, additional to those included in determining the minimum regulatory capital requirements under BS2B. Other material risks assessed by the Banking Group include liquidity risk, funding risk, contagion risk, concentration risk, pension risk, regulatory and compliance risk and strategic risk.

As at 30 September 2016, the Banking Group had an internal capital allocation for strategic business risk of $157 million (30 September 2015: $95 million).

National Australia Bank Limited capital adequacy

The table below shows the capital adequacy ratios based on APRA capital adequacy standards, expressed as a percentage of total risk-weighted assets.

	Ultimate Parent Banking Group		Ultimate Parent Bank	
	Unaudited	Unaudited	**Unaudited**	Unaudited
Dollars in Millions	**30/9/16**	30/9/15	**30/9/16**	30/9/15
Common Equity Tier One capital ratio	**9.77%**	10.24%	**9.99%**	11.60%
Tier One capital ratio	**12.19%**	12.44%	**12.71%**	13.97%
Total qualifying capital ratio	**14.14%**	14.15%	**14.80%**	15.78%

The ultimate parent banking group data is the Level 2 capital ratio (as published in the National Australia Bank Limited Pillar 3 report) and represents the consolidation of NAB and all its subsidiary entities, other than the non-consolidated subsidiaries as outlined in the Pillar 3 report. The Level 2 Group operates in multiple regulatory jurisdictions and applies a combination of Basel capital framework and standardised approaches depending on the prescribed prudential requirements within those jurisdictions. Further information on the Basel capital framework methodologies applied across the ultimate parent banking group is outlined in the Pillar 3 report.

The ultimate parent bank of the Banking Group is National Australia Bank Limited which reports under the Advanced approach for credit risk (other than for defined assets that are immaterial in terms of risk-weighted Assets or are not required to be treated as IRB under the Basel capital framework), and the Advanced Measurement Approach ("AMA") for operational risk. The ultimate parent bank capital ratios are effectively represented by the Level 1 capital ratios, which comprises National Australia Bank Limited and its subsidiary entities approved by APRA as part of the Extended Licensed Entity.

Under prudential regulations, NAB is required to hold capital above the prudential capital ratio ("PCR") as determined by APRA for both the Level 1 and Level 2 Groups. The PCR is prescribed on a bilateral basis, and is not publicly disclosed. National Australia Bank Limited met the minimum capital adequacy requirements set by APRA as at 30 September 2016.

National Australia Bank Limited is required to publicly disclose risk management and capital adequacy information as at the reporting date, as specified in APRA's Pillar 3 Prudential Standard APS 330 Capital Adequacy: Public Disclosure ("APS 330"). Updates are provided on a semi-annual and quarterly basis in accordance with the APS 330 reporting requirements.

National Australia Bank Limited's Annual Financial Report and Pillar 3 report, incorporating the requirements of APS 330, can be accessed at www.nab.com.au.

Note 41 Risk Management

Risk Management

Risk exists in all aspects of the Banking Group and the environment in which it operates. Risk is identified and managed as part of the Banking Group's risk management framework that starts with the BNZ Board approved Strategy, Risk Appetite and Financial Plans. Risk appetite is translated and cascaded to the businesses qualitatively (through risk policies, standards and operating procedures) and quantitatively (through the Banking Group's risk limits, settings and decision authorities).

Compliance with the risk management framework is non-negotiable. The operating model differentiates accountabilities using the Three Lines of Defence Model as follows:

- First line: Management (who owns the risks)
- Second line: Risk (who establish frameworks and provide insight, oversight and appetite)
- Third line: Internal Audit (who provide independent assurance)

Bank of New Zealand is regulated by the RBNZ and the Banking Group is also subject to the prudential reporting requirements of APRA as part of the NAB Group.

The key risks faced by the Banking Group include:

- Credit risk
- Traded market risk
- Non-traded market risk
- Liquidity risk
- Operational risk
- Compliance risk

Further details regarding the nature and extent of each key risk faced by the Banking Group, and how these risks are managed, are outlined as part of this note. Other risks faced by the Banking Group including strategic execution, regulatory and conduct risks are managed and overseen as part of the Banking Group's broader corporate governance structure and risk management framework as follows:

Board Governance

The Banking Group's corporate governance structure provides guidance for effective decision making in all areas of the Banking Group through:

- Strategic and operational planning
- Risk management and compliance
- Financial management and external reporting
- Succession planning and culture

The Board determines the most appropriate corporate governance practices for the Banking Group and is supported by a number of committees. The Board Risk Committee ("BRC") supports the framework for risk management across the Banking Group.

Executive Governance

At an executive level, risk is overseen by the Chief Executive Officer through the Risk Return Management Committee ("RRMC"), which leads management in respect of risk matters relating to culture, integrated governance processes, risk strategy and performance.

Internal audit function

The internal audit function is the responsibility of the Head of Internal Audit who reports to the New Zealand Regional Audit Committee ("NZRAC"), the Managing Director and CEO of BNZ and to the Executive General Manager, NAB Group Audit. Audits are conducted using a risk-based approach to assess key business risks and internal control systems. Both core banking and specialist functions are audited with high risk areas covered regularly.

NZRAC assists the Board to fulfill its statutory and fiduciary responsibilities relating to accounting and financial controls, reporting systems and processes of the Banking Group and to oversee the internal audit function.

Note 41 Risk Management *continued*

External auditor and credit rating agencies

As part of their work in issuing an auditor's independent review report on the Banking Group's six month Disclosure Statement or an auditor's independent audit report on the Banking Group's year end Disclosure Statement, the Banking Group's external auditor, Ernst & Young, may review parts of the Banking Group's risk management framework that impact significant aspects of the financial systems, to the extent necessary to form their independent review or audit opinion.

Credit rating agencies also conduct periodic reviews of the Banking Group's risk management approach and risk profile.

Strategy in using financial instruments

By their nature, the Banking Group's activities involve the use of financial instruments. The core activity of the Banking Group is to accept deposits from customers at both fixed and floating rates for various periods, and seek to earn interest margins by investing these funds. The Banking Group also deals in a range of other financial products including derivatives and foreign exchange contracts where the Bank has deemed it has the expertise in the relevant market and infrastructure to support management processes.

Executing this strategy may result in market risk for the Banking Group, which is the risk of financial loss from unfavourable movements in market variables such as interest or foreign exchange rates. The Banking Group may use financial instruments to mitigate this market risk or selectively position for favourable movements in these market variables. The Board places limits on the level of market risk exposure that can be taken from these activities while a comprehensive governance structure is in place to ensure compliance with the Banking Group's risk appetite. This includes independent risk oversight teams which provide oversight over the Banking Group's market risk exposures and escalate any limit breaches.

The Banking Group's activities are divided into traded market risk and non-traded market risk. The differences between the two, including the measures used to control the level of market risk exposure, are documented further in this note.

Traded market risk

Financial instruments designated as traded market risk include those which:

- are held for short term resale;
- are taken on by the Banking Group with the intention of benefiting in the short term from actual and/or expected differences between their buying and selling prices, or from other price or interest rate variations; or
- arise from broking and market making.

The trading activities of the Banking Group are principally carried out by BNZ Markets.

The types of market risk arising from these activities include interest rate, foreign exchange, commodity, credit spread and volatility risk.

Independent oversight of traded market risk, including compliance with market risk limits, is undertaken by the traded market risk team, which reports through to the Chief Risk Officer. Governance is provided by the Market Risk Committee, which is a subcommittee of the Banking Group's RRMC.

All trading activities are subject to the disciplines prescribed in the National Australia Bank Group Market Risk Policy which is approved by the National Australia Bank Limited Board. This includes the use of the Value at Risk ("VaR") methodology.

Objectives and limitations of the VaR methodology

VaR is an estimate of potential loss resulting from shifts in market variables such as interest rates, foreign exchange rates, traded credit spreads, option volatility, and commodity prices. The estimate is calculated on an entire trading portfolio basis, which includes all financial instruments and derivatives.

VaR is calculated using the historical simulation method. This method involves multiple revaluations of the trading books using two years of historical pricing shifts. The pricing data is updated daily so as to have the most recent two-year history of prices. The results are ranked and the loss at the 99th percentile confidence interval identified. The calculation and rate shifts used assume a one day holding period for all positions.

The use of a VaR methodology has limitations, which include:

- the historical data used to calculate VaR is not always an appropriate proxy for current market conditions. If market volatility or correlation conditions change significantly, losses may occur more frequently and to a greater magnitude than in the VaR measure suggests;
- the VaR methodology assumes that positions are held for one day and may underestimate losses on positions that cannot be hedged or reversed inside that timeframe;
- VaR is calculated on positions at the close of each trading day, and does not measure risk on positions taken and closed before the end of each trading session; and
- VaR does not describe the directional bias or size of the positions generating the risk.

VaR estimates are checked against profit/loss via back testing for reasonableness and to assess the continued relevance of the model assumptions.

Note 41 Risk Management *continued*

The following table shows the Banking Group VaR for the trading portfolio, including both physical and derivative positions:

	Consolidated							
	As At		Average Value During Year		Minimum Value During Year		Maximum Value During Year	
Dollars in Millions	30/9/16	30/9/15	30/9/16	30/9/15	30/9/16	30/9/15	30/9/16	30/9/15
VaR at a 99% confidence level								
Foreign exchange risk	0.70	0.16	0.34	0.26	0.03	0.04	1.49	0.99
Interest rate risk	1.19	1.29	1.24	1.76	0.58	0.79	1.93	3.53
Volatility risk	0.02	0.01	0.01	0.02	-	-	0.05	0.04
Commodities risk	-	-	-	-	-	-	-	-
Credit spread risk	0.26	0.31	0.31	0.33	0.15	0.22	0.54	0.56
Diversification benefit	(0.81)	(0.52)	(0.56)	(0.59)	(0.18)	(0.30)	(1.79)	(1.60)
Total VaR for physical and derivative positions	1.36	1.25	1.34	1.78	0.58	0.75	2.22	3.52

VaR is measured individually for foreign exchange risk, interest rate risk, volatility, commodities and credit spread risk. The individual risk categories do not sum up to the total risk number due to diversification benefits.

Due to the limitations of the measure, VaR is supplemented with stress testing which is reported daily and also by other measures such as foreign exchange limits, basis point sensitivity limits, stop loss limits, and profit/loss referral levels.

Foreign exchange risk

Foreign exchange risk results from exposures to changes in foreign exchange rates. Currency risk arises from foreign currency balances and the trading of any foreign currency denominated product.

Foreign exchange limits are in place to control the level of foreign currency exposure run by the Banking Group. This exposure is measured by calculating the net present value position of the products the Banking Group deals in which are denominated in a non-New Zealand dollar currency. This includes foreign currency loans and deposits, foreign currency cash balances and the trading of foreign currency denominated products, such as spot and forward contracts, currency options, foreign currency interest rate derivatives and foreign currency securities.

An analysis of the net open position by currency is shown in the following table. The net open position in each currency represents the net of the non-derivative assets and liabilities in that currency aggregated with the net expected cash flows from derivative financial instrument purchases and sales from foreign exchange transactions in that currency including foreign currency options and futures and the principal on currency swaps. The amounts are stated in New Zealand dollar equivalents translated using the spot exchange rates as at the reporting date.

Net open position

	Consolidated	
Dollars in Millions	30/9/16	30/9/15
US dollar	32	8
Australian dollar	-	4
Japanese yen	5	4
Pound sterling	1	1
Euro	(2)	(8)
Swiss franc	1	-
Other	3	1

Non-traded market risk

Non-traded market risk includes all market risks which are not designated as traded market risk. Non-traded market risk largely consists of structural interest rate risk in the balance sheet arising from loans and deposits, and also liquidity and funding risk.

Policies, inclusive of risk appetite and limits, are approved by the National Australia Bank Limited Board and noted by the relevant Bank of New Zealand risk committee.

Independent oversight of the Banking Group's banking activities, including compliance with limits, is undertaken by the Balance Sheet and Liquidity risk team, which reports through to the Chief Risk Officer. Governance is provided by the Banking Group's ALCCO, which is a subcommittee of the Banking Group's RRMC.

Note 41 Risk Management *continued*

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the fair value of a financial instrument will fluctuate because of changes in market interest rates.

Interest rate risks primarily result from exposures to changes in the level, slope and curvature of the yield curve, the volatility of interest rates, mortgage prepayment speeds and credit spreads. The Banking Group has exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Exposure to interest rate risk arises in respect of the following activities: borrowing from and lending to customers; borrowing to fund the Banking Group in both domestic and international wholesale debt markets; trading and investing in money market instruments such as government stock, bank bills, commercial paper; foreign exchange instruments such as foreign exchange contracts; and derivative financial instruments such as swaps, options and futures.

Interest rate risk for non-traded market risk is measured, managed and monitored regionally using VaR and Earnings at Risk ("EaR") limits, complemented by cash flow analysis, basis point sensitivity and stress testing limits, and loss referral levels.

Similar to the methodology applied for traded market risk, VaR is calculated using the historic simulation method. Due to the generally longer holding period for non-traded products, the parameters applied differ. The key parameters for measuring non-traded market risk are as follows:

- 99% confidence level;
- three-month holding period;
- eight years of historical data;
- rate changes are proportional rather than absolute;
- investment term for capital is three years; and
- investment term for core "Non-Interest Bearing" liabilities (the sum of low and non-interest rate bearing liabilities) is five years.

EaR is the amount of the VaR that could accrue as lost net interest income over the next 12 months (the forecast period). VaR exposures are measured and reported weekly and EaR exposures are measured and reported monthly.

The table below shows the aggregate VaR figures for non-traded market risk:

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
VaR for physical and derivative positions at a 99% confidence level		
New Zealand		
As at end of year	**4**	10
Average value during year ended	**14**	18
Minimum value during year ended	**4**	9
Maximum value during year ended	**26**	25

The table below shows the aggregate EaR figures for non-traded market risk:

	Consolidated	
Dollars in Millions	**30/9/16**	30/9/15
EaR for physical and derivative positions at a 99% confidence level		
New Zealand		
As at end of year	**4**	12
Average value during year ended	**11**	16
Minimum value during year ended	**4**	7
Maximum value during year ended	**26**	28

Note 41 Risk Management *continued*

Interest rate repricing schedule

The following tables represent a breakdown of the balance sheet by repricing dates or contractual maturity, whichever is the earlier. As interest rates and yield curves change over time, the Banking Group may be exposed to a loss in earnings due to the characteristics of the assets and their corresponding liability funding. These mismatches are actively managed as part of the overall interest rate risk management process. In managing the structural interest rate risk, the primary objectives are to limit the extent to which net interest income could be impacted from an adverse movement in interest rates and to maximise shareholders' earnings.

	Consolidated (30/9/16)						
Dollars in Millions	Total	Up to 3 Months	Over 3 Months and up to 6 Months	Over 6 Months and up to 1 year	Over 1 Year and up to 2 Years	Over 2 Years	Not Interest Bearing
Assets							
Cash and liquid assets	1,799	1,446	-	-	-	-	353
Due from central banks and other institutions	2,299	2,283	16	-	-	-	-
Trading securities	4,703	4,703	-	-	-	-	-
Derivative financial instruments	7,319	-	-	-	-	-	7,319
Gross loans and advances to customers	74,693	41,910	3,603	9,096	11,318	7,238	1,528
Deductions from loans and advances to customers	(315)	-	-	-	-	-	(315)
Amounts due from related entities	934	826	-	-	-	-	108
All other assets	1,109	-	-	-	-	-	1,109
Total assets	92,541	51,168	3,619	9,096	11,318	7,238	10,102
Liabilities							
Due to central banks and other institutions	1,244	1,154	41	28	14	6	1
Short term debt securities	6,030	5,237	793	-	-	-	-
Trading liabilities	72	72	-	-	-	-	-
Derivative financial instruments	7,786	-	-	-	-	-	7,786
Deposits from customers	51,481	30,092	8,259	5,749	1,743	1,022	4,616
Bonds and notes	16,723	2,705	1,219	455	4,203	8,141	-
Amounts due to related entities	434	375	-	-	-	-	59
Other liabilities	844	-	-	-	-	-	844
Subordinated debt	922	380	-	-	-	542	-
Total liabilities	85,536	40,015	10,312	6,232	5,960	9,711	13,306
Shareholders' equity							
Total shareholders' equity	7,005	-	-	-	-	-	7,005
Total liabilities and shareholders' equity	92,541	40,015	10,312	6,232	5,960	9,711	20,311
On-balance sheet sensitivity gap	-	11,153	(6,693)	2,864	5,358	(2,473)	(10,209)
Derivative financial instruments							
Net balance of derivative financial instruments	-	(10,421)	7,214	(1,440)	(2,584)	7,231	-
Interest sensitivity gap - net	-	732	521	1,424	2,774	4,758	(10,209)
Interest sensitivity gap - cumulative	-	732	1,253	2,677	5,451	10,209	-

Note 41 Risk Management *continued*

Interest rate repricing schedule *continued*

Dollars in Millions	Total	Up to 3 Months	Over 3 Months and up to 6 Months	Over 6 months and up to 1 year	Over 1 Year and up to 2 Years	Over 2 Years	Not Interest Bearing
	Consolidated (30/9/15)						
Assets							
Cash and liquid assets	1,634	1,279	-	-	-	-	355
Due from central banks and other institutions	2,009	2,009	-	-	-	-	-
Trading securities	4,918	4,918	-	-	-	-	-
Derivative financial instruments	7,895	-	-	-	-	-	7,895
Gross loans and advances to customers*	68,430	37,846	2,006	5,197	14,370	7,602	1,409
Deductions from loans and advances to customers	(214)	-	-	-	-	-	(214)
Amounts due from related entities	1,259	1,229	-	-	-	-	30
All other assets	856	-	-	-	-	-	856
Total assets	86,787	47,281	2,006	5,197	14,370	7,602	10,331
Liabilities							
Due to central banks and other institutions	1,439	1,399	7	12	17	3	1
Short term debt securities	5,027	4,894	133	-	-	-	-
Trading liabilities	51	51	-	-	-	-	-
Derivative financial instruments	8,310	-	-	-	-	-	8,310
Deposits from customers	46,729	28,841	5,946	5,588	1,640	1,026	3,688
Bonds and notes	16,156	3,542	342	836	1,896	9,540	-
Amounts due to related entities	380	318	-	-	-	-	62
Other liabilities	938	-	-	-	-	-	938
Subordinated debt	715	715	-	-	-	-	-
Total liabilities	79,745	39,760	6,428	6,436	3,553	10,569	12,999
Shareholders' equity							
Total shareholders' equity	7,042	-	-	-	-	-	7,042
Total liabilities and shareholders' equity	86,787	39,760	6,428	6,436	3,553	10,569	20,041
On-balance sheet sensitivity gap	-	7,521	(4,422)	(1,239)	10,817	(2,967)	(9,710)
Derivative financial instruments							
Net balance of derivative financial instruments	-	(9,581)	7,017	2,342	(7,676)	7,898	-
Interest sensitivity gap - net	-	(2,060)	2,595	1,103	3,141	4,931	(9,710)
Interest sensitivity gap - cumulative	-	(2,060)	535	1,638	4,779	9,710	-

* September 2015 restated due to change in methodology of interest earning assets to exclude mortgage offset accounts.

Equity risk

Equity risk results from exposures to changes in the price of individual equities, equity baskets and equity indices. Management reviews the Banking Group's exposure to any equity risk on a monthly basis.

Liquidity risk

Maintaining adequate liquidity to meet current and future payment obligations is a core objective of the Banking Group.

The following are types of liquidity risks:

- Intra-Day: Ability of the Banking Group to meet its intra-day collateral requirements in relation to its clearing and settlement obligations
- Operational: Ability of the Banking Group to meet its refinancing requirements for a predefined period, e.g. up to 30 days
- Structural: Liquidity Risk profile of the balance sheet to accommodate the Banking Group's Strategic Plan and risk appetite

The Banking Group manages liquidity risk through a combination of positive cash flow management, the maintenance of portfolios containing high quality liquid assets and maintenance of a prudent funding strategy. The Banking Group undertakes a conservative approach by imposing internal limits that are in addition to regulatory requirements.

The BNZ Board has the ultimate responsibility to monitor and review the adequacy of the Banking Group's liquidity compliance and management framework with the guidance of the Banking Group's BRC. To aid in the fulfilment of its guidance responsibilities the BRC receives recommendations from the Banking Group's RRMC and regular reports on the Banking Group's liquidity management activity, risk limits and sensitivity metrics. The ALCCO is responsible for approval, and providing overview, of the execution of the liquidity strategy and escalation of issues to the RRMC.

The Banking Group is subject to RBNZ's liquidity requirements (as set out in the RBNZ's Liquidity Policy (BS13/BS13A) ("BS13")). Consistent with the requirements of BS13, liquidity risk is measured and managed in the Banking Group on a cash flow mismatch and also core funding basis to ensure that the Banking Group exceeds RBNZ's specified minimum standards for these metrics. The Banking Group maintains an Internal Liquidity Adequacy Assessment framework that meets the requirements set out in BS13.

Note 41 Risk Management *continued*

Liquidity risk *continued*

The Banking Group also complies with APRA's prudential standard APS 210 "Liquidity" ("APS 210") as a member of NAB. In accordance with the requirements of APS 210, liquidity risk is measured and managed in the Banking Group on a cash flow basis.

The Liquidity Coverage Ratio ("LCR"), a Basel III requirement, came into effect on 1 January 2015. The LCR requires a bank to hold sufficient high quality liquid assets to cover its total net cash outflows over a 30 day period.

The Banking Group is required to monitor both 'one week' and 'one month' mismatches. Cash flow mismatch limits have been established to limit the Banking Group's exposure in these time buckets.

The ability to realise assets quickly is an important source of liquidity for the Banking Group. The Banking Group holds sizeable balances of high quality assets such as cash and securities that are acceptable under repurchase agreements with the RBNZ to meet these needs.

A three-level contingency plan has been established for the management of an escalated liquidity event where the Banking Group experiences either restricted access to wholesale funding, or a large increase in the withdrawal of funds. The plan identifies triggers at each level, details the actions required, allocates the key tasks to individuals, provides timeframes and defines a management committee to oversee the action plan.

Maturity profile

The tables on pages 74 and 75 present the Banking Group's cash flows by remaining contractual maturities as at the reporting date, except Trading securities and Trading liabilities, which the Banking Group has the ability to realise at short notice and are presented by expected maturity.

The gross cash flows disclosed hereafter are the contractual undiscounted cash flows and include both principal and associated future interest payments and therefore will not agree to the carrying values on the balance sheet. Actual cash flows can differ significantly from contractual cash flows as a result of future actions of the Banking Group and its counterparties, such as early repayments or refinancing of term loans. Off-balance sheet exposures are excluded from the tables on pages 74 and 75 as contractual cash flows, if any, are contingent in nature. Irrevocable commitments to extend credit can be drawn down at any time before the commitments expire. Details of off-balance sheet exposures are included in note 36. Other assets and other liabilities only include balances which have contractual future cash flows.

			Consolidated (30/9/16)				
Dollars in Millions	Carrying Amount	Gross Cash Inflow/ (Outflow)	On Demand	3 Months or less	3 to 12 Months	1 to 5 Years	Over 5 Years
Assets							
Cash and liquid assets	1,799	1,799	1,799	-	-	-	-
Due from central banks and other institutions	2,299	2,300	-	2,292	8	-	-
Trading securities	4,703	4,703	-	4,703	-	-	-
Loans and advances to customers	74,378	92,035	5,998	14,974	9,067	24,764	37,232
Amounts due from related entities	934	953	89	633	21	210	-
Other assets	460	460	-	460	-	-	-
Total	84,573	102,250	7,886	23,062	9,096	24,974	37,232
Liabilities							
Due to central banks and other institutions	(1,244)	(1,248)	(576)	(570)	(74)	(28)	-
Short term debt securities	(6,030)	(6,048)	-	(3,855)	(2,193)	-	-
Trading liabilities	(72)	(72)	-	(72)	-	-	-
Deposits from customers	(51,481)	(52,022)	(23,677)	(11,102)	(14,307)	(2,936)	-
Bonds and notes	(16,723)	(17,374)	-	(232)	(2,069)	(14,136)	(937)
Amounts due to related entities	(434)	(434)	(349)	(78)	(7)	-	-
Other liabilities	(720)	(720)	-	(720)	-	-	-
Subordinated debt	(922)	(1,251)	-	(10)	(29)	(157)	(1,055)
Total	(77,626)	(79,169)	(24,602)	(16,639)	(18,679)	(17,257)	(1,992)
Derivatives*							
Derivative financial instruments inflow		120,243	-	49,433	24,303	36,080	10,427
Derivative financial instruments (outflow)		(121,359)	-	(49,468)	(24,755)	(36,847)	(10,289)

* Derivative financial instruments includes hedging and trading derivative cash flows.

Note 41 Risk Management *continued*

Maturity profile *continued*

Dollars in Millions	Carrying Amount	Gross Cash Inflow/ (Outflow)	Consolidated (30/9/15) On Demand	3 Months or less	3 to 12 Months	1 to 5 Years	Over 5 Years
Assets							
Cash and liquid assets	1,634	1,634	1,634	-	-	-	-
Due from central banks and other institutions	2,009	2,010	-	2,010	-	-	-
Trading securities	4,918	4,918	-	4,918	-	-	-
Loans and advances to customers	68,216	93,559	6,085	12,654	8,389	25,594	40,837
Amounts due from related entities	1,259	1,299	9	1,038	24	26	202
Other assets	296	296	-	296	-	-	-
Total	78,332	103,716	7,728	20,916	8,413	25,620	41,039
Liabilities							
Due to central banks and other institutions	(1,439)	(1,440)	(655)	(745)	(19)	(21)	-
Short term debt securities	(5,027)	(5,044)	-	(3,259)	(1,785)	-	-
Trading liabilities	(51)	(51)	-	(51)	-	-	-
Deposits from customers	(46,729)	(47,341)	(21,930)	(10,708)	(11,872)	(2,831)	-
Bonds and notes	(16,156)	(16,817)	-	(282)	(2,750)	(13,096)	(689)
Amounts due to related entities	(380)	(380)	(335)	(32)	(13)	-	-
Other liabilities	(768)	(768)	-	(768)	-	-	-
Subordinated debt	(715)	(843)	-	(6)	(18)	(98)	(721)
Total	(71,265)	(72,684)	(22,920)	(15,851)	(16,457)	(16,046)	(1,410)
Derivatives*							
Derivative financial instruments inflow		123,893	-	53,049	24,567	36,782	9,495
Derivative financial instruments (outflow)		(125,201)	-	(53,008)	(25,314)	(37,328)	(9,551)

* Derivative financial instruments includes hedging and trading derivative cash flows.

Liquidity portfolio management

The table below shows financial assets held by the Banking Group for the purpose of managing liquidity risk.

Dollars in Millions	**Consolidated** 30/9/16	30/9/15
Cash and balances immediately convertible to cash	**1,799**	2,167
Securities purchased under agreements to resell	**651**	327
Government bonds, notes and securities**	**3,002**	2,384
Semi-government bonds, notes and securities	**510**	749
Corporate and other institution bonds, notes and securities	**952**	1,513
Total liquidity portfolio	**6,914**	7,140

** Government bonds, notes and securities that are encumbered through repurchase agreements have been excluded in the above table as they are not held for liquidity management purposes.

As at 30 September 2016, the Banking Group also held unencumbered RMBS of $4,491 million (30 September 2015: $4,491 million) of which $4,300 million can be sold to RBNZ under agreements to repurchase for liquidity purposes. These RMBS are secured by residential housing loans and other assets. Refer to note 11 for further information. The Banking Group had not entered into any repurchase agreements for residential mortgage-backed securities with the RBNZ as at 30 September 2016 (30 September 2015: nil).

There is a standby liquidity facility, which is reviewed annually, provided from National Australia Bank Limited for the Banking Group's liquidity management. Refer to note 30 for further information.

Note 41 Risk Management *continued*

Concentrations of funding

The Banking Group's concentrations of funding is reported by geographical location and industry sector in the following table. The concentrations of funding by geographical location is based on the geographical location of the office in which the funds are recognised. The concentrations of funding by industry sector is based on the categories in the RBNZ M3 Institutions Standard Statistical Return.

		Consolidated	
Dollars in Millions	Note	30/9/16	30/9/15
New Zealand			
Agriculture, forestry and fishing		2,210	2,144
Mining		72	65
Manufacturing		1,295	1,117
Electricity, gas and water		152	84
Construction		717	622
Wholesale and retail trade		1,541	1,294
Accommodation, restaurants, culture and recreation		954	911
Transport and storage		621	490
Communications		186	119
Financial, investment and insurance		15,002	13,523
Property, business and personal services		8,750	7,994
Government, education, health and community services		2,777	2,399
Personal deposits		25,502	23,223
Related entities	30	814	1,095
Total New Zealand		60,593	55,080
United Kingdom *			
Financial, investment and insurance		16,313	15,417
Total United Kingdom		16,313	15,417
Total funding		76,906	70,497
Total funding comprised:			
Due to central banks and other institutions		1,244	1,439
Short term debt securities		6,030	5,027
Trading liabilities		72	51
Deposits from customers		51,481	46,729
Bonds and notes		16,723	16,156
Amounts due to related entities		434	380
Subordinated debt **		922	715
Total funding		76,906	70,497

* This represents the funding activities of BNZ-IF which are sourced worldwide. Refer to notes 20 and 22.

** Includes subordinated debt of $380 million due to related entities as at 30 September 2016 (30 September 2015: $715 million). Refer to note 24 for further information.

Operational and compliance risk

Operational risk is the risk of loss resulting from inadequate or failed processes, people, systems or from external events. The Banking Group has adopted the NAB Group's Operational Risk Framework, which sets out the principles for managing operational risks across the Banking Group.

Compliance risk is the risk of legal or regulatory sanctions resulting from failure to understand and comply with laws, regulations, licence conditions, supervisory requirements, self-regulatory industry codes of conduct, as well as internal policies, procedures, organisational frameworks and standards. The NAB Compliance Framework sets out the principles for managing compliance risks across the Banking Group.

Effective operational and compliance risk management within the Banking Group is based upon a three lines of defence model. The Banking Group's business units are the first line of defence and are accountable for management of their risks. Oversight is provided by the operational risk and compliance team and divisional Chief Risk Officers (second line of defence) who report to the Banking Group's Chief Risk Officer. Assurance is provided by the internal audit function (third line of defence).

The primary roles of the operational and compliance risk function are policy making; advisory and support, including monitoring and oversight; the assessment of new and re-engineered products and processes; business continuity; risk measurement and control; and reporting. The team also provides subject matter expertise and additional assistance to business units and identifies systemic trends across the business.

The Banking Group is accredited by the RBNZ to use the Advanced Measurement Approach ("AMA") for operational risk. As a result, the Bank calculates its operational risk implied risk-weighted exposure and resultant capital requirement (including any required regulatory adjustments) as required by BS2B.

Note 41 Risk Management *continued*

Operational and compliance risk *continued*

The Banking Group's quantitative operational risk measurement approach is based on the AMA and uses the factors below to estimate the aggregate loss distribution for total operational risk losses over a 12-month horizon:

- internal loss data;
- relevant external loss data;
- consideration of business environment and controls; and
- the outputs of a scenario analysis process.

The operational risk calculations are performed on an aggregate Bank-wide basis, and the resultant capital is allocated across major business lines. At present, no adjustment is made to regulatory capital to account for expected losses, or for the mitigating effect of the Bank's insurance programme.

Conduct risk is inherent in the Banking Group's business activities. Conduct Risk is the risk of the Banking Group intentionally or unintentionally treating its customers unfairly and delivering negative outcomes for customers, clients, counterparties, investors, shareholders and the markets in which the Banking Group operates resulting from inappropriate, unlawful or unethical judgements made during the execution of the Banking Group's business activities. Conduct Risk is managed by leveraging policies, processes and tools used for other material risk types, such as operational risk, compliance risk and regulatory risk. For capital adequacy purposes, conduct risk is part of the calculation of operational risk capital.

Credit risk

Credit risk is the risk of financial loss resulting from the failure of a customer to settle their financial and contractual obligations to the Banking Group as they fall due.

Bank lending activities account for most of the Banking Group's credit risk, however other sources of credit risk also exist throughout the Banking Group. These activities include the trading book, and other financial instruments and loans, as well as in the extension of commitments and guarantees and the settlement of transactions.

Administration of the Banking Group's credit policies and procedures is the responsibility of the Risk division of the Banking Group. All loans are subject to a customer rating which estimates the probability of default derived from historical default data. There are monitoring procedures and systems in place to control exposures to individual customer, geographical and industry segments to ensure diversification and asset quality are maintained. Exposure to any one customer is further restricted by sub-limits covering on and off-balance sheet exposures, and daily settlement risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored on a daily basis. Lending authorities are delegated from the National Australia Bank Limited's Board through the Group Chief Credit Officer with approval to sub-delegate to business units. Individual lending authorities are allocated according to demonstrated skills, accreditation, and experience. Consequences are in place for any breaches of these authorities.

Exposure to credit risk is managed through regular analysis of the ability of existing or potential counterparties, customers, groups of related counterparties or groups of related customers to meet interest and capital repayment obligations and by changing limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

The Banking Group continuously monitors its credit risk to counterparties through the examination of key risk indicators such as irregular or delinquent accounts and early warning signals. In addition, there are specialist units such as Credit Risk Assurance which undertake regular reviews of loan portfolios and Strategic Business Services which has specific responsibility for the management of accounts classified as categorised assets. These processes enable doubtful debts to be identified at the earliest possible time. Impairment provisions are raised based on an expected credit loss model in line with the requirements of NZ IFRS 9. Recoverable amounts for impaired assets take into account the current market value of collateral held and the realisability of securities.

The following section discloses the Bank's policies and procedures for collateral taken to mitigate credit risk.

Due from central banks and other institutions

Due from central banks and other institutions comprise primarily collateral on securities borrowing and reverse repurchase agreements with financial institutions, which are permitted to be sold or re-pledged. Securities borrowing and reverse repurchase agreements are collateralised with highly liquid securities which are permitted to be sold or re-pledged. The fair values of this collateral are disclosed in note 9.

Balances held with central supervisory banks and other interest bearing assets that are due from other banks are managed based on the counterparty's creditworthiness. The Banking Group will utilise master netting arrangements where possible to reduce its exposure to credit risk.

Trading securities

The Banking Group has not accepted any collateral for Trading securities. The Banking Group may utilise credit derivatives, guarantees provided by central banks or other forms of credit enhancements or collateral in order to minimise the Banking Group's exposure to credit risk.

Derivative financial instruments

The Banking Group uses documentation including ISDA Master Agreements to document derivative activities. Under the ISDA Master Agreements, if a counterparty defaults, all contracts with that counterparty are terminated. They are then settled on a net basis at market rates current at the time of settlement. The Banking Group also executes Credit Support Annexures in conjunction with ISDA Master Agreements.

Gross loans and advances to customers

The majority of Gross loans and advances to customers comprise general lending and line of credit products. The distinction in classification is reflective of the type of lending product. These lending and line of credit products will generally have a significant level of collateralisation depending on the nature of the product.

Credit card outstandings are mostly unsecured. However, where the borrower has provided collateral for other lending, the collateral can also be available to secure any credit card debt.

Housing loans are secured by mortgages over residential properties. LVR thresholds range up to, or exceed 100% in limited circumstances, including remediation of damaged properties that are held by the Banking Group as security. Further details on LVR are provided in note 40.

Note 41 Risk Management *continued*

Credit risk *continued*

Overdrafts and Other term lending to non-retail customers are mostly secured by acceptable collateral (highly rated investment grade institutional clients may borrow on an unsecured basis). Collateral generally comprises commercial or agricultural properties, business assets, inventories, and in some cases personal assets of the borrower (e.g. residential properties). The Banking Group manages its exposure to these products by completing a credit evaluation to assess the customer's character, industry, business model and capacity to meet their commitments. Collateral provides a secondary source of repayment in the event that a customer cannot meet its contractual repayment obligations.

Amounts due from related entities

Depending on the nature of the transaction entered into, collateral may be taken to secure such exposures.

Credit quality of financial assets

The Banking Group has an internally developed credit rating master-scale derived from historical default data drawn from a number of sources to assess the potential risk in lending or through providing other financial services products to counterparties or customers. For loans and advances, the Banking Group has a single common master-scale across all retail and non-retail counterparties for probability of default. The probability of default master-scale can be broadly mapped to external rating agencies and has performing (pre-default) and non-performing (post-default) grades.

In assessing for the impairment of financial assets under the expected credit loss model, the Banking Group defines default in accordance with its Credit Policy and Procedures, which includes defaulted assets and impaired assets as described below:

Defaulted assets consist of retail loans (excluding unsecured portfolio managed facilities) and non-retail loans which are at least 90 days past due on any material obligation.

Impaired assets under the expected credit loss model consist of:

- Retail loans: excluding unsecured portfolio managed facilities, which are contractually past due 90 days and there is sufficient doubt about the ultimate collectability of principal and interest;
- Non-retail loans: which are contractually past due 90 days, including loans where there is sufficient doubt about the ultimate collectability of principal and interest;
- Impaired off-balance sheet credit exposures where current circumstances indicate that losses may be incurred; and
- Unsecured portfolio managed facilities which are 180 days past due (if not written off).

An asset will migrate down the ECL stages as asset quality deteriorates by comparing the credit risk rating of the asset at reporting date with its credit risk rating at origination using the Banking Group's internal credit rating system. The trigger to move down an ECL stage is based on a pre-determined ratings downgrade shift that determines whether significant deterioration has occurred. Conversely, assets will migrate up an ECL stage as asset quality improves.

Credit risk exposures by risk grade

The table below shows significant exposures to credit risk to which the expected credit loss model is applied, for recognised and unrecognised financial assets at amortised cost, based on the following risk grades:

- Senior investment grade: broadly corresponds with Standard & Poor's ratings of AAA to A-;
- Investment grade: broadly corresponds with Standard & Poor's ratings of BBB+ to BBB-;
- Sub-investment grade: broadly corresponds with Standard & Poor's ratings of BB+; and
- Default: broadly corresponds with Standard & Poor's rating of D.

	Consolidated (30/9/16) Loans and advances and loan commitments for which the loss allowance is measured at:			
Dollars in Millions	12-months ECL	Lifetime ECL Not Credit Impaired	Lifetime ECL Credit Impaired	Total
Credit risk exposure by risk grade				
Senior investment grade	**22,392**	**-**	**-**	**22,392**
Investment grade	**26,280**	**536**	**-**	**26,816**
Sub-investment grade	**22,460**	**15,090**	**-**	**37,550**
Default	**-**	**5**	**1,323**	**1,328**
Total	**71,132**	**15,631**	**1,323**	**88,086**
	Consolidated (30/9/15)			
Credit risk exposure by risk grade				
Senior investment grade	20,458	-	-	20,458
Investment grade	22,558	1,057	-	23,615
Sub-investment grade	19,845	14,258	-	34,103
Default	-	-	752	752
Total	62,861	15,315	752	78,928

Note 41 Risk Management *continued*

Concentrations of credit exposure

The Banking Group's concentrations of credit exposure is reported by geographical location and industry sector in the table below. The concentrations of credit exposure on financial assets by geographical location is based on the geographical location of the counterparty's tax residency. The concentrations of credit exposure by industry sector is based on the categories in the RBNZ M3 Institutions Standard Statistical Return.

The table below presents the maximum exposure to credit risk of financial assets before taking into account any collateral held or other credit enhancements. Except for derivative financial instruments, the majority of the overseas credit exposures are raised for New Zealand based assets funded in New Zealand dollars for offshore customers. For more information on guarantees and credit related commitments, refer to note 36.

		Consolidated	
Dollars in Millions	Note	30/9/16	30/9/15
New Zealand			
Agriculture		**13,880**	13,287
Forestry and fishing		**991**	763
Mining		**192**	191
Manufacturing		**3,103**	3,422
Electricity, gas and water		**1,184**	991
Construction		**879**	867
Wholesale and retail trade		**3,487**	3,183
Accommodation, restaurants, culture and recreation		**1,082**	1,156
Transport and storage		**1,483**	1,243
Communications		**324**	334
Financial, investment and insurance		**8,776**	8,510
Property, business and personal services		**9,757**	8,449
Government, education, health and community services		**2,242**	1,917
Real estate - mortgage		**34,338**	31,307
Personal lending		**1,504**	1,624
Related entities	30	**227**	250
Total New Zealand		**83,449**	77,494
Overseas			
Agriculture		**9**	9
Manufacturing		**22**	-
Electricity, gas and water		**3**	3
Wholesale and retail trade		**6**	7
Accommodation, restaurants, culture and recreation		**7**	9
Communications		**3**	-
Financial, investment and insurance		**4,950**	4,723
Property, business and personal services		**113**	20
Government, education, health and community services		**11**	42
Real estate - mortgage		**576**	523
Personal lending		**17**	18
Related entities*	30	**2,446**	3,144
Total overseas		**8,163**	8,498
Total credit exposures		**91,612**	85,992
Total credit exposures comprised:			
Cash and liquid assets		**1,664**	1,481
Due from central banks and other institutions		**2,299**	2,009
Trading securities		**4,703**	4,918
Derivative financial instruments		**7,319**	7,895
Gross loans and advances to customers		**74,693**	68,430
Amounts due from related entities		**934**	1,259
Total credit exposures		**91,612**	85,992

* Includes derivative financial assets with related entities.

Note 41 Risk Management *continued*

Derivatives

The Banking Group maintains strict control limits on net open derivative positions (the difference between purchase and sale contracts), by both amount and term. At any one time, the amount subject to risk is limited to the current fair value of instruments that are favourable to the Banking Group (assets where their fair value is positive), which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding. This credit risk exposure is managed as part of the overall lending limits with customers, together with potential exposures from market movements. The requirement for collateral or other security for these instruments is assessed based on the creditworthiness of the counterparty.

Undrawn credit commitments

Undrawn credit commitments represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. The Banking Group is potentially exposed to credit risk for undrawn credit commitments for an amount equal to the total amount undrawn. However, the level of credit risk is mitigated through most commitments to extend credit being contingent upon customers maintaining specific credit standards. The Banking Group monitors the term to maturity of all credit commitments, drawn and undrawn, because longer term commitments generally have a greater degree of credit risk than shorter term commitments.

Note 42 Subsequent Events

On 20 October 2016, the Bank issued $900 million of mandatorily convertible subordinated perpetual unsecured notes (“Perpetual Notes”) to National Australia Bank Limited. The interest rate for the Perpetual Notes is fixed at 6.7539% per annum until 20 October 2021 and, thereafter, will be based on a floating interest rate. The Perpetual Notes qualify as Additional Tier One capital of the Bank for regulatory purposes.

The Board of the Bank has resolved to buy back the $200 million 2009A BNZ PPS issued to NAGNZ, to be effected on 28 December 2016.

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Independent Auditor's Report

To the Shareholders of Bank of New Zealand

Report on the Financial Statements (excluding Supplementary Information Relating to Capital Adequacy)
We have audited pages 8 to 80 of the Disclosure Statement of Bank of New Zealand (the "Bank"), which includes the financial statements required by Clause 24 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order") and the supplementary information required by Schedules 4, 7, 13 to 15 and 17 of the Order. The financial statements comprise the balance sheet as at 30 September 2016, the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information for the Banking Group. The Banking Group comprises the Bank and the entities it controlled at 30 September 2016 or from time to time during the year.

Directors' Responsibility for the Financial Statements (excluding the Supplementary Information Relating to Capital Adequacy)
The directors of the Bank are responsible, on behalf of the Bank, for the Disclosure Statement, which includes financial statements prepared in accordance with Clause 24 of the Order and New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards and that give a true and fair view of the matters to which they relate. The directors are also responsible, on behalf of the Bank, for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In addition, the directors are responsible, on behalf of the Bank, for including supplementary information in the Disclosure Statement which complies with Schedules 2, 4, 7, 13 to 15 and 17 of the Order.

Auditor's Responsibility (excluding the Supplementary Information Relating to Capital Adequacy)
Our responsibility is to express an opinion on the financial statements and the supplementary information disclosed in accordance with Clause 24 and Schedules 4, 7, 13 to 15 and 17 of the Order based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements (excluding the supplementary information relating to capital adequacy) whether due to fraud or error. In making those risk assessments, the auditor considers the internal control relevant to the Banking Group's preparation of the financial statements that give a true and fair view of the matters to which they relate, in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Banking Group's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the overall presentation of the financial statements.

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

Ernst & Young provides other assurance and remuneration benchmarking services to the Banking Group. 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 Banking Group. These matters have not impaired our independence as auditors of the Banking Group. We have no other relationship, or interest in the Banking Group.

Opinion
In our opinion the financial statements on pages 8 to 80 (excluding the supplementary information in Notes 12, 13, 29 and 37 to 41):

- comply with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards; and
- give a true and fair view of the financial position of the Banking Group as at 30 September 2016 and its financial performance and cash flows for the year then ended.

In our opinion, the supplementary information prescribed by Schedules 4, 7, 13 to 15 and 17 of the Order fairly states, in all material respects, the matters to which it relates in accordance with those schedules.

Report on Other Legal and Regulatory Requirements (excluding Supplementary Information relating to Capital Adequacy)
We also report in accordance with the requirements of Clauses 2(1)(d) and 2(1)(e) of Schedule 1 of the Order that in relation to our audit of the financial statements (excluding the supplementary information relating to capital adequacy disclosed in Note 40) for the year ended 30 September 2016:

- 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.

Auditor's Report

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Report on the Supplementary Information Relating to Capital Adequacy
We have reviewed the supplementary information relating to capital adequacy required by Schedule 11 of the Order as disclosed in Note 40 of the financial statements of the Banking Group for the year ended 30 September 2016.

Directors' Responsibility for the Supplementary Information Relating to Capital Adequacy
The directors are responsible for the preparation of the supplementary information relating to capital adequacy that is prepared in accordance with the Bank's conditions of registration and the Bank's internal models for credit risk and operational risk as accredited by the Reserve Bank of New Zealand and is disclosed in accordance with Schedule 11 of the Order.

Reviewer's Responsibilities for the Supplementary information Relating to Capital Adequacy

Our responsibility is to express a conclusion on the supplementary information relating to capital adequacy, disclosed in Note 40, based on our review.

We conducted our review in accordance with New Zealand Standard on Review Engagements 2410 Review of Financial Statements Performed by the Independent Auditor of the Entity (NZ SRE 2410). NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the supplementary information relating to capital adequacy, disclosed in Note 40, is not, in all material respects:

► prepared in accordance with the Bank's conditions of registration;
► prepared in accordance with the Bank's internal models for credit risk and operational risk as accredited by the Reserve Bank of New Zealand; and
► disclosed in accordance with Schedule 11 of the Order;

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

A review of the supplementary information relating to capital adequacy 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 International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on the supplementary information relating to capital adequacy.

Conclusion
Based on our review procedures, which are not an audit, nothing has come to our attention that causes us to believe that the supplementary information relating to capital adequacy disclosed in Note 40, as required by Schedule 11 of the Order, is not in all material respects:

► prepared in accordance with the Bank's conditions of registration;
► prepared in accordance with the Bank's internal models for credit risk and operational risk as accredited by the Reserve Bank of New Zealand; and
► disclosed in accordance with Schedule 11 of the Order.

Restriction on Distribution or Use
This report is made solely to the Bank's shareholders, as a body. Our work has been undertaken so that we might state to the Bank's shareholders those matters we are required to state to them in an 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 Bank and the Bank's shareholders, as a body, for our audit work, for this report, or for the opinions we have formed.

Ernst + Young

7 December 2016
Auckland

Credit Ratings

Bank of New Zealand has the following credit ratings applicable to its long term senior unsecured obligations payable in New Zealand, in New Zealand dollars.

Rating Agency	Current Credit Rating	Qualification
Standard & Poor's (Australia) Pty Limited	AA -	Outlook Negative
Moody's Investors Service Pty Limited	Aa3	Outlook Negative
Fitch Australia Pty Limited	AA-	Outlook Stable

During the two-year period ended 30 September 2016, there was no change to the Bank's Fitch Ratings issuer credit ratings.

During the two-year period ended 30 September 2016, Standard & Poor's (Australia) Pty Limited and Moody's Investors Service Pty Limited revised the credit rating outlook for a number of Australian banks and their New Zealand subsidiaries, including NAB and Bank of New Zealand, from "outlook stable" to "outlook negative".

The following is a summary of the descriptions of the major rating categories for rating agencies for the rating of long term obligations.

Standard & Poor's	Moody's Investors Service	Fitch Ratings	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.
A	A	A	Strong ability to repay principal and interest although somewhat susceptible to adverse changes in financial conditions.
BBB	Baa	BBB	Adequate ability to repay principal and interest. More vulnerable to adverse changes.
BB	Ba	BB	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	Caa	CCC	Likelihood of default considered high. Timely repayment of principal and interest is dependent on favourable financial conditions.
CC to C	Ca to C	CC to C	Highest risk of default.
D	-	RD & D	Obligations currently in default.

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

Conditions of Registration

The conditions of registration imposed on Bank of New Zealand by the Reserve Bank of New Zealand pursuant to section 74 of the Reserve Bank of New Zealand Act 1989 which were applicable as at the balance date of this Disclosure Statement are as follows:

Conditions of registration that apply on and after 1 November 2015 - Bank of New Zealand

The registration of Bank of New Zealand (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; and
   (e) the bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued after 1 January 2013 in the calculation of its capital ratios unless it has received a notice of non-objection to the instrument from the Reserve Bank; and
   (f) the bank meets the requirements of Part 3 of the Reserve Bank of New Zealand document "Application requirements for capital recognition or repayment and notification requirements in respect of capital" (BS16) dated November 2015 in respect of regulatory capital instruments.

   For the purposes of this condition of registration,

   the scalar referred to in the Reserve Bank of New Zealand document “Capital adequacy framework (Internal Models Based Approach)” (BS2B) dated November 2015 is 1.06;

   “Total capital ratio”, “Tier 1 capital ratio”, “Common Equity Tier 1 capital ratio”, and “Total capital” must be calculated in accordance with the Reserve Bank of New Zealand document: “Capital adequacy framework (Internal Models Based Approach)” (BS2B) dated November 2015;

   an Additional Tier 1 capital instrument is an instrument that meets the requirements of subsection 2.13(a) or (c) of the Reserve Bank of New Zealand document "Capital Adequacy Framework (Internal Models Based Approach)" (BS2B) dated November 2015.

   a Tier 2 capital instrument is an instrument that meets the requirements of subsection 2.16(a) or (c) of the Reserve Bank of New Zealand document "Capital Adequacy Framework (Internal Models Based Approach)" (BS2B) dated November 2015.

1A. That:
   (a) the bank has an internal capital adequacy assessment process (“ICAAP”) that accords with the requirements set out in the document “Guidelines on a bank’s internal capital adequacy assessment process (“ICAAP”)” (BS12) dated December 2007;
   (b) under its ICAAP the bank identifies and measures its “other material risks” defined as all material risks of the banking group that are not explicitly captured in the calculation of the Common Equity Tier 1 capital ratio, the Tier 1 capital ratio and the Total capital ratio under the requirements set out in the document “Capital Adequacy Framework (Internal Models Based Approach)” (BS2B) dated November 2015; and
   (c) the bank determines an internal capital allocation for each identified and measured “other material risk”.

1B. That the banking group complies with all requirements set out in the Reserve Bank of New Zealand document “Capital adequacy framework (Internal Models Based Approach)” (BS2B) dated November 2015.

1C. That, if the buffer ratio of the banking group is 2.5% or less, the bank must:
   (a) according to the following table, limit the aggregate distributions of the bank’s earnings to the percentage limit to distributions that corresponds to the banking group’s buffer ratio:

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

   (b) prepare a capital plan to restore the banking group’s buffer ratio to above 2.5% within any timeframe determined by the Reserve Bank for restoring the buffer ratio; and
   (c) have the capital plan approved by the Reserve Bank.

   For the purposes of this condition of registration,

   “buffer ratio”, “distributions”, and “earnings” have the same meaning as in Part 3 of the Reserve Bank of New Zealand document: “Capital Adequacy Framework (Internal Models Based Approach)” (BS2B) dated November 2015.

   the scalar referred to in the Reserve Bank of New Zealand document “Capital adequacy framework (Internal Models Based Approach)” (BS2B) dated November 2015 is 1.06

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.

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

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

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

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

   In determining the total amount of the banking group's insurance business:

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

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

   For the purposes of this condition of registration,

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

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

4. That the 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	Connected exposure limit (% of the banking group's Tier 1 capital)
AA / Aa2 and above	75
AA- / Aa3	70
A+ / A1	60
A / A2	40
A- /A3	30
BBB+ /Baa1 and below	15

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

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

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

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

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

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

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

   (d) an alternate director,—

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

      (ii) for an independent director must be independent;

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

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

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

   For the purposes of this condition of registration, "non-executive" and "independent" have 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, "non-executive" and "independent" have the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014.

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

11. That the bank will not, without first obtaining the written approval of the Reserve Bank, revoke the constitution of BNZ International Funding Limited or alter the constitution of BNZ International Funding Limited if such alteration would delete or amend or negate the effect of clause 2.2 of the constitution.

12. That:
    (a) the business and affairs of the bank are managed by, or under the direction or supervision of, the board of the bank;
    (b) the employment contract of the chief executive officer of the bank or person in an equivalent position (together "CEO") is with the bank, and the terms and conditions of the CEO's employment agreement are determined by, and any decisions relating to the employment or termination of employment of the CEO are made by, the board of the bank; and
    (c) all staff employed by the bank shall have their remuneration determined by (or under the delegated authority of) the board or the CEO of the bank and be accountable (directly or indirectly) to the CEO of the bank.

13. That the bank has legal and practical ability to control and execute any business, and any functions relating to any business, of the bank that are carried on by a person other than the bank, sufficient to achieve, under normal business conditions and in the event of stress or failure of the bank or of a service provider to the bank, the following outcomes:
    (a) that the bank's clearing and settlement obligations due on a day can be met on that day;
    (b) that the bank's financial risk positions on a day can be identified on that day;
    (c) that the bank's financial risk positions can be monitored and managed on the day following any failure and on subsequent days; and
    (d) that the bank's existing customers can be given access to payments facilities on the day following any failure and on subsequent days.

    For the purposes of this condition of registration, the term "legal and practical ability to control and execute" is explained in the Reserve Bank of New Zealand document entitled "Outsourcing Policy" (BS11) dated January 2006.

14. 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 per cent at the end of each business day;
    (b) the one-month mismatch ratio of the banking group is not less than zero per cent at the end of each business day; and
    (c) the one-year core funding ratio of the banking group is not less than 75 per cent 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 July 2014 and "Liquidity Policy Annex: Liquid Assets" (BS13A) dated December 2011.

15. 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.

16. 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.

17. 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.

18. 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.

19. 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).

    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.

20. That the bank has a compendium of liabilities that-
    (a) at the product-class level lists all liabilities, indicating which are-
        (i) pre-positioned for Open Bank Resolution; and
        (ii) not pre-positioned for Open Bank Resolution;
    (b) is agreed to by the Reserve Bank; and
    (c) if the Reserve Bank's agreement is conditional, meets the Reserve Bank's conditions.

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

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

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

22. That, for a loan-to-valuation measurement period, the total of the bank’s qualifying new mortgage lending amounts in respect of APIL with a loan-to-valuation ratio of more than 70%, must not exceed 5% of the total of the qualifying new mortgage lending amount in respect of APIL arising in the loan-to-valuation measurement period.

23. That, for a loan-to-valuation measurement period, the total of the bank's qualifying new mortgage lending amount in respect of ANPIL 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 APRIL arising in the loan to valuation measurement period.

Conditions of Registration

24. That, for a loan-to-valuation measurement period, the total of the bank's qualifying new mortgage lending amount in respect of non-Auckland loans with a loan-to valuation ratio of more than 80%, must not exceed 15% of the total of the qualifying new mortgage lending amount in respect of non-Auckland loans arising in the loan-to valuation measurement period.

25. 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 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 Bank of New Zealand (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 (unless paragraph (b) applies); or

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

In conditions of registration 22 to 25,-

"ANPIL", "APIL", "loan-to-valuation ratio", "non-Auckland loan", "qualifying new mortgage lending amount in respect of[...]" 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 November 2015:

"loan-to-valuation measurement period" means-

(a) the six calendar month period ending on the last day of April 2016; and

(b) thereafter a period of three calendar months ending on the last day of the third calendar month, the first of which ends on the last day of May 2016.

Changes in conditions of registration
The Bank’s Conditions of Registration were updated to include the following changes with effect on and after 1 October 2016, which in summary:

- Impose conditions of registration relating to residential mortgage lending nationwide to property investors and non-property investors. As signalled previously, the conditions allow only a small (5%) flow of investor mortgage lending with LVRs greater than 60%, and a 10% flow of non-property investor lending with LVRs above 80%.
- Refer to a revised version of “Framework for Restrictions on High-LVR Residential Mortgage Lending” (BS19) which amends some of the terms and conditions (including exemptions) relating to the LVR conditions of registration.

Non-compliance with conditions of registration
The Banking Group fully complied with all of the RBNZ’s capital requirements as set out in the Bank’s conditions of registration since 30 September 2015, except that the Bank:

- did not have the required RBNZ approvals in place for three of its capital models on 1 July 2014 when a revised version of BS2B came into effect. As a result of its failure to have obtained the required RBNZ approvals, the Bank had been in breach of its condition of registration 1B since 1 July 2014. This breach situation was remedied in December 2015 when all exposures previously rated by the three unapproved capital models were migrated to models approved by the RBNZ; and
- observed an RBNZ operational risk capital floor, but failed to execute its operational risk capital model process as required under BS2B. While the calculated capital was at all times under the RBNZ floor, the failure to execute the model was a breach of Condition of Registration 1B.

Directors' Statement

The Directors of Bank of New Zealand (the "Bank") state that each Director of the Bank believes, after due enquiry, that:

1. as at the date on which the 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; and
2. during the year ended 30 September 2016:
   (a) the Bank has complied with its conditions of registration applicable during that period, except as disclosed on page 88 of this Disclosure Statement;
   (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 the Banking Group's material risks, 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 7th December 2016 and signed by Messrs. McKay and Healy as Directors and as responsible persons on behalf of all the other Directors.

D A McKay
Chairman

A J Healy
Managing Director and Chief Executive Officer