HEARTLAND NEW ZEALAND LIMITED

FINANCIAL STATEMENTS

For the year ended 30 June 2013

DIRECTORS' RESPONSIBILITY STATEMENT

The directors are responsible for ensuring that the financial statements give a true and fair view of the financial position of Heartland New Zealand Limited (Company) and its subsidiaries (Group) as at 30 June 2013 and the financial performance and cash flows for the year ended 30 June 2013.

The directors consider that the financial statements of the Group and the Company have been prepared using appropriate accounting policies consistently applied and supported by reasonable judgements and estimates and that all the relevant financial reporting and accounting standards have been followed.

The directors believe that proper accounting records have been kept which enable, with reasonable accuracy, the determination of the financial position of the Group and facilitate compliance of the financial statements with the Financial Reporting Act 1993.

The Board of Directors (Board) of Heartland New Zealand Limited authorised the financial statements set out on pages 3 to 43 for issue on 26 August 2013.

For and on behalf of the Board

Director

Director

STATEMENTS OF COMPREHENSIVE INCOME
For the year ended 30 June 2013

		GROUP		COMPANY	
	NOTE	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Interest income	6	206,349	205,148	36	17
Interest expense	6	110,895	121,502	-	-
Net interest income		**95,454**	**83,646**	**36**	**17**
Operating lease income	7	14,861	15,064	-	-
Operating lease expenses	7	9,687	9,954	-	-
Net operating lease income		**5,174**	**5,110**	**-**	**-**
Lending and credit fee income		1,760	1,392	-	-
Dividends received		-	-	15,605	1,597
Other income	8	4,499	4,736	170	-
Net operating income		**106,887**	**94,884**	**15,811**	**1,614**
Selling and administration expenses	9	70,347	65,547	1,284	1,365
Profit before impaired asset expense and income tax		**36,540**	**29,337**	**14,527**	**249**
Impaired asset expense	10	22,527	5,642	-	-
Decrease in fair value of investment properties	17	5,101	3,900	-	-
Operating profit		**8,912**	**19,795**	**14,527**	**249**
Share of equity accounted investee's profit	22	504	534	-	-
Profit before income tax		**9,416**	**20,329**	**14,527**	**249**
Income tax expense / (benefit)	11	2,504	(3,277)	(214)	(303)
Profit for the year		**6,912**	**23,606**	**14,741**	**552**
Other comprehensive income					
Items that are or may be reclassified subsequently to profit or loss:					
Effective portion of changes in fair value of cash flow hedges, net of income tax		1,056	378	-	-
Net change in available for sale reserve, net of income tax		276	(103)	-	-
Items that will not be reclassified to profit or loss:					
Net change in defined benefit reserve, net of income tax		462	(435)	-	-
Other comprehensive income / (loss) for the year, net of income tax		**1,794**	**(160)**	**-**	**-**
Total comprehensive income for the year		**8,706**	**23,446**	**14,741**	**552**
Earnings per share from continuing operations					
Basic earnings per share	13	2c	6c	n/a	n/a
Diluted earnings per share	13	2c	6c	n/a	n/a

All comprehensive income for the year is attributable to owners of the Group.

The notes on pages 8 to 43 are an integral part of these financial statements.

STATEMENTS OF CHANGES IN EQUITY

For the year ended 30 June 2013

		GROUP						
	NOTE	Share Capital $000	Employee Benefits Reserve $000	Available for sale Reserve $000	Defined benefit Reserve $000	Hedging Reserve $000	Retained Earnings $000	Total Equity $000
Balance at 1 July 2012		**192,020**	**-**	**8**	**(421)**	**(1,010)**	**184,201**	**374,798**
Total comprehensive income for the year								
Profit for the year		-	-	-	-	-	6,912	6,912
Other comprehensive income, net of income tax		-	-	276	462	1,056	-	1,794
Total comprehensive income for the year		**-**	**-**	**276**	**462**	**1,056**	**6,912**	**8,706**
Contributions by and distributions to owners								
Dividends paid	14	-	-	-	-	-	(13,591)	(13,591)
Staff share ownership expense for the year		-	629	-	-	-	-	629
Total transactions with owners		**-**	**629**	**-**	**-**	**-**	**(13,591)**	**(12,962)**
Balance at 30 June 2013		**192,020**	**629**	**284**	**41**	**46**	**177,522**	**370,542**
Balance at 1 July 2011		**137,074**	**-**	**111**	**14**	**(1,388)**	**160,595**	**296,406**
Total comprehensive income for the year								
Profit for the year		-	-	-	-	-	23,606	23,606
Other comprehensive income, net of income tax		-	-	(103)	(435)	378	-	(160)
Total comprehensive income for the year		**-**		**(103)**	**(435)**	**378**	**23,606**	**23,446**
Contributions by and distributions to owners								
Capital raising proceeds	28	57,347	-	-	-	-	-	57,347
Transaction costs associated with capital raising		(1,402)	-	-	-	-	-	(1,402)
Treasury shares acquired		(999)	-	-	-	-	-	(999)
Total transactions with owners		**54,946**	**-**	**-**	**-**	**-**	**-**	**54,946**
Balance at 30 June 2012		**192,020**	**-**	**8**	**(421)**	**(1,010)**	**184,201**	**374,798**

The notes on pages 8 to 43 are an integral part of these financial statements.

STATEMENTS OF CHANGES IN EQUITY

For the year ended 30 June 2013

		COMPANY						
	NOTE	Share Capital $000	Employee Benefits Reserve $000	Available for sale Reserve $000	Defined benefit Reserve $000	Hedging Reserve $000	Retained Earnings $000	Total Equity $000
Balance at 1 July 2012		**342,288**	-	**-**	**-**	**-**	**826**	**343,114**
Total comprehensive income for the year								
Profit for the year		-	-	-	-	-	14,741	14,741
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**-**	**14,741**	**14,741**
Contributions by and distributions to owners								
Dividends paid	14	-	-	-	-	-	(13,605)	(13,605)
Total transactions with owners		**-**		**-**	**-**	**-**	**(13,605)**	**(13,605)**
Balance at 30 June 2013		**342,288**	**-**	**-**	**-**	**-**	**1,962**	**344,250**
Balance at 1 July 2011		**286,343**	**-**	**-**	**-**	**-**	**274**	**286,617**
Total comprehensive income for the year								
Profit for the year		-	-	-	-	-	552	552
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**-**	**552**	**552**
Contributions by and distributions to owners								
Capital raising proceeds	28	57,347	-	-	-	-	-	57,347
Transaction costs associated with capital raising		(1,402)	-	-	-	-	-	(1,402)
Total transactions with owners		**55,945**	**-**	**-**	**-**	**-**	**-**	**55,945**
Balance at 30 June 2012		**342,288**	**-**	**-**	**-**	**-**	**826**	**343,114**

The notes on pages 8 to 43 are an integral part of these financial statements.

STATEMENTS OF FINANCIAL POSITION
As at 30 June 2013

		GROUP		COMPANY	
	NOTE	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Assets					
Cash and cash equivalents	15	174,262	89,689	1,485	469
Investments	16	165,223	24,327	-	-
Investment properties	17	58,287	55,504	-	-
Finance receivables	18	2,010,376	2,078,276	-	-
Operating lease vehicles	19	32,395	34,550	-	-
Current tax assets		-	5,635	707	363
Other assets	20	10,133	15,785	36	317
Investment in subsidiaries	21	-	-	342,234	342,343
Investment in joint venture	22	4,320	3,116	-	-
Intangible assets	23	22,963	22,997	-	-
Property, plant and equipment	24	10,281	10,067	-	-
Deferred tax assets	25	16,387	8,143	14	-
Total assets		**2,504,627**	**2,348,089**	**344,476**	**343,492**
Liabilities					
Borrowings	26	2,097,553	1,939,489	-	-
Current tax liabilities		2,859	-	-	-
Trade and other payables	27	33,673	33,802	226	378
Total liabilities		**2,134,085**	**1,973,291**	**226**	**378**
Equity					
Share capital	28	192,020	192,020	342,288	342,288
Retained earnings and reserves		178,522	182,778	1,962	826
Total equity		**370,542**	**374,798**	**344,250**	**343,114**
Total equity and liabilities		**2,504,627**	**2,348,089**	**344,476**	**343,492**

The notes on pages 8 to 43 are an integral part of these financial statements.

STATEMENTS OF CASH FLOWS
For the year ended 30 June 2013

	NOTE	GROUP Jun 13 $000	GROUP Jun 12 $000	COMPANY Jun 13 $000	COMPANY Jun 12 $000
Cash flows from operating activities					
Interest received		199,279	197,152	36	17
Dividends received		-	-	15,605	1,597
Operating lease income received		11,958	13,099	-	-
Proceeds from sale of operating lease vehicles		10,710	7,932	-	-
Lending, credit fees and other income received		6,259	6,219	155	-
Net decrease in finance receivables		32,908	-	-	-
Total cash provided from operating activities		**261,114**	**224,402**	**15,796**	**1,614**
Payments to suppliers and employees		61,009	68,183	1,140	1,243
Interest paid		112,820	121,742	-	-
Purchase of operating lease vehicles		15,611	16,905	-	-
Net increase in finance receivables		-	20,547	-	-
Taxation paid		2,946	23	144	-
Total cash applied to operating activities		**192,386**	**227,400**	**1,284**	**1,243**
Net cash flows from / (applied to) operating activities	31	**68,728**	**(2,998)**	**14,512**	**371**
Cash flows from investing activities					
Sale of investment property		3,194	832	-	-
Decrease in investment in subsidiaries		-	-	809	-
Total cash provided from investing activities		**3,194**	**832**	**809**	**-**
Purchase of office fit-out, equipment and intangible assets		2,256	3,191	-	-
Net increase in investments		130,687	6,496	-	-
Purchase of PGG Wrightson Finance Limited		-	24,898	-	-
Increase in investment in subsidiaries		-	-	700	56,000
Increase in investment in joint venture		700	-	-	-
Purchase of investment property		-	937	-	-
Total cash applied to investing activities		**133,643**	**35,522**	**700**	**56,000**
Net cash flows (applied to) / from investing activities		**(130,449)**	**(34,690)**	**109**	**(56,000)**
Cash flows from financing activities					
Net increase in borrowings		159,885	-	-	-
Increase in share capital		-	57,347	-	57,347
Total cash provided from financing activities		**159,885**	**57,347**	**-**	**57,347**
Dividends paid		13,591	-	13,605	-
Purchase of treasury shares		-	999	-	-
Transaction costs associated with capital raising		-	1,402	-	1,402
Net decrease in borrowings		-	256,399	-	-
Total cash applied to financing activities		**13,591**	**258,800**	**13,605**	**1,402**
Net cash flows from / (applied to) financing activities		**146,294**	**(201,453)**	**(13,605)**	**55,945**
Net increase / (decrease) in cash held		**84,573**	**(239,141)**	**1,016**	**316**
Opening cash and cash equivalents		89,689	267,187	469	153
Cash impact of business combinations		-	61,643	-	-
Closing cash and cash equivalents	15	**174,262**	**89,689**	**1,485**	**469**

The notes on pages 8 to 43 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 30 June 2013

1 Reporting entity

The financial statements presented are the consolidated financial statements comprising Heartland New Zealand Limited (Company) and its subsidiaries and joint venture (Group).

The Company, through a subsidiary, owns 100% of Heartland Bank Limited (Bank). The Bank was formerly known as Heartland Building Society. Heartland Building Society was established in January 2011, as a result of the merger of Canterbury Building Society (CBS) and Southern Cross Building Society (SCBS).

The Bank owns 100% of MARAC Finance Limited (MARAC) and PGG Wrightson Finance Limited (PWF). The Company owns 100% of Heartland Financial Services Limited (HFSL) which holds a 50% joint venture interest in MARAC JV Holdings Limited (MJV) with the New Zealand Automobile Association. Refer to Note 5 - Significant subsidiaries.

The Bank acquired PWF on 31 August 2011, as a result comparatives for the year ended 30 June 2012 only include the PWF result from the date of acquisition.

The Group includes Heartland ABCP Trust 1 and CBS Warehouse A Trust (collectively the Trusts), which are special purpose vehicles holding securitised loans purchased from MARAC and the Bank.

All entities within the Group offer financial services or are special purpose entities. The Group operates and is domiciled in New Zealand. The registered office address is 75 Riccarton Road, Christchurch.

2 Basis of preparation

(a) Statement of compliance

The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP) and with the requirements of the Financial Reporting Act 1993. 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 also comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

The Company and all entities within the Group are profit-oriented entities. The Company is a reporting entity and an issuer for the purposes of the Financial Reporting Act 1993 and its financial statements comply with that Act. The financial statements have been prepared in accordance with the requirements of the Companies Act 1993 and the Securities Regulations 2009.

(b) Basis of measurement

The financial statements have been prepared on the basis of historical cost, unless stated otherwise.

(c) Functional and presentation currency and rounding

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

(d) Estimates and judgements

The preparation of financial statements requires the use of management judgement, estimates and assumptions that effect reported amounts. Actual results may differ from these judgements. For further information about significant areas of estimation, uncertainty and critical judgements that have the most significant effect on the financial statements, refer to Note 36 - Credit risk exposure.

(e) Going concern

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

(f) Comparative information

Certain comparatives have been restated to comply with current year presentation.

3 Significant accounting policies

(a) Consolidation of subsidiaries

Subsidiaries are entities that are controlled by the Group. Investments in subsidiary companies are recorded at cost by the Company.

The consolidated financial statements are prepared by consolidating the financial statements of the Company and its subsidiaries. All intercompany transactions, balances and unrealised profits are eliminated on consolidation.

3 Significant accounting policies (continued)

(b) Jointly controlled entities

Joint ventures are those entities over whose activities the Group has joint control, established by contractual agreement and requiring unanimous consent for strategic financial and operating decisions.

Investments in jointly controlled entities are accounted for by the Group using the equity method and are recognised initially at cost. The consolidated financial statements include the Group's share of the income and expenses and equity movements of equity accounted investees, from the date that significant influence or joint control commences until the date that significant influence or joint control ceases. Dividends received from associates and jointly controlled entities are recorded in profit or loss.

(c) Special purpose entities

Special purpose entities are created to accomplish a narrow and well-defined objective such as the securitisation or holding of particular assets, or the execution of a specific borrowing or lending transaction. The financial statements of special purpose entities are included in the Group's financial statements where the substance of the relationship is that the Company controls the special purpose entity.

(d) Interest

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

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

(e) Operating lease income and expense

Income from operating lease vehicles is apportioned over the term of the operating lease on a straight line basis.

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

(f) Lending and credit fee income

Lending and credit fee income that is integral to the effective interest rate of a financial asset or liability is included in the measurement of the effective interest rate. Other lending and credit fee income is recognised as the related services are rendered.

(g) Dividend income

Dividend income is recognised in profit or loss on the date that the Company's right to receive payment is established.

(h) Tax

Income tax expense

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

Current tax

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

Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amount of assets and liabilities and the amounts used for tax purposes.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year(s) when the assets or liabilities giving rise to them are realised or settled, based on the tax rates (and tax laws) that have been enacted or substantively enacted by the reporting date. The measurement reflects the tax consequences that would follow from the manner in which the Group, at the reporting date, recovers or settles the carrying amount of its assets and liabilities.

3 Significant accounting policies (continued)

(h) Tax (continued)

Deferred tax (continued)

Deferred tax assets, including those related to the tax effects of income tax losses and credits available to be carried forward, are recognised only to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences or unused tax losses and credits can be utilised. Deferred tax assets are reviewed each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Current and deferred tax assets and liabilities are offset only to the extent that they relate to income taxes imposed by the same taxation authority and there is a legal right and intention to settle on a net basis and it is allowed under tax law.

(i) Share capital

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

The Group's share capital differs from the share capital of the Company as a result of the reverse acquisition accounting applied when the Company was formed. Under NZ IFRS MARAC (a subsidiary of the Company) was treated as the acquirer of the Company. As a result, the Group's result represents a continuation of the MARAC business, and the share capital of the Group reflects this.

(j) Cash and cash equivalents

Cash and cash equivalents consist of cash and liquid assets used in the day to day cash management of the Group. Cash and cash equivalents are carried at amortised cost in the Statements of Financial Position.

(k) Investments

The Group holds investments in local authority stock, public securities and corporate bonds. Investments held are classified as being available for sale and are stated at fair value less impairment, if any. The fair values are derived by reference to published price quotations in an active market or modelled using observable market inputs.

(l) Investment properties

Investment properties have been acquired through the enforcement of security over finance receivables and are held to earn rental income or for capital appreciation (or both). Investment property is initially recognised at its fair value, with subsequent changes in fair value recognised in profit or loss.

Fair values are supported by independent valuations or other similar external evidence, adjusted for changes in market conditions and the time since the last valuation.

(m) Finance receivables

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

(n) Operating lease vehicles

Operating lease vehicles are stated at cost less accumulated depreciation. Profits on the sale of operating lease vehicles are included as part of operating lease income. Current year depreciation and losses on the sale of operating lease vehicles are included as part of operating lease expenses.

(o) Derivative financial instruments

Derivative financial instruments are contracts entered into to reduce the exposure to the volatility of variable rate borrowings (cash flow hedges), or to convert fixed rate borrowings or assets to variable rates (fair value hedges), in order to mitigate the Group's interest rate risk. The financial instruments are subject to the risk that market values may change subsequent to their acquisition; however such changes would be offset by corresponding, but opposite, effects on the variable rate borrowings or fixed rate borrowings or assets being hedged. Derivatives are initially valued at fair value and subsequently remeasured at fair value.

Fair value movements of derivatives that are not designated in a qualifying cash flow hedge relationship, are recognised in profit or loss. Fair value movements of the effective portion of a qualifying cash flow hedge derivative, are recognised directly in other comprehensive income and held in the hedging reserve in equity. The amount recognised in equity is transferred to profit or loss in the same year as the hedged cash flow affects profit or loss, disclosed in the same line as the hedged item. Any ineffective portion of changes in fair value of the derivative is recognised immediately in profit or loss. Fair value movements of a derivative designated as a fair value hedge are recognised directly in profit or loss together with the hedged item.

3 Significant accounting policies (continued)

(p) Property, plant, equipment and depreciation

Land and buildings are measured at fair value. Fair value is determined on the basis of independent valuations prepared by external valuation experts, based on discounted cash flows or capitalisation of net income.

Any revaluation increase arising on the revaluation of land and buildings is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of land and buildings is charged as an expense to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset.

Depreciation on revalued buildings is charged to profit or loss. On the subsequent sale or retirement of a revalued property, the attributable revaluation surplus remaining in the asset revaluation reserve, net of any related deferred taxes, is transferred directly to retained earnings.

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

The following annual rates are used in the calculation of depreciation:

Buildings	1.0% - 4.0%
Fixtures and fittings	5.5% - 36.0%
Office equipment and furniture	6.0% - 30.0%
Computer equipment	16.2% - 48.0%
Motor vehicles	21.0% - 25.2%

(q) Intangible assets and goodwill

Goodwill

Goodwill arising on acquisition represents the excess of the cost of the acquisition over the Group's interest in the fair value of the identifiable net assets and contingent liabilities. When the fair value of the identifiable net assets and contingent liabilities exceeds the cost of an acquisition, the resulting discount is recognised immediately in profit or loss for the year. Goodwill is tested for impairment at least annually, and is carried at cost less accumulated impairment losses.

Computer software

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

(r) Financial assets and liabilities

Classification

Financial assets and liabilities are classified in the following accounting categories:

Financial assets/liabilities	Accounting category
Cash and cash equivalents	Loans and receivables
Investments	Available for sale
Due from related parties	Loans and receivables
Finance receivables	Loans and receivables
Other financial assets	Loans and receivables
Borrowings	Other liabilities at amortised cost
Other financial liabilities	Other liabilities at amortised cost
Derivatives	Held for trading (or qualifying hedges as described in Note 3(o))

Recognition

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

3 Significant accounting policies (continued)

(r) Financial assets and liabilities (continued)

Derecognition

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

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

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

(s) Impaired assets and past due assets

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

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

Restructured assets are impaired assets where the Group expects to recover all amounts owing although the original terms have been changed due to the counterparty's difficulty in complying with the original terms of the contract and the amended terms are not comparable with similar new lending.

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

(t) Provision for impairment

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

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

Collective provisioning

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

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

3 Significant accounting policies (continued)

(t) Provision for impairment (continued)

Individual provisioning

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

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

Individual provisioning in regards to property development lending carries the greatest amount of risk of a material adjustment to the carrying amounts of the Group's assets within the next year. Estimating the timing and amount of future cash repayments and proceeds from the realisation of collateral are management's most difficult and subjective judgements. Subjective judgements made by management comprise the time taken for new sales being achieved and the amount received, determining the timing and amount of future cash flows.

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

(u) Goods and services tax (GST)

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

(v) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

(w) Employee benefits

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

(x) Defined benefit plan

The cost of providing benefits for defined benefit superannuation plans is determined using the Projected Unit Credit Method. Actuarial gains and losses are recognised in full in the year in which they occur by way of a movement in the defined benefit plan reserve, and are recognised in other comprehensive income and presented in the Statements of Changes in Equity.

Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average year until the benefit becomes vested. The defined benefit obligation is deducted from the fair value of the defined benefit plan asset to derive the defined benefit plan surplus recognised in trade receivables in the Statements of Financial Position.

(y) Share schemes

The Group operates share-based compensation plans that are cash settled and equity settled.

For the cash settled plan, the Group recognises a liability based on the estimated fair value of the obligation. The value of this liability is recognised in the Statement of Comprehensive Income over the relevant service period and is re-measured at each reporting date.

For the equity-settled plan, share based payments to employees providing services are measured at the fair value of the equity instruments at the grant date. Details regarding the determination of the fair value of equity-settled share-based transactions are set out in Note 33 - Staff share ownership arrangements.

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

3 Significant accounting policies (continued)

(z) Borrowings

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

(aa) Statements of Cash Flows

The Statements of Cash Flows have been prepared using the direct method modified by the netting of certain cash flows associated with cash and cash equivalents, investments, related party balances, finance receivables and borrowings. Netting of cash flows provides more meaningful disclosure as many of the cash flows are received and paid on behalf of customers and reflect the activities of those customers rather than the Group.

(ab) Changes in accounting policies

There have been no material changes in accounting policies in the current year.

(ac) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 30 June 2013, and have not been applied in preparing these financial statements. The new standards identified which may have an effect on the financial statements of the Group are:

Standard and description	*Effective for annual years beginning on or after:*	*Expected to be initially applied in year ending:*
NZ IFRS 10 Consolidated Financial Statements, which introduces a new approach to determining which investees should be consolidated and provides a single model to be applied in the control analysis for all investees.	1 January 2013	30 June 2014
NZ IFRS 11 Joint Arrangements, which outlines the accounting by entities that jointly control an arrangement.	1 January 2013	30 June 2014
NZ IFRS 13 Fair Value Measurement, which defines fair value, and establishes a framework for measuring fair value including disclosure requirements.	1 January 2013	30 June 2014
NZ IFRS 12 Disclosure of Interests in Other Entities, which contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities.	1 January 2013	30 June 2014
NZ IFRS 9 Financial Instruments, which specifies how an entity should classify and measure financial assets and liabilities.	1 January 2013	30 June 2014
NZ IAS 27 Separate Financial Statements, which carries forward existing accounting and disclosure requirements for separate financial statements with minor clarifications.	1 January 2013	30 June 2014
NZ IFRS 7 Financial Instruments: Disclosures, amendment to offsetting financial assets and financial liabilities.	1 January 2013	30 June 2014
NZ IAS 28 Investments in Associates and Joint Ventures, which amends IFRS 5 to apply to an investment, or a portion of investment in an associate or joint venture that meets the criteria to be classified as held for sale and on cessation of significant influence or joint control, the entity does not remeasure the retained interest.	1 January 2013	30 June 2014
NZ IAS 32 Financial Instruments: Presentation, amendment to offsetting financial assets and financial liabilities.	1 January 2014	30 June 2015
NZ IAS 19 Employee Benefits, which requires actuarial gains and losses to be recognised immediately in other comprehensive income and the expected return on plan assets recognised in profit or loss to be calculated based on the rate used to discount the defined benefit obligation.	1 January 2013	30 June 2014

Initial application of the above standards and interpretations relevant to the Group are not expected to have any material impact on the financial statements of the Group.

4 Segmental analysis

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

All income received is from external sources, except those transactions with related parties, refer to Note 30 - Related party transactions. Certain selling and administration expenses, such as premises, IT and support centre costs are not allocated to operating segments and are included in Other.

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

Retail and Consumer	Providing a comprehensive range of financial services to New Zealand businesses and families, including term, transactional and savings based deposit accounts together with residential mortgage lending, motor vehicle finance and asset finance.
Business	Providing term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium sized New Zealand businesses.
Rural	Providing specialist financial services to the farming sector primarily offering livestock finance, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers.
Non-core Property	Funding assets of the non-core property division.

The Group's operating segments are different than the industry categories detailed in Note 37 - Asset quality. The operating segments are primarily categorised by sales channel, whereas Note 37 - Asset quality categorises exposures based on credit risk concentrations (see Note 37 - Asset quality exposure for further details).

	GROUP					
	Retail & Consumer $000	Business $000	Rural $000	Non-core Property $000	Other $000	Total $000
Jun 13						
Interest income	90,991	51,679	45,762	8,734	9,183	206,349
Interest expense	46,611	26,261	22,952	7,767	7,304	110,895
Net interest income	**44,380**	**25,418**	**22,810**	**967**	**1,879**	**95,454**
Net operating lease income	5,151	23	-	-	-	5,174
Net other income	622	285	49	3,860	1,443	6,259
Net operating income	**50,153**	**25,726**	**22,859**	**4,827**	**3,322**	**106,887**
Depreciation and amortisation expense	-	-	-	-	1,940	1,940
Other selling and administration expenses	11,696	5,864	6,152	12,438	32,257	68,407
Selling and administration expenses	**11,696**	**5,864**	**6,152**	**12,438**	**34,197**	**70,347**
Profit before impaired asset expense and income tax	**38,457**	**19,862**	**16,707**	**(7,611)**	**(30,875)**	**36,540**
Impaired asset expense	2,770	3,360	(195)	16,592	-	22,527
Decrease in fair value of investment properties	-	-	-	5,101	-	5,101
Operating profit / (loss)	**35,687**	**16,502**	**16,902**	**(29,304)**	**(30,875)**	**8,912**
Share of equity accounted investee's profit	-	-	-	-	504	504
Profit / (loss) before income tax	**35,687**	**16,502**	**16,902**	**(29,304)**	**(30,371)**	**9,416**
Income tax expense	-	-	-	-	2,504	2,504
Profit / (loss) for the year	**35,687**	**16,502**	**16,902**	**(29,304)**	**(32,875)**	**6,912**
Total assets	987,796	549,177	456,647	107,438	403,569	**2,504,627**
Total liabilities	-	-	-	-	2,134,085	**2,134,085**
Total equity	-	-	-	-	370,542	**370,542**

4 Segmental analysis (continued)

	GROUP					
	Retail & Consumer $000	Business $000	Rural $000	Non-core Property $000	Other $000	Total $000
Jun 12						
Interest income	94,606	49,867	41,391	12,630	6,654	205,148
Interest expense	55,572	28,911	22,340	10,370	4,309	121,502
Net interest income	**39,034**	**20,956**	**19,051**	**2,260**	**2,345**	**83,646**
Net operating lease income	5,097	13	-	-	-	5,110
Net other income	927	57	66	4,104	974	6,128
Net operating income	**45,058**	**21,026**	**19,117**	**6,364**	**3,319**	**94,884**
Depreciation and amortisation expense	-	-	-	-	1,830	1,830
Other selling and administration expenses	11,475	5,273	5,837	6,350	34,782	63,717
Selling and administration expenses	**11,475**	**5,273**	**5,837**	**6,350**	**36,612**	**65,547**
Profit / (loss) before impaired asset expense and income tax	**33,583**	**15,753**	**13,280**	**14**	**(33,293)**	**29,337**
Impaired asset expense	1,991	2,445	689	517	-	5,642
Decrease in fair value of investment properties	-	-	-	3,900	-	3,900
Operating profit / (loss)	**31,592**	**13,308**	**12,591**	**(4,403)**	**(33,293)**	**19,795**
Share of equity accounted investee's profit	-	-	-	-	534	534
Profit / (loss) before income tax	**31,592**	**13,308**	**12,591**	**(4,403)**	**(32,759)**	**20,329**
Income tax expense	-	-	-	-	(3,277)	(3,277)
Profit/(loss) for the year	**31,592**	**13,308**	**12,591**	**(4,403)**	**(29,482)**	**23,606**
Total assets	989,352	540,228	478,582	160,168	179,759	**2,348,089**
Total liabilities	-	-	-	-	1,973,291	**1,973,291**
Total equity	-	-	-	-	374,798	**374,798**

5 Significant subsidiaries and interests in jointly controlled entities

Significant subsidiaries	Nature of business	Jun 13 % held	Jun 12 % held
Heartland Bank Limited	Financial services	100%	100%
and its subsidiaries:			
MARAC Finance Limited	Financial services	100%	100%
PGG Wrightson Finance Limited	Financial services	100%	100%
VPS Parnell Limited	Investment property holding company	100%	100%
VPS Properties Limited	Investment property holding company	100%	100%
Heartland NZ Trustee Limited	Holding company	100%	100%
Heartland Financial Services Limited	Holding company	100%	100%
and its jointly controlled entity:			
MARAC JV Holdings Limited	Holding company	50%	50%
and its subsidiary:			
MARAC Insurance Limited	Insurance services	50%	50%

The Group includes Heartland ABCP Trust 1, CBS Warehouse A Trust and Heartland Cash and Term PIE Fund, refer to Note 32 - Special Purpose entities for more details.

6 Net interest income

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Interest income				
Cash and cash equivalents	5,736	5,149	36	17
Finance receivables	197,999	199,526	-	-
Derivatives held for risk management:				
- Net interest income on cash flow hedges	2,614	473	-	-
Total interest income	**206,349**	**205,148**	**36**	**17**
Interest expense				
Retail deposits	94,198	100,769	-	-
Bank and securitised borrowings	16,697	20,733	-	-
Total interest expense	**110,895**	**121,502**	**-**	**-**
Net interest income	**95,454**	**83,646**	**36**	**17**

Included within the Group's interest income on finance receivables is $2,591,000 (2012: $2,674,000) on individually impaired assets.

7 Net operating lease income

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Operating lease income				
Lease income	12,898	13,065	-	-
Gain on disposal of lease vehicles	1,963	1,999	-	-
Total operating lease income	**14,861**	**15,064**	**-**	**-**
Operating lease expense				
Depreciation on lease vehicles	9,019	9,149	-	-
Direct lease costs	668	805	-	-
Total operating lease expenses	**9,687**	**9,954**	**-**	**-**
Net operating lease income	**5,174**	**5,110**	**-**	**-**

8 Other income

		GROUP		COMPANY	
	NOTE	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Rental income from investment properties		3,859	4,094	-	-
Management fees	30	335	328	-	-
Other income		305	314	170	-
Total other income		**4,499**	**4,736**	**170**	**-**

9 Selling and administration expenses

		GROUP		COMPANY	
		Jun 13	Jun 12	Jun 13	Jun 12
	NOTE	$000	$000	$000	$000
Personnel expenses		33,448	34,186	-	-
Directors' fees		726	804	549	628
Superannuation		413	475	-	-
Audit fees		419	576	60	60
Audit related fees		104	35	-	-
Amortisation - intangible assets	23	1,226	1,075	-	-
Depreciation - property, plant and equipment	24	714	755	-	-
Operating lease expense as a lessee		1,651	1,648	-	-
RECL Agreement fees	36(e)	7,700	2,200	-	-
Legal and professional fees		3,631	3,714	246	499
Other operating expenses		20,315	20,079	429	178
Total selling and administration expenses		**70,347**	**65,547**	**1,284**	**1,365**

Audit related fees include professional fees in connection with trustee reporting, due diligence, review of prospectus documentation for various Group entities, accounting advice and review work completed.

During the year ended 30 June 2013, the Group recognised direct operating expenses of $3,563,000 (2012: $2,975,000) arising from investment property that generated rental income and direct operating expenses of $219,000 (2012: $107,000) arising from investment property that did not generate rental income.

Included in Directors' fees are Directors' fees the Company has paid on behalf of the Bank and its subsidiaries.

10 Impaired asset expense

		GROUP		COMPANY	
		Jun 13	Jun 12	Jun 13	Jun 12
	NOTE	$000	$000	$000	$000
Non-securitised					
Individually impaired expense		13,098	6,920	-	-
Collectively impaired expense / (recovery)		9,108	(1,897)	-	-
Total non-securitised impaired asset expense		**22,206**	**5,023**	**-**	**-**
Securitised					
Individually impaired expense		3	1	-	-
Collectively impaired expense		318	618	-	-
Total securitised impaired asset expense		**321**	**619**	**-**	**-**
Total					
Individually impaired expense	37(e)	13,101	6,921	-	-
Collectively impaired expense / (recovery)	37(e)	9,426	(1,279)	-	-
Total impaired asset expense		**22,527**	**5,642**	**-**	**-**

The Group has changed its workout strategy with respect to non-core legacy property assets. This change has affected the periods over which assets are expected to be realised and the values expected to be realised for those assets. As a result of this change an additional provision of $12.9 million has been raised against finance receivables in the year ended 30 June 2013.

11 Income tax expense

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
(a) Current income tax expense / (benefit)				
Current year	11,699	4,639	(300)	(303)
Adjustments for prior year	(193)	(3,218)	63	-
Deferred tax (benefit) / expense				
Origination and reversal of temporary differences	(9,002)	1,484	23	-
Tax legislation changes	-	(6,182)	-	-
Total income tax expense / (benefit)	**2,504**	**(3,277)**	**(214)**	**(303)**
Reconciliation of effective tax rate				
Profit before income tax	9,416	20,329	14,527	249
Prima facie tax at 28%	2,636	5,692	4,068	70
Plus / (less) tax effect of items not taxable / deductible	61	431	24	74
Adjustments for prior year	(193)	(3,218)	63	-
Dividends received	-	-	(4,369)	(447)
Tax legislation changes	-	(6,182)	-	-
Total income tax expense / (benefit)	**2,504**	**(3,277)**	**(214)**	**(303)**

On 29 August 2011, the Taxation (Tax Administration and Remedial Matters) Act 2011 received Royal Assent. This Act contains a retrospective legislative change in relation to mergers of building societies. The result was that $6.2 million benefit of future tax deductions which were lost on the merger of MARAC, SCBS and CBS were made available to entities in the Heartland New Zealand Consolidated (Tax) Group, and cash that would otherwise have been required to pay tax became available to the Group.

During the year ended 30 June 2012 MARAC made a subvention payment to MARAC Financial Services Limited (its former parent) for the use of tax losses to 31 May 2011. The amount paid was less than the tax rate of 30%. As a result the Group recognised a benefit of $3.4 million included in adjustments for prior year.

(b) Tax recognised in other comprehensive income

	GROUP			
	Cash flow hedges $000	Available for sale investments $000	Defined benefit plan $000	Total $000
Jun 2013				
Other comprehensive income before tax	1,467	383	478	2,328
less tax expense	411	107	16	534
Total other comprehensive income, net of income tax	**1,056**	**276**	**462**	**1,794**
Jun 2012				
Other comprehensive income before tax	476	(147)	(463)	(134)
less tax expense / (benefit)	98	(44)	(28)	26
Total other comprehensive income, net of income tax	**378**	**(103)**	**(435)**	**(160)**

12 Imputation credit account

As at 30 June 2013, the imputation credit account of the Group was a credit of $1,688,000 (2012: credit of $23,000).

13 Earnings per share

The calculation of basic and diluted earnings of 2c per share at 30 June 2013 (2012: 6c per share) is based on the profit for the year of $6,912,000 (2012: $23,606,000), and a weighted average number of shares on issue of 388,703,975 (2012: 373,879,475).

14 Dividends paid

The Company paid dividends of $5,830,560 on 21 December 2012 and $7,774,079 on 5 April 2013 (2012: nil).

15 Cash and cash equivalents

	GROUP		COMPANY	
	Jun 13 $000	**Jun 12 $000**	**Jun 13 $000**	**Jun 12 $000**
Cash and cash equivalents - not securitised	162,676	74,110	1,485	469
Cash and cash equivalents - securitised	11,586	15,579	-	-
Total cash and cash equivalents	**174,262**	**89,689**	**1,485**	**469**

Cash and cash equivalents are short term funds held with New Zealand registered international banks.

16 Investments

	GROUP		COMPANY	
	Jun 13 $000	**Jun 12 $000**	**Jun 13 $000**	**Jun 12 $000**
Bank deposits	121,780	24,327	-	-
Public securities and corporate bonds	9,162	-	-	-
Local authority stock	34,281	-	-	-
Total investments	**165,223**	**24,327**	**-**	**-**

17 Investment properties

	GROUP		COMPANY	
	Jun 13 $000	**Jun 12 $000**	**Jun 13 $000**	**Jun 12 $000**
Opening balance	55,504	34,499	-	-
Acquisitions	10,800	23,584	-	-
Additional capital expenditure	278	2,153	-	-
Sales	(3,194)	(832)	-	-
Decrease in fair value	(5,101)	(3,900)	-	-
Closing balance	**58,287**	**55,504**	**-**	**-**

Following the unwind of the RECL Agreement (refer to Note 36(e) - Credit risk exposure for more details), the Group has acquired net investment properties during the year ended 30 June 2013 of $11 million.

As a result of the change in the Group's workout strategy with respect to non-core legacy property assets (see Note 10 - Impaired asset expense) a $5.1 million reduction in the fair value of investment properties has been recognised reflecting the Directors' view on the current market value of this portfolio.

18 Finance receivables

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Non-securitised				
Neither at least 90 days past due or impaired	1,687,480	1,711,802	-	-
At least 90 days past due	24,837	50,508	-	-
Individually impaired	69,301	56,805	-	-
Restructured assets	3,566	9,086	-	-
Gross finance receivables	**1,785,184**	**1,828,201**	**-**	**-**
Less allowance for impairment	49,786	26,693	-	-
Total non-securitised finance receivables	**1,735,398**	**1,801,508**	**-**	**-**
Securitised				
Neither at least 90 days past due or impaired	273,922	275,985	-	-
At least 90 days past due	1,761	1,496	-	-
Individually impaired	-	20	-	-
Restructured assets	-	-	-	-
Gross finance receivables	**275,683**	**277,501**	**-**	**-**
Less allowance for impairment	705	733	-	-
Total securitised finance receivables	**274,978**	**276,768**	**-**	**-**
Total				
Neither at least 90 days past due or impaired	1,961,402	1,987,787	-	-
At least 90 days past due	26,598	52,004	-	-
Individually impaired	69,301	56,825	-	-
Restructured assets	3,566	9,086	-	-
Gross finance receivables	**2,060,867**	**2,105,702**	**-**	**-**
Less allowance for impairment	50,491	27,426	-	-
Total finance receivables	**2,010,376**	**2,078,276**	**-**	**-**

Refer to Note 37 - Asset quality for further analysis of finance receivables by credit risk concentration.

19 Operating lease vehicles

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Cost				
Opening balance	51,236	47,230	-	-
Additions	15,611	16,905	-	-
Disposals	(19,508)	(12,899)	-	-
Closing balance	**47,339**	**51,236**	**-**	**-**
Accumulated depreciation				
Opening balance	16,686	14,503	-	-
Depreciation charge for the year	9,019	9,149	-	-
Disposals	(10,761)	(6,966)	-	-
Closing balance	**14,944**	**16,686**	**-**	**-**
Opening net book value	34,550	32,727	-	-
Closing net book value	**32,395**	**34,550**	**-**	**-**

The future minimum lease payments receivable under non-cancellable operating leases not later than one year is $9,412,000 (2012: $11,123,000), within one to five years is $8,390,000 (2012: $7,635,000) and over five years is nil (2012: $7,000).

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 30 June 2013

20 Other assets

		GROUP		COMPANY	
		Jun 13	Jun 12	Jun 13	Jun 12
	NOTE	$000	$000	$000	$000
Derivative financial assets	29	649	2,122	-	-
Trade receivables		7,286	3,080	16	14
Due from related parties	30	-	-	20	194
Prepayments		2,198	10,583	-	109
Total other assets		**10,133**	**15,785**	**36**	**317**

21 Investment in subsidiaries

	GROUP		COMPANY	
	Jun 13	Jun 12	Jun 13	Jun 12
	$000	$000	$000	$000
Heartland Bank Limited	-	-	338,843	338,843
Heartland Financial Services Limited	-	-	3,200	2,500
Heartland NZ Trustee Limited	-	-	191	1,000
Total investments in subsidiaries	**-**	**-**	**342,234**	**342,343**

All subsidiary companies were incorporated in New Zealand.

22 Investment in joint venture

	GROUP		COMPANY	
	Jun 13	Jun 12	Jun 13	Jun 12
	$000	$000	$000	$000
Carrying amount at beginning of year	3,116	2,582	-	-
Investment in joint venture	700	-	-	-
Equity accounted earnings of joint venture	504	534	-	-
Carrying amount at end of year	**4,320**	**3,116**	**-**	**-**
Total assets of joint venture	9,610	6,927	-	-
Total liabilities of joint venture	3,726	3,453	-	-
Total income of joint venture	3,309	2,842	-	-
Total net profit after tax of joint venture	1,010	769	-	-

Heartland Financial Services Limited (HFSL), a wholly owned subsidiary of the Company, owns 50% of MJV. MJV is jointly owned by HFSL and the New Zealand Automobile Association Limited.

23 Intangible assets

	GROUP		COMPANY	
	Jun 13	Jun 12	Jun 13	Jun 12
	$000	$000	$000	$000
Computer software - cost				
Opening balance	6,748	6,142	-	-
Additions	1,320	2,370	-	-
Disposals	(335)	(1,764)	-	-
Closing balance	**7,733**	**6,748**	**-**	**-**
Computer software - accumulated amortisation				
Opening balance	4,038	4,727	-	-
Amortisation charge for the year	1,226	1,075	-	-
Disposals	(335)	(1,764)	-	-
Closing balance	**4,929**	**4,038**	**-**	**-**
Computer software - opening net book value	2,710	1,415	-	-
Computer software - closing net book value	**2,804**	**2,710**	**-**	**-**
Goodwill				
Opening balance	20,287	20,187	-	-
Additions	-	100	-	-
Disposals	(128)	-	-	-
Closing balance	**20,159**	**20,287**	**-**	**-**
Total intangible assets - opening net book value	22,997	21,602	-	-
Total intangible assets - closing net book value	**22,963**	**22,997**	**-**	**-**

On 5 January 2011, 100% of each of SCBS and CBS amalgamated to form the Bank. As part of this amalgamation $20.1 million of goodwill was recognised.

Goodwill has not been allocated to individual cash generating units, as the future economic benefit is attributable to all business units. The Group's management and Board of Directors continue to monitor goodwill at a group level.

24 Property, plant and equipment

	GROUP		COMPANY	
	Jun 13	Jun 12	Jun 13	Jun 12
	$000	$000	$000	$000
Cost				
Opening balance	13,161	15,191	-	-
Additions	936	735	-	-
Acquired on acquisition	-	22	-	-
Disposals	(91)	(2,787)	-	-
Closing balance	**14,006**	**13,161**	**-**	**-**
Accumulated depreciation				
Opening balance	3,094	5,112	-	-
Depreciation charge for the year	714	755	-	-
Disposals	(83)	(2,773)	-	-
Closing balance	**3,725**	**3,094**	**-**	**-**
Opening net book value	10,067	10,079	-	-
Closing net book value	**10,281**	**10,067**	**-**	**-**

25 Deferred tax

	GROUP		COMPANY	
	Jun 13	Jun 12	Jun 13	Jun 12
	$000	$000	$000	$000
Employee entitlements	1,232	1,201	-	-
Provision for impairment	13,939	7,475	-	-
Trade and other payables	225	152	14	-
Investment properties	2,925	1,054	-	-
Intangible assets	27	-	-	-
Derivatives held for risk management	-	392	-	-
Tax assets	**18,348**	**10,274**	**14**	**-**
Property, plant and equipment	834	877	-	-
Intangible assets	-	52	-	-
Derivatives held for risk management	18	-	-	-
Operating lease vehicles	1,109	1,202	-	-
Tax liabilities	**1,961**	**2,131**	**-**	**-**
Net tax assets	**16,387**	**8,143**	**14**	**-**

All deferred tax movements are included in profit or loss except for those in respect of the available for sale and hedging reserves which are recognised in other comprehensive income.

26 Borrowings

	GROUP		COMPANY	
	Jun 13	Jun 12	Jun 13	Jun 12
	$000	$000	$000	$000
Deposits	1,838,619	1,625,120	-	-
Bank borrowings	-	50,010	-	-
Securitised borrowings	258,934	264,359	-	-
Total borrowings	**2,097,553**	**1,939,489**	**-**	**-**

Bank borrowings and deposits (which include NZDX bonds) rank equally and are unsecured. The Group has securitised bank facilities totalling $500 million, all in relation to the Trusts. Heartland ABCP Trust 1 (ABCP Trust) has a securitisation facility of $400 million maturing 5 February 2014 and CBS Warehouse A Trust (CBS Trust) has a securitisation facility of $100 million maturing 22 January 2014. The facilities are drawn by $259 million (2012: $264 million) as shown above.

Investors in ABCP Trust rank equally with each other and are secured over the securitised assets of that trust. Investors in CBS Trust rank equally with each other and are secured over the securitised assets of that trust.

27 Trade and other payables

		GROUP		COMPANY	
		Jun 13	Jun 12	Jun 13	Jun 12
	NOTE	$000	$000	$000	$000
Derivative financial liabilities	29	30	1,459	-	-
Trade payables		12,360	13,734	226	300
GST payable		16,249	14,014	-	-
Due to related parties	30	500	-	-	78
Employee benefits		4,534	4,595	-	-
Total trade and other payables		**33,673**	**33,802**	**226**	**378**

28 Share capital

	COMPANY	
	Jun 13	Jun 12
	Number of shares	
	000	000
Issued shares		
Opening balance	388,704	300,000
Shares issued during the year	-	88,704
Closing balance	**388,704**	**388,704**

The share capital above represents the share capital of the Company. This differs from the share capital reflected in the Group's Statement of Financial Position as a result of the reverse acquisition accounting. Refer to Note 3(i) for more details.

On 31 August 2011, the Company issued 23,257,528 new shares at $0.52 per share to existing shareholders under a share purchase plan, issued 34,164,396 new shares at $0.65 per share to underwriters of the share purchase plan, placed 4,615,385 new shares at $0.65 per share and placed 26,666,666 new shares at $0.75 per share to institutions and investors. The total new capital raised was $57,346,857.

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

29 Derivative financial instruments

		GROUP		COMPANY	
		Jun 13	Jun 12	Jun 13	Jun 12
	NOTE	$000	$000	$000	$000
Qualifying cash flow hedges -securitised		567	-	-	-
Qualifying fair value hedges - non-securitised		82	2,122	-	-
Total derivative financial assets	20	**649**	**2,122**	**-**	**-**
Qualifying cash flow hedges - non-securitised		-	297	-	-
Qualifying fair value hedges - securitised		-	118	-	-
Qualifying cash flow hedges - securitised		30	1,044	-	-
Total derivative financial liabilities	27	**30**	**1,459**	**-**	**-**

Derivatives consist of interest rate swaps held to manage the Group's exposure to interest rate repricing risk on its interest bearing assets and liabilities.

The Group uses interest rate swaps to hedge the interest rate risk arising from its commercial paper issuance and its current and future floating rate bank debt and designates those swaps as qualifying cash flow hedges. The Group uses interest rate swaps to hedge the interest rate risk arising from deposits and fixed rate mortgage loans and designates these swaps as qualifying fair value hedges.

Securitised derivatives are held in the name of the Trusts to hedge the interest rate risk arising in the Trusts.

30 Related party transactions

The Company holds all shares in the Bank, HFSL, MARAC and PWF, refer Note 5 - Significant subsidiaries and interests in jointly controlled entities.

(a) Transactions with related parties

MARAC provided administrative assistance to MARAC Insurance Limited and received insurance commission from MARAC Insurance Limited.

MARAC Insurance Limited and some key management personnel invested in the Bank's deposits. The investments of Heartland Cash and Term PIE Fund are detailed in Note 32 - Special purpose entities. Key management personnel investments are detailed in Note 30(b).

	GROUP		COMPANY	
	Jun 13 $000	**Jun 12 $000**	**Jun 13 $000**	**Jun 12 $000**
Transactions with related parties				
Dividend income from subsidiaries	-	-	15,605	1,597
Lending and credit fee income	312	368	-	-
Other income	335	328	-	-
Total transactions with other related parties	**647**	**696**	**15,605**	**1,597**
Due from related parties				
Subsidiaries	-	-	20	194
Total due from related parties	**-**	**-**	**20**	**194**
Due to related parties				
Subsidiaries	-	-	-	78
MARAC Insurance Limited	500	-	-	-
Total due to related parties	**500**	**-**	**-**	**78**

(b) Transactions with key management personnel

Key management personnel, being directors of the Company and those staff reporting directly to the Chief Executive Officer and their immediate relatives, have transacted with the Group during the year as follows:

	GROUP		COMPANY	
	Jun 13 $000	**Jun 12 $000**	**Jun 13 $000**	**Jun 12 $000**
Deposit investments by key management personnel:				
Closing balance	825	468	-	-
Loans to key management personnel:				
Closing balance	-	304	-	-
Key management personnel interest expense and compensation is as follows:				
Interest expense	28	21	-	-
Short-term employee benefits	5,933	5,118	549	628
Share-based payments	718	459	-	-
Total	**6,679**	**5,598**	**549**	**628**

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

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Profit for the year	**6,912**	**23,606**	**14,741**	**552**
Add / (less) non-cash items:				
Depreciation and amortisation expense	1,940	1,830	-	-
Change in fair value of investment properties	5,101	3,900	-	-
Impaired asset expense	22,527	5,642	-	-
Deferred tax benefit	(8,244)	(2,978)	(14)	-
Derivative financial instruments revaluation	1,100	(219)	-	-
Accruals	(836)	529	-	-
Total non-cash items	**21,588**	**8,704**	**(14)**	**-**
Add / (less) movements in working capital items:				
Other assets	6,022	2,239	267	(271)
Current tax	8,494	(6,785)	(344)	(109)
Other liabilities	(2,337)	154	(138)	199
Total movements in working capital items	**12,179**	**(4,392)**	**(215)**	**(181)**
Net cash flows from operating activities before movements in finance receivables and operating lease vehicles	**40,679**	**27,918**	**14,512**	**371**
Movement in operating lease vehicles	2,155	(1,823)	-	-
Movement in finance receivables	25,894	(29,093)	-	-
Net cash flows from operating activities	**68,728**	**(2,998)**	**14,512**	**371**

32 Special purpose entities

Heartland Cash and Term PIE Fund (PIE Fund)

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

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Deposits	33,226	12,347	-	-

Heartland ABCP Trust 1 and CBS Warehouse A Trust

The Group has securitised a pool of receivables comprising residential, commercial, and motor vehicle loans to the Trusts. The Group substantially retains the credit risks and rewards associated with the securitised assets, and continues to recognise these assets and associated borrowings on the Statements of Financial Position. Despite this presentation in the financial statements, the loans sold to the Trusts are set aside for the benefit of investors in the Trusts and are represented as follows:

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Cash and cash equivalents - securitised	11,586	15,579	-	-
Finance receivables - securitised	274,978	276,768	-	-
Borrowings - securitised	(258,934)	(264,359)	-	-
Derivative financial asset - securitised	567	-	-	-
Derivative financial liabilities - securitised	(30)	(1,162)	-	-

33 Staff share ownership arrangements

Heartland Long Term Executive Share Plan

The Heartland Long Term Executive Share Plan (the LTESP) was introduced in the year ended 30 June 2013 for selected executives and senior employees of the Bank. Under the LTESP, the Banking Group lent funds to the participants. These funds were used by the participants to acquire shares of HNZ. The HNZ shares acquired by participants are held on their behalf by Heartland NZ Trustee Limited, an HNZ subsidiary. If a participant is still employed by the Banking Group on 30 June 2014, that participant may be entitled to some or all of the HNZ shares held on their behalf. The number of HNZ shares to which a participant will be entitled is determined by performance hurdles relating to the period which commenced 1 July 2011 (which include corporate values targets and financial performance targets). To the extent a participant is entitled to HNZ shares held on their behalf, the participant is given a cash bonus which is applied toward repayment of the loan. To the extent a participant is not entitled to HNZ shares held on their behalf, those shares are acquired by Heartland NZ Trustee Limited for a purchase price which is applied toward repayment of the loan. The weighted average grant date fair value of the shares issued under the LTESP was $0.60 (based on the volume weighted average price of the shares for the 20 business days immediately preceding the grant date).

Information regarding the shares under the LTESP is as follows:

	GROUP		COMPANY	
	Jun 13 Shares 000	Jun 12 Shares 000	Jun 13 Shares 000	Jun 12 Shares 000
Opening unvested shares	-	-	-	-
Number of shares granted	1,607	-	-	-
Less: forfeited over life of scheme	(35)	-	-	-
Less: vested over life of scheme	-	-	-	-
Closing unvested shares	**1,572**	**-**	**-**	**-**

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Total amount recognised as an expense	459	480	-	-

Heartland LTI Cash Entitlements Plan

The Heartland LTI Cash Entitlements Plan (LTICEP) was introduced for selected executives of the Bank. Under the LTICEP, participants are granted a cash entitlement. This cash entitlement is based on the amount by which the market price of HNZ shares at a future date exceeds an agreed reference price (no payment is made in the event that the market price of HNZ shares at that future date is lower than the reference price). Cash entitlements based on a reference pool of 5.65 million shares were issued in the year ending 30 June 2013 at a reference price of $0.72 per share.

Any cash entitlements are payable on the earlier of 20 business days after the release of the HNZ's financial results for the year ended 30 June 2015, or 2 November 2015. The market price of HNZ shares at this date will be based on the volume weighted average price for the 20 business days prior to this date.

Compensation expense is recognised over the service period, being the period from the date the instrument is granted until the expiry date. Grant date was 23 November 2012. Information regarding the entitlements under the LTICEP is as follows:

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Total amount recognised as an expense	350	-	-	-
Liability recognised for bonus payable	350	-	-	-

The assumptions utilised in the modal are as follows:

Volatility (%)	30%
Risk free interest rate (%)	3%
Annual dividends per share (cents)	4.1
Expiry date	30/06/2015
Exercise price ($)	0.72
Market price ($)	0.83

34 Fair value

The following methods and assumptions were used to estimate the fair value of each class of financial asset and liability.

Finance receivables

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

The current average market rate used to fair value finance receivables with a fixed interest rate was 8.58% (2012: 9.06%). Finance receivables with a floating interest rate are deemed to be at current market rates. The current amount of credit provisioning has been deducted from the fair value calculation of finance receivables as a proxy for future losses. Prepayment rates have not been factored into the fair value calculation as they are not deemed to be material.

Investments

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

Other financial assets and liabilities

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

Derivative items

The fair value of interest rate contracts is modelled using observable market inputs (Level 2 under the fair value hierarchy).

Borrowings

The fair value of deposits, bank borrowings and other borrowings is the present value of future cash flows and is based on the current market interest rates payable by the Group for debt of similar maturities.

	GROUP					
	Held for trading	Loans and receivables	Available for sale	Financial liabilities at amortised cost	Total Carrying Value	Total Fair Value
	$000	$000	$000	$000	$000	$000
June 13						
Cash and cash equivalents	-	174,262	-	-	174,262	174,262
Investments	-	-	165,223	-	165,223	165,223
Finance receivables	-	1,735,398	-	-	1,735,398	1,734,792
Finance receivables - securitised	-	274,978	-	-	274,978	278,540
Derivative financial assets	649	-	-	-	649	649
Other financial assets	-	7,286	-	-	7,286	7,286
Total financial assets	**649**	**2,191,924**	**165,223**	**-**	**2,357,796**	**2,360,752**
Borrowings	-	-	-	1,838,619	1,838,619	1,841,657
Borrowings - securitised	-	-	-	258,934	258,934	258,934
Derivative financial liabilities	30	-	-	-	30	30
Other financial liabilities	-	-	-	17,394	17,394	17,394
Total financial liabilities	**30**	**-**	**-**	**2,114,947**	**2,114,977**	**2,118,015**
June 12						
Cash and cash equivalents	-	89,689	-	-	89,689	89,689
Investments	-	-	24,327	-	24,327	24,327
Finance receivables	-	1,801,508	-	-	1,801,508	1,800,616
Finance receivables - securitised	-	276,768	-	-	276,768	281,104
Derivative financial assets	2,122	-	-	-	2,122	2,122
Other financial assets	-	3,080	-	-	3,080	3,080
Total financial assets	**2,122**	**2,171,045**	**24,327**	**-**	**2,197,494**	**2,200,938**
Borrowings	-	-	-	1,675,130	1,675,130	1,681,134
Borrowings - securitised	-	-	-	264,359	264,359	264,359
Derivative financial liabilities	1,459	-	-	-	1,459	1,459
Other financial liabilities	-	-	-	18,329	18,329	18,329
Total financial liabilities	**1,459**	**-**	**-**	**1,957,818**	**1,959,277**	**1,965,281**

34 Fair value (continued)

	COMPANY					
	Held for trading	Loans and receivables	Available for sale	Financial liabilities at amortised cost	Total Carrying Value	Total Fair Value
	$000	$000	$000	$000	$000	$000
June 13						
Cash and cash equivalents	-	1,485	-	-	1,485	1,485
Other financial assets	-	36	-	-	36	36
Total financial assets	**-**	**1,521**	**-**	**-**	**1,521**	**1,521**
Other financial liabilities	-	-	-	226	226	226
Total financial liabilities	**-**	**-**	**-**	**226**	**226**	**226**
June 12						
Cash and cash equivalents	-	469	-	-	469	469
Other financial assets	-	194	-	-	194	194
Total financial assets	**-**	**663**	**-**	**-**	**663**	**663**
Other financial liabilities	-	-	-	300	300	300
Total financial liabilities	**-**	**-**	**-**	**300**	**300**	**300**

35 Risk management policies

The Group is committed to the management of risk. The primary risk categories are credit, liquidity, market (including interest rate), operational and compliance. The Group's risk management strategy is set by the Board of Directors (Board). The Group has put in place management structures and information systems to manage risks incorporated in the Group's Risk Management Programme (RMP). The Group has separate monitoring tasks where feasible and subjects all risk processes to hindsight and internal audit, and accounting systems to regular internal and external audits.

Role of the Board and the Risk Committee

The Board, through its Board Risk Committee (BRC) is responsible for the overall risk management process and the development of the RMP. The role of the BRC is to assist the Board to formulate its risk appetite, understand the risks the Group faces for each strategic, credit, liquidity, market (including interest rate), legal and governance, financial and tax, operational and capital adequacy risk and to ensure that all policy and decisions are made in accordance with the Group's corporate values and guiding principles. The BRC has the following responsibilities:

- To oversee the Group's risk profile and review and approve the Group's Risk Management Framework within the context of the risk-reward strategy determined by the Board at least annually.
- To make recommendations regarding high-level liquidity / capital / funding policies and strategy, including the use of securitisation and special investment vehicles.
- To agree and recommend for Board approval and annual review; a set of risk limits and conditions that apply to the taking of risk, as delegated to the Risk Committee by the Board, that are consistent with the Board's determined risk appetite. This includes the authorities delegated by the Board to the Chief Executive Officer (CEO), Chief Financial Officer (CFO), Chief Risk Officer (CRO) and any other officers of the Bank to whom the Board or the Committee have delegated authority, and to consider and accept risks beyond management's approval discretion where deemed appropriate.
- To monitor the risk profile, performance, capital levels, exposures against limits and the management and control of the Group's risks.
- To review significant correspondence with the Group's regulators, and receive reports from management on the Group's regulatory relations and report any significant issues to the Board.
- To monitor changes anticipated in the economic and business environment and other factors considered relevant to the Group's risk profile and capital adequacy.
- To review significant risk management issues that are raised in external or internal audits as well as the length of time and action taken to resolve such issues.
- To ensure an appropriate set of applicable corporate governance principles are developed, and reviewed on a regular basis.

35 Risk management policies (continued)

The BRC consists of four directors, of which at least three are non-executive directors and two are independent directors. In addition the CEO, CRO and CFO are in attendance at meetings. The BRC meets at least bi-monthly to review identified risk issues, and reports directly to the Board. A member of the BRC sits on the Audit Committee and vice versa.

Audit Committee and Internal Audit

The Group has an internal audit function, the objective of which is to provide independent, objective assurance over the internal control environment and additional services designed to add value and improve the Group's operations. It assists the Group to accomplish its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. Internal audit is granted full, free and unfettered access to any and all of the organisation's records, personnel and physical properties deemed necessary to accomplish its internal audit activities.

A regular cycle of testing has been implemented to cover all areas of the business. Its focus is on assessment, management and control of risks. The intention is to cycle through various business units and operational areas on a pre-set and agreed cycle relative to assessed risk, looking at the specific internal control issues pertinent to the area, with a requirement to meet or exceed the Standards for the Professional Practice of Internal Auditing of The Institute of Internal Auditors.

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

All internal audit reports are addressed to the manager of the relevant area that is being audited. Management comments are obtained from the process owner(s) and are included in the report.

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

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

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

Asset and Liability Committee (ALCO)

The ALCO comprises the CEO (Chair), CFO, CRO, Head of Treasury & Strategy, Treasurer, Head of Consumer & Retail and Head of Business & Rural. The ALCO has responsibility for overseeing aspects of the Bank's financial position risk management. The purpose of the ALCO is to support the BRC with specific responsibilities for decision making and oversight of risk matters in relation to:

- Balance sheet structure;
- Non-traded interest rate risk (including the investment of capital);
- Liquidity and funding; and
- Capital management.

The ALCO usually meet monthly, and reports to the BRC.

Executive Risk Committee (ERC)

The ERC comprises the CEO (Chair), CFO, CRO, Chief Operating Officer, Head of Treasury & Strategy, Head of Consumer & Retail and Head of Business & Rural, Head of Human Resources and Group General Counsel. The ERC has responsibility for overseeing all risk aspects not considered by ALCO. The purpose of ERC is to support the BRC with specific responsibilities for decision making and oversight of risk matters in relation to:

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

35 Risk management policies (continued)

Specific areas of risk management

Credit risk

Credit risk is the risk of loss arising from the non-performance of a counterparty to an instrument or facility. Credit risk arises when funds are extended, committed, invested or otherwise exposed through contractual arrangements, and encompasses both on and off balance sheet instruments.

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

To manage this risk the BRC has been delegated the task of overseeing a formal credit risk management strategy. The BRC reviews the Group's credit risk exposures to ensure consistency with the Group's credit policies to manage all aspects of credit risk. The credit risk management strategies ensure that:

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

The Group has adopted a detailed Credit Policy Framework supported by Lending Standards providing criteria for finance products within each business sector. The combination of the Credit Policy Framework and Lending Standards guides credit assessment, credit risk grading, documentation standards, legal procedures and compliance with regulatory and statutory requirements.

The Risk Committee has authority from the Board for approval of all credit exposures. Lending authority has been individually provided to the Chief Risk Officer, for delegation through the business units under a detailed Delegated Lending Authority framework. Application of credit discretions in the business operation are monitored through a defined review and hindsight structure. Delegated Lending Authorities are provided to individual officers with due cognisance of their experience and ability. Larger and higher risk exposures require approval of senior management, the credit risk committee and ultimately through to the CRO or the BRC.

Although the Group relies primarily on the integrity of borrowers and their ability to make contracted repayments, the Group also requires appropriate collateral for loans. This collateral is usually by way of first charge over the asset financed and usually includes personal guarantees from borrowers and business owners. Because of the wide nature of the collateral held against loans it is impractical to provide an accurate estimate of their fair value.

The Group's exposure to credit risk is governed by a policy approved by the Board and managed by the ERC. This policy sets out the nature of risk which may be taken and aggregate risk limits, and the ERC must conform to this. The objective of the ERC is to manage the best risk return result from lending activities and avoid risk at a transactional and portfolio level inconsistent with the Groups risk appetite.

In addition to regular internal audit activity in regards to credit standards, the Group employs a comprehensive process of hind sighting loans to ensure that credit policies and the quality of credit processes are maintained.

Market risk

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

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

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

35 Risk management policies (continued)

Market risk (continued)

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

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

Liquidity risk

Liquidity risk is the risk that under certain conditions, cash outflows can exceed cash inflows in a given period. The Group maintains sufficient liquid funds to meet its commitments based on historical and budgeted cash flow forecasts. Management of liquidity risk is achieved by maintaining a prudent level of liquid assets, utilisation of securitisation vehicles and management control of the growth of the business.

The Group's liquidity risks are governed by a Board approved liquidity strategy that defines policy, systems and procedures for measuring, assessing, reporting and managing liquidity. This also includes a formal contingency plan for dealing with a liquidity crisis.

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

Operational risk

Operational risk is the risk arising from day to day operational activities which may result in direct or indirect loss. Operational risk losses can occur as a result of fraud, human error, missing or inadequately designed processes, failed systems, damage to physical assets, improper behaviour or from external events. The losses range from direct financial losses, to reputational damage, unfavourable media attention, or loss of staff or clients. Examples include failure to comply with policy and legislation, human error, natural disasters, fraud and other malicious acts. Where appropriate, risks are mitigated by insurance.

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

- The first line of defence is the business line management for the identification, management and mitigation of the risks associated with the products and processes of the business. This accountability includes regular testing and certification of the adequacy and effectiveness of controls and compliance with the Group's policies.
- The second line of defence is the Risk & Compliance function, responsible for the design and ownership of the Operational Risk Policies. It incorporates key processes including risk and control assessment, scenario analysis, loss data collection, new product approval process, key risk indicators, notifiable events process, and the self-certification process.
- The third line of defence is audit. Internal Audit is responsible for assessing compliance with policy frameworks and for providing independent evaluation of the adequacy and effectiveness of the risk and control framework.

The Group's exposure to Operational risk is governed by a policy approved by the Board and managed by the ERC. This policy sets out the nature of risk which may be taken and aggregate risk limits, and the ERC must conform to this. The objective of the ERC is to manage the identification of risk and maintenance of a suitable control environment so residual risk to the Group is consistent with the Groups risk appetite.

36 Credit risk exposure

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

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

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Cash and cash equivalents	174,262	89,689	1,485	469
Investments	165,223	24,327	-	-
Finance receivables	2,010,376	2,078,276	-	-
Derivative financial assets	649	2,122	-	-
Other financial assets	7,286	3,080	36	208
Total on balance sheet credit exposures	**2,357,796**	**2,197,494**	**1,521**	**677**

(b) Concentration of credit risk by geographic region

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Auckland	706,137	653,517	1,501	483
Wellington	217,928	120,469	-	-
Rest of North Island	548,046	482,342	-	-
Canterbury	531,871	584,086	-	-
Rest of South Island	369,775	365,112	-	-
	2,373,757	**2,205,526**	**1,501**	**483**
Provision for collectively impaired assets	(15,961)	(8,032)	-	-
Due from related parties	-	-	20	194
Total on balance sheet credit exposures	**2,357,796**	**2,197,494**	**1,521**	**677**

(c) Concentration of credit risk by industry sector

Agriculture	499,942	530,440	-	-
Forestry and Fishing	29,565	35,698	-	-
Mining	19,044	14,325	-	-
Manufacturing	79,915	56,304	-	-
Finance & Insurance	348,166	134,630	1,501	483
Wholesale trade	76,816	38,669	-	-
Retail trade	155,962	144,608	-	-
Households	629,854	678,508	-	-
Property and Business services	320,198	297,944	-	-
Transport and storage	25,267	57,709	-	-
Other Services	189,028	216,691	-	-
	2,373,757	**2,205,526**	**1,501**	**483**
Provision for collectively impaired assets	(15,961)	(8,032)	-	-
Due from related parties	-	-	20	194
Total on balance sheet credit exposures	**2,357,796**	**2,197,494**	**1,521**	**677**

(d) Commitments to extend credit

Undrawn facilities available to customers	106,702	125,492	-	-
Conditional commitments to fund at future dates	48,428	38,796	-	-

As at 30 June 2013 there are no undrawn lending commitments to counterparties for whom drawn balances are classified as individually impaired (2012: nil).

36 Credit risk exposure (continued)

(e) Real Estate Credit Limited Management agreement (RECL Agreement)

MARAC entered into the RECL agreement on 5 January 2011. Under this arrangement, Real Estate Credit Limited (RECL) managed certain non-core real estate loans of MARAC for a 5 year period ending 5 January 2016, and assumed the risk of loss on those loans for that period. The payment obligations of RECL were "limited in recourse" to a pool of security provided by RECL. This pool of security included an $11 million 5 year zero coupon bond (issued by Westpac New Zealand Limited which is rated AA- by Standard & Poor's (Australia) Pty Limited), and other assets (initially real estate or real estate loans) with a required minimum security value of (initially) $19 million.

MARAC paid RECL an upfront fee of $11 million (which was being amortised over the 5 year period of the arrangement), and paid an ongoing management fee of $200,000 per annum.

On 4 June 2013 the RECL Agreement was terminated and RECL transferred to MARAC the assets charged to secure the compensation payment.

As a result of the RECL Agreement being terminated, the unamortised portion of the upfront fee paid to RECL has been written off. This write off is reflected in the Group's result for the year ended 30 June 2013, refer to Note 9 - Selling and administration expenses. The amount written off was $6.1 million.

For the year ended 30 June 2012, the benefit of the RECL agreement was included in the determination of the charge and the analysis of risk gradings and the classification of individually impaired assets, refer to Note 37 - Asset quality.

(f) PGG Wrightson Finance Limited guaranteed loans

On 31 August 2011, Heartland acquired 100% of PGG Wrightson Finance Limited from PGG Wrightson Limited (PGW). As part of the acquisition, the Bank and PGW entered into a Deed of Guarantee and Indemnity in relation to certain loans (the Recourse Loans), with book value on acquisition of $30.6 million. This arrangement provides Heartland with a guarantee from PGW in relation to the future payment of principal and interest on the Recourse Loans for a prescribed period of three years. As at 30 June 2013, total recourse loans of $5.7 million were included in the Banking Group's finance receivables (2012: $28.9 million).

37 Asset quality

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

Corporate	
Rural	Lending to the farming sector primarily livestock, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers. Includes lending to individuals and small to medium enterprises.
Non-core Property	Property asset lending including non-core property.
Other	All other lending that does not fall into another category.
Residential	Lending secured by a first ranking mortgage over a residential property used primarily for residential purposes either by the mortgagor or a tenant of the mortgagor.
All Other	Consumer lending to individuals.

(a) Finance receivables by credit risk concentration

		GROUP					
	NOTE	Rural $000	Corporate Property $000	Other $000	Residential $000	All Other $000	Total $000
Jun 13							
Neither at least 90 days past due or impaired		522,815	17,866	797,195	230,283	393,243	1,961,402
At least 90 days past due	37(b)	3,975	11,045	7,584	814	3,180	26,598
Individually impaired	37(c)	2,979	61,634	4,688	-	-	69,301
Restructured assets		6	-	1,225	-	2,335	3,566
Provision for impairment	37(e)	(1,706)	(41,512)	(5,632)	(134)	(1,507)	(50,491)
Total net finance receivables		**528,069**	**49,033**	**805,060**	**230,963**	**397,251**	**2,010,376**
Jun 12							
Neither at least 90 days past due or impaired		552,740	50,202	713,550	322,243	349,052	1,987,787
At least 90 days past due	37(b)	13,014	27,167	8,945	15	2,863	52,004
Individually impaired	37(c)	1,060	50,860	2,275	2,630	-	56,825
Restructured assets		19	5,522	1,145	-	2,400	9,086
Provision for impairment	37(e)	(2,519)	(17,877)	(4,401)	(774)	(1,855)	(27,426)
Total net finance receivables		**564,314**	**115,874**	**721,514**	**324,114**	**352,460**	**2,078,276**

(b) Past due but not impaired

	GROUP					
	Rural $000	Corporate Property $000	Other $000	Residential $000	All Other $000	Total $000
Jun 13						
Less than 30 days past due	7,510	179	6,050	1,909	8,675	24,323
At least 30 and less than 60 days past due	1,390	-	3,457	690	2,371	7,908
At least 60 but less than 90 days past due	143	127	3,263	200	1,434	5,167
At least 90 days past due	3,975	11,045	7,584	814	3,180	26,598
Total past due but not impaired	**13,018**	**11,351**	**20,354**	**3,613**	**15,660**	**63,996**
Jun 12						
Less than 30 days past due	5,295	365	9,724	1,658	6,696	23,738
At least 30 and less than 60 days past due	2,427	139	4,492	722	2,529	10,309
At least 60 but less than 90 days past due	2,544	3,455	1,401	251	1,208	8,859
At least 90 days past due	13,014	27,167	8,945	15	2,863	52,004
Total past due but not impaired	**23,280**	**31,126**	**24,562**	**2,646**	**13,296**	**94,910**

37 Asset quality (continued)

(c) Individually impaired assets

	GROUP					
	Rural	Corporate Property	Other	Residential	All Other	Total
	$000	$000	$000	$000	$000	$000
Jun 13						
Opening	1,060	50,860	2,275	2,630	-	56,825
Additions	2,980	30,938	5,631	133	-	39,682
Deletions	(795)	(16,740)	(1,160)	(1,832)	-	(20,527)
Write offs	(266)	(3,424)	(2,058)	(931)	-	(6,679)
Closing gross individually impaired assets	**2,979**	**61,634**	**4,688**	**-**	**-**	**69,301**
Less: provision for individually impairment assets	1,125	31,252	2,153	-	-	34,530
Total net impaired assets	**1,854**	**30,382**	**2,535**	**-**	**-**	**34,771**
Jun 12						
Opening	195	51,853	16,489	-	-	68,537
Additions	2,589	30,070	5,056	2,661	-	40,376
Deletions	(1,837)	(24,359)	(13,096)	(31)	-	(39,323)
Assumed on acquisition	1,871	-	-	-	-	1,871
Write offs	(1,758)	(6,704)	(6,174)	-	-	(14,636)
Closing gross individually impaired assets	**1,060**	**50,860**	**2,275**	**2,630**	**-**	**56,825**
Less: provision for individually impairment assets	696	16,917	1,086	695	-	19,394
Total net impaired assets	**364**	**33,943**	**1,189**	**1,935**	**-**	**37,431**

(d) Credit risk grading

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

The Group classifies finance receivables as Behavioural or Judgement.

The Behavioural portfolio consists mainly of consumer and retail receivables and usually relates to financing the acquisition of a single asset. Consumer loans are typically introduced by vendors of the asset financed and are smaller in value than Judgement loans. Behavioural loans are risk graded based on arrears status.

Behavioural loans are classified as either not in arrears, active, arrangement, non-performing / repossession or recovery, as described below:

- Active – loans for which the arrears category has reached 5 days overdue.
- Arrangement – 5 to 34 days overdue accounts for which arrangements have or are in the process of being made for arrears to be repaid.
- Non-performing / Repossession – residential mortgage loans that are greater than 90 days past due / other loans for which security has or is in the process of being repossessed.
- Recovery loans – loans for which security has been sold and shortfalls are being sought from the customer or where other recovery action is being taken.

The Judgement portfolio consists mainly of business and rural lending and includes non-core property. Judgement loans relate to loans where an ongoing and detailed working relationship with the customer has been developed.

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

In the Judgement portfolio, grade 1 is the strongest risk grade for undoubted risk and grade 9 represents the highest risk grade where a loss is probable. Grade 10 reflects loss accounts written off. Grades 2 to 8 represent ascending steps in management's assessment of risk of exposures. The Group typically finances new loans in risk grades 2 to 5 of the Judgement portfolio.

37 Asset quality (continued)

(d) Credit risk grading (continued)

	GROUP					
	Rural $000	Corporate Property $000	Other $000	Residential $000	All Other $000	Total $000
Jun 13						
Judgement portfolio						
Grade 1 - Very Strong	575	-	-	-	-	575
Grade 2 - Strong	6,689	-	8,877	41	-	15,607
Grade 3 - Sound	17,050	-	64,242	2,320	-	83,612
Grade 4 - Adequate *	106,467	-	153,848	4,671	-	264,986
Grade 5 - Acceptable	234,912	1,979	181,851	19,326	-	438,068
Grade 6 - Monitor	122,876	12,297	60,560	2,637	-	198,370
Grade 7 - Substandard	5,150	-	12,120	764	-	18,034
Grade 8 - Doubtful	269	20,924	325	-	-	21,518
Grade 9 - At risk of loss	1,850	24,093	1,818	-	-	27,761
Total Judgement portfolio	**495,838**	**59,293**	**483,641**	**29,759**	**-**	**1,068,531**
Behavioural portfolio						
Not in arrears	32,565	-	318,094	196,545	381,730	928,934
Active	197	-	3,346	4,517	8,444	16,504
Arrangement	45	-	1,985	-	6,116	8,146
Non-performing / Repossession	5	-	902	-	1,319	2,226
Recovery	-	-	571	276	1,149	1,996
Total Behavioural portfolio	**32,812**	**-**	**324,898**	**201,338**	**398,758**	**957,806**
Provision for collectively impaired assets	(581)	(10,260)	(3,479)	(134)	(1,507)	(15,961)
Total finance receivables	**528,069**	**49,033**	**805,060**	**230,963**	**397,251**	**2,010,376**
Jun 12						
Judgement portfolio						
Grade 1 - Very Strong	1,280	-	-	-	-	1,280
Grade 2 - Strong	3,273	-	12,648	1,169	-	17,090
Grade 3 - Sound	20,137	6,018	52,240	4,564	-	82,959
Grade 4 - Adequate *	120,779	58,054	134,472	10,472	-	323,777
Grade 5 - Acceptable	220,508	23,388	181,421	17,704	-	443,021
Grade 6 - Monitor	121,666	565	61,249	1,835	-	185,315
Grade 7 - Substandard	32,410	7,397	12,984	569	-	53,360
Grade 8 - Doubtful	4,994	8,141	961	-	-	14,096
Grade 9 - At risk of loss	169	13,271	31	-	-	13,471
Total Judgement portfolio	**525,216**	**116,834**	**456,006**	**36,313**	**-**	**1,134,369**
Behavioural portfolio						
Not in arrears	39,887	-	259,493	283,301	338,438	921,119
Active	244	-	2,443	1,657	5,600	9,944
Arrangement	365	-	4,143	972	8,270	13,750
Non-performing / Repossession	81	-	1,972	1,950	383	4,386
Recovery	344	-	772	-	1,624	2,740
Total Behavioural portfolio	**40,921**	**-**	**268,823**	**287,880**	**354,315**	**951,939**
Provision for collectively impaired assets	(1,823)	(960)	(3,315)	(79)	(1,855)	(8,032)
Total finance receivables	**564,314**	**115,874**	**721,514**	**324,114**	**352,460**	**2,078,276**

* *In determining the Group's risk grading, the following arrangements have been taken into consideration:*

- *PGG Wrightson Finance Limited guaranteed loans, refer to Note 36(f) - Credit risk exposure for more details. In the risk grading table above, as at 30 June 2013 $6 million (2012: $29 million) of Judgement loans have been transferred from risk grades below Acceptable to an Adequate risk grade as they are covered by the Deed of Guarantee and Indemnity with PGG Wrightson Limited.*
- *The RECL Agreement, refer to Note 36(e) - Credit risk exposure for more details. In the risk grading table above, as at 30 June 2012 $48 million of Judgement loans had been transferred from risk grades below Acceptable to an Adequate risk grade as they were covered by the RECL Agreement. The RECL Agreement was terminated on 4 June 2013.*

37 Asset quality (continued)

(e) Provision for impairment

For Behavioural loans, as arrears drive provision outcomes, the trend in arrears behaviour is an indicator of future provisioning impact. Each arrears classification carries a provision for potential loss based on historical experience for that classification in the same portfolio.

Judgement loans in grades 6 to 8 ordinarily attract a collective provision based on risk grading overlaid with the strength of security position, except for risk grades 6 which have strong security and accordingly attract no collective provision (typically rural exposures). Other collective provisions are also maintained where considered appropriate against a class of loans or those with common risk characteristics. Judgement loans with a risk grade of 1 to 5 may be past due and not attract a provision if the Group has reviewed the risk position and it is deemed to remain sound. Under such circumstances normally an amended credit risk grade will result.

The Group raises provisions based on historical loss experience for loans risk graded in grades 6 to 8. Loans in grade 9 of the Judgement portfolio are individually assessed for impairment.

	GROUP					
	Rural $000	Corporate Property $000	Other $000	Residential $000	All Other $000	Total $000
Jun 13						
Provision for individually impaired assets						
Opening provision for individually impaired assets	696	16,917	1,086	695	-	19,394
Impairment loss for the year						
- charge for the year	687	9,115	3,036	263	-	13,101
- RECL recovery	-	9,809	-	-	-	9,809
- recoveries	26	1	135	-	-	162
- write offs	(266)	(3,424)	(2,058)	(931)	-	(6,679)
- effect of discounting	(18)	(1,166)	(46)	(27)	-	(1,257)
Closing provision for individually impaired assets	**1,125**	**31,252**	**2,153**	**-**	**-**	**34,530**
Provision for collectively impaired assets						
Opening provision for collective impaired assets	1,823	960	3,315	79	1,855	8,032
Impairment loss for the year						
- charge/(credit) for the year	(1,244)	9,090	980	62	538	9,426
- RECL recovery	-	216	-	-	-	216
- recoveries	6	1	114	-	147	268
- write offs	(4)	(7)	(930)	(7)	(1,033)	(1,981)
Closing provision for collective impaired assets	**581**	**10,260**	**3,479**	**134**	**1,507**	**15,961**
Total provision for impairment	**1,706**	**41,512**	**5,632**	**134**	**1,507**	**50,491**
Jun 12						
Provision for individually impaired assets						
Opening provision for individually impaired assets	134	20,047	5,976	-	-	26,157
Impairment loss for the year						
- charge for the year *	1,001	3,697	1,528	695	-	6,921
- recoveries	35	32	160	-	-	227
- write offs	(1,758)	(6,704)	(6,174)	-	-	(14,636)
- assumed on acquisition	1,284	-	-	-	-	1,284
- effect of discounting	-	(155)	(404)	-	-	(559)
Closing provision for individually impaired assets	**696**	**16,917**	**1,086**	**695**	**-**	**19,394**
Provision for collectively impaired assets						
Opening provision for collective impaired assets	2,501	1,595	5,079	2,037	928	12,140
Impairment loss for the year						
- charge/(credit) for the year *	(682)	(907)	(182)	(1,958)	2,450	(1,279)
- recoveries	4	-	231	-	116	351
- write offs	-	272	(1,813)	-	(1,639)	(3,180)
Closing provision for collective impaired assets	**1,823**	**960**	**3,315**	**79**	**1,855**	**8,032**
Total provision for impairment	**2,519**	**17,877**	**4,401**	**774**	**1,855**	**27,426**

* *In determining the charge for the year ended 30 June 2012, the RECL Agreement was taken into consideration, refer to Note 36(e) - Credit risk exposure for more details. In assessing the requirements for provisions, the Group identified loans for which a loss was expected to be covered by the RECL Agreement of $28.5 million as at 30 June 2012, and to this extent the RECL Agreement was fully utilised. The agreement covered the MARAC non-core property loans with a net book value of $94 million as at 30 June 2012.*

38 Liquidity risk

Contractual liquidity profile of financial assets and liabilities

The following tables show the cash flows on the Group's financial liabilities and unrecognised loan commitments on the basis of their earliest possible contractual maturity. In the following tables, total financial assets do not include unrecognised loan commitments and total financial liabilities do not include undrawn committed bank facilities.

The tables have been prepared using estimates of the average interest rate applicable for each asset or liability class during the contractual term.

	GROUP						
	On Demand $000	0-6 Months $000	6-12 Months $000	1-2 Years $000	2-5 Years $000	5+ Years $000	Total $000
Jun 13							
Cash and cash equivalents	174,262	-	-	-	-	-	174,262
Investments	11,520	1,647	47,882	36,923	79,522	-	177,494
Finance receivables	-	562,696	283,239	415,549	496,023	448,422	2,205,929
Finance receivables - securitised	-	55,889	55,910	89,524	91,789	65,199	358,311
Derivative financial assets	649	-	-	-	-	-	649
Other financial assets	-	7,286	-	-	-	-	7,286
Total financial assets	**186,431**	**627,518**	**387,031**	**541,996**	**667,334**	**513,621**	**2,923,931**
Borrowings	452,201	859,386	387,733	119,944	63,501	-	1,882,765
Borrowings - securitised	-	4,496	260,834	-	-	-	265,330
Derivative financial liabilities	30	-	-	-	-	-	30
Other financial liabilities	-	17,394	-	-	-	-	17,394
Total financial liabilities	**452,231**	**881,276**	**648,567**	**119,944**	**63,501**	**-**	**2,165,519**
Net financial (liabilities) / assets	**(265,800)**	**(253,758)**	**(261,536)**	**422,052**	**603,833**	**513,621**	**758,412**
Unrecognised loan commitments	106,702	-	-	-	-	-	106,702
Undrawn committed bank facilities	240,000	-	-	-	-	-	240,000

The undrawn committed bank facilities totalling $240.0 million were available to be drawn down on demand. To the extent drawn, 240.0 million is contractually repayable in 6-12 months' time upon facility expiry.

	On Demand $000	0-6 Months $000	6-12 Months $000	1-2 Years $000	2-5 Years $000	5+ Years $000	Total $000
Jun 12							
Cash and cash equivalents	89,689	-	-	-	-	-	89,689
Investments	-	498	498	996	25,314	-	27,306
Finance receivables	-	572,857	336,063	342,005	509,685	638,107	2,398,717
Finance receivables - securitised	-	53,568	54,157	86,874	83,887	112,015	390,501
Derivative financial assets	2,122	-	-	-	-	-	2,122
Other financial assets	-	3,080	-	-	-	-	3,080
Total financial assets	**91,811**	**630,003**	**390,718**	**429,875**	**618,886**	**750,122**	**2,911,415**
Borrowings	237,036	760,301	419,224	272,619	49,549	-	1,738,729
Borrowings - securitised	-	4,578	192,072	75,157	-	-	271,807
Derivative financial liabilities	1,459	-	-	-	-	-	1,459
Other financial liabilities	-	18,329	-	-	-	-	18,329
Total financial liabilities	**238,495**	**783,208**	**611,296**	**347,776**	**49,549**	**-**	**2,030,324**
Net financial (liabilities) / assets	**(146,684)**	**(153,205)**	**(220,578)**	**82,099**	**569,337**	**750,122**	**881,091**
Unrecognised loan commitments	125,492	-	-	-	-	-	125,492
Undrawn committed bank facilities	335,000	-	-	-	-	-	335,000

The undrawn committed bank facilities totalling $335.0 million are available to be drawn down on demand. To the extent drawn, $50.0 million is contractually repayable in 0-6 months' time, $110.0 million is contractually repayable in 6-12 months' time and $175.0 million is contractually repayable in 1-2 years' time upon facility expiry.

38 Liquidity risk (continued)

Expected maturity profile of financial assets and liabilities

The tables below show management's expected maturities of existing financial assets and financial liabilities.

Expected maturities of financial assets are based on management's best estimate having regard to current market conditions and past experience. Historical deposit reinvestment levels have been applied to borrowings. Other financial liabilities reflect contractual maturities.

The below does not reflect a forward looking view of how the Group expects actual financial assets and liabilities to perform in the future, as it does not include new lending and borrowing.

	GROUP						
	On Demand $000	0-6 Months $000	6-12 Months $000	1-2 Years $000	2-5 Years $000	5+ Years $000	Total $000
Jun 13							
Cash and cash equivalents	174,262	-	-	-	-	-	174,262
Investments	11,520	1,647	47,882	36,923	79,522	-	177,494
Finance receivables	-	520,198	421,900	514,305	468,854	61,358	1,986,615
Finance receivables - securitised	-	81,562	72,570	97,603	64,991	776	317,502
Derivative financial assets	649	-	-	-	-	-	649
Other financial assets	-	7,286	-	-	-	-	7,286
Total financial assets	**186,431**	**610,693**	**542,352**	**648,831**	**613,367**	**62,134**	**2,663,808**
Borrowings	4,522	342,029	231,600	357,000	590,880	474,783	2,000,814
Borrowings - securitised	-	53,918	3,572	7,203	21,628	210,000	296,321
Derivative financial liabilities	30	-	-	-	-	-	30
Other financial liabilities	-	17,394	-	-	-	-	17,394
Total financial liabilities	**4,552**	**413,341**	**235,172**	**364,203**	**612,508**	**684,783**	**2,314,559**
Net financial assets / (liabilities)	**181,879**	**197,352**	**307,180**	**284,628**	**859**	**(622,649)**	**349,249**
Unrecognised loan commitments	106,702	-	-	-	-	-	106,702
Undrawn committed bank facilities	240,000	-	-	-	-	-	240,000
Jun 12							
Cash and cash equivalents	89,689	-	-	-	-	-	89,689
Investments	-	498	498	996	25,314	-	27,306
Finance receivables	-	579,947	386,570	372,340	666,179	56,459	2,061,495
Finance receivables - securitised	-	67,976	60,171	82,716	115,136	-	325,999
Derivative financial assets	2,122	-	-	-	-	-	2,122
Other financial assets	-	3,080	-	-	-	-	3,080
Total financial assets	**91,811**	**651,501**	**447,239**	**456,052**	**806,629**	**56,459**	**2,509,691**
Borrowings	2,370	267,212	226,095	456,293	546,244	359,443	1,857,657
Borrowings - securitised	-	4,578	4,503	9,082	27,269	265,746	311,178
Derivative financial liabilities	1,459	-	-	-	-	-	1,459
Other financial liabilities	-	18,329	-	-	-	-	18,329
Total financial liabilities	**3,829**	**290,119**	**230,598**	**465,375**	**573,513**	**625,189**	**2,188,623**
Net financial assets / (liabilities)	**87,982**	**361,382**	**216,641**	**(9,323)**	**233,116**	**(568,730)**	**321,068**
Unrecognised loan commitments	125,492	-	-	-	-	-	125,492
Undrawn committed bank facilities	335,000	-	-	-	-	-	335,000

39 Interest rate risk

Contractual Repricing Analysis

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

	GROUP						
	0-3 Months $000	4-6 Months $000	6-12 Months $000	1-2 Years $000	2+ Years $000	Non-interest bearing $000	Total $000
Jun 13							
Financial assets							
Cash and cash equivalents	174,262	-	-	-	-	-	174,262
Investments	128,370	-	15,545	4,291	17,017	-	165,223
Finance receivables	1,206,542	95,833	147,126	157,208	128,155	534	1,735,398
Finance receivables - securitised	80,968	29,685	50,699	67,597	46,029	-	274,978
Other financial assets	649	-	-	-	-	7,286	7,935
Total financial assets	**1,590,791**	**125,518**	**213,370**	**229,096**	**191,201**	**7,820**	**2,357,796**
Financial liabilities							
Borrowings	961,916	339,250	373,581	111,129	52,743	-	1,838,619
Borrowings - securitised	258,934	-	-	-	-	-	258,934
Other financial liabilities	30	-	-	-	-	17,394	17,424
Total financial liabilities	**1,220,880**	**339,250**	**373,581**	**111,129**	**52,743**	**17,394**	**2,114,977**
Effect of derivatives held for risk management	179,350	(18,700)	(45,330)	(61,200)	(54,120)	-	-
Net financial assets	**549,261**	**(232,432)**	**(205,541)**	**56,767**	**84,338**	**(9,574)**	**242,819**
Jun 12							
Financial assets							
Cash and cash equivalents	89,689	-	-	-	-	-	89,689
Investments	22,149	-	-	-	2,178	-	24,327
Finance receivables	1,248,945	98,677	153,534	172,003	127,642	707	1,801,508
Finance receivables - securitised	89,285	30,031	49,895	69,868	37,689	-	276,768
Other financial assets	2,122	-	-	-	-	3,080	5,202
Total financial assets	**1,452,190**	**128,708**	**203,429**	**241,871**	**167,509**	**3,787**	**2,197,494**
Financial liabilities							
Borrowings	669,815	308,897	396,086	259,956	40,376	-	1,675,130
Borrowings - securitised	75,105	189,254	-	-	-	-	264,359
Other financial liabilities	1,459	-	-	-	-	18,329	19,788
Total financial liabilities	**746,379**	**498,151**	**396,086**	**259,956**	**40,376**	**18,329**	**1,959,277**
Effect of derivatives held for risk management	218,387	42,690	(43,869)	(175,718)	(41,490)	-	-
Net financial assets	**924,198**	**(326,753)**	**(236,526)**	**(193,803)**	**85,643**	**(14,542)**	**238,217**

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

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

40 Concentrations of funding

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
(a) Concentration of funding by industry				
Finance	258,934	314,369	-	-
Households	1,732,074	1,518,657	-	-
Listed bond	106,545	106,463	-	-
Total borrowings	**2,097,553**	**1,939,489**	**-**	**-**
(b) Concentration of funding by geographical area				
Auckland	409,923	442,727	-	-
Wellington	304,297	240,758	-	-
Rest of North Island	392,056	325,091	-	-
Canterbury	725,365	681,474	-	-
Rest of South Island	184,800	173,787	-	-
Overseas	81,112	75,652	-	-
Total borrowings	**2,097,553**	**1,939,489**	**-**	**-**

41 Contingent liabilities and commitments

	GROUP		COMPANY	
	Jun 13 $000	Jun 12 $000	Jun 13 $000	Jun 12 $000
Letters of credit, guarantees and performance bonds	5,033	13,404	-	-
Total contingent liabilities	**5,033**	**13,404**	**-**	**-**

The Group also has contingent commitments to fund at future dates as set out in Note 36(d) - Credit risk exposure.

42 Events after the reporting date

Maturity of NZDX listed bond

On 15 July 2013 the NZDX listed bond matured and was repaid in full from funds reported within Cash and Cash equivalents as at 30 June 2013.

CBS Trust securitisation facility

On 31 July 2013, the Group cancelled $50 million of the CBS Trust securitisation facility. On 15 August 2013, the remaining $50 million CBS Trust securitisation facility was cancelled and all of the receivables in CBS Trust were sold back to the Bank.

Declaration of dividend

On 26 August 2013, the Directors resolved to pay a final dividend for the year ended 30 June 2013 of $9.7 million, representing 2.5 cents per share. The dividend is payable on 4 October 2013.

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

Independent auditor’s report

To the shareholders of Heartland New Zealand Limited

Report on the company and group financial statements

We have audited the accompanying financial statements of Heartland New Zealand Limited ("the company") and the group, comprising the company and its subsidiaries, on pages 3 to 43. The financial statements comprise the statements of financial position as at 30 June 2013, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, for both the company and the group.

Directors' responsibility for the company and group financial statements

The directors are responsible for the preparation of company and group financial statements in accordance with generally accepted accounting practice in New Zealand and International Financial Reporting Standards that give a true and fair view of the matters to which they relate, and for such internal control as the directors determine is necessary to enable the preparation of company and group financial statements that are free from material misstatement whether due to fraud or error.

Auditor’s responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the company and group financial statements. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company and 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 company and 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 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.

Our firm has also provided other services to the company and group in relation to general accounting services. Subject to restrictions, partners and employees of our firm may also deal with the company and group on normal terms within the ordinary course of trading activities of the business of the company and group. These matters have not impaired our independence as auditor of the company and group. The firm has no other relationship with, or interest in, the company and group.

Opinion

In our opinion the financial statements on pages 3 to 43:

- comply with generally accepted accounting practice in New Zealand;
- comply with International Financial Reporting Standards;
- give a true and fair view of the financial position of the company and the group as at 30 June 2013 and of the financial performance and cash flows of the company and the group for the year then ended.

Report on other legal and regulatory requirements

In accordance with the requirements of sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993, we report that:

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

KPMG

26 August 2013
Auckland