

**Southland Building Society**

144th Annual Report 2013

Disclosure Statement No. 20 & Annual Financial Statements

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difference  
every day.**

 **SBS** | Bank

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### Chairman

Mr J F Ward  
B Com FCA FlntD  
Chartered Accountant  
Invercargill

### Deputy Chairman

Mr J B Walker  
LLB  
Barrister & Solicitor  
Invercargill

### Directors

Mrs K J Ball  
B Com CA  
Chartered Accountant  
Invercargill

Mr G J Mulvey  
B Com FCA FNZIM  
General Manager  
Invercargill

Mr J J Grant  
Farmer/Company Director  
Balfour

Mr F E Spencer  
BBS (Val & Pty Mgt)  
FNZIV FPINZ AREINZ  
Registered Valuer  
Hastings

Mr A G Neill  
LLB  
Solicitor  
Christchurch

Mr R L Smith  
B Com FNZIM  
Group Managing Director /  
Chief Executive Officer of  
Southland Building Society  
Invercargill

All directors can be  
contacted through:  
Southland Building Society  
51 Don Street  
Invercargill

### Group Managing Director / Chief Executive Officer

Mr R L Smith  
B Com FNZIM  
Invercargill

### Secretary

Mr T D R Loan  
B Com CA DipBusStuds (IS)  
(General Manager Finance)  
Invercargill

### Registered Office

51 Don Street  
Invercargill

### Solicitors

Buddle Findlay  
245 St Asaph Street  
Christchurch

### Auditors

KPMG  
10 Customhouse Quay  
Wellington

# Disclosure Statement for the year ended 31 March 2013

## General Information

Southland Building Society (SBS) is registered as a bank under the Reserve Bank of New Zealand Act 1989 and is required to comply with the conditions of registration as laid down by the Reserve Bank of New Zealand. Southland Building Society operates under two brands "SBS Bank" and "HBS Bank".

This Disclosure Statement has been issued by Southland Building Society in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2013 (the 'Order').

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

### Name and Address for Service of Registered Bank

The name of the registered bank is Southland Building Society (referred to either by its full name, as "SBS", or as the "Bank", or as the "Registered Bank") and the address for service is 51 Don Street, Invercargill. The "Banking Group" consists of the Bank and all of its controlled entities. All controlled entities are incorporated in New Zealand.

### Details of Incorporation

Southland Building Society was established in 1869 and is incorporated under the Building Societies Act 1965. SBS's registration number is 1781001.

### Ownership

Southland Building Society is a mutual building society and is owned by its members by virtue of their membership interests in Southland Building Society. Membership entitlements and voting rights are set out in the Rules of Southland Building Society.

## Guarantee Arrangements

As at the signing date of this Disclosure Statement, the material obligations of the Bank are not guaranteed.

## Pending Proceedings or Arbitration

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

## Other Material Matters

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

## Directorate

All directors of the Bank reside in New Zealand. All directors can be contacted at Southland Building Society, 51 Don Street, Invercargill.

### Independent Non-Executive Directors

JF (John) Ward, BCom FCA FInstD  
(Chairman - Board of Directors)  
Chartered Accountant

JB (Jeff) Walker, LLB  
(Deputy Chairman - Board of Directors)  
Barrister & Solicitor

External Directorships: H&J Smith Holdings Ltd, H&J Smith Ltd, H&J Smith Corporate Ltd, H&J's Hardware Ltd, H&J's Electrical Ltd, H&J's Queenstown Properties Ltd, H&J Smith Parking Building Ltd, H&J Smith Finance Ltd, H&J's Carpet World Ltd, H&J's Properties Ltd, Outdoor World Ltd, Shotover Hardware Ltd, Symphony Retailing Ltd, Lorneville Discount Centre Ltd, South Island Retail Ltd, Outdoor Adventures Ltd, South Island Sports Ltd, Simmer Investments Ltd, Cross Roads Properties Ltd, South Island Department Stores Ltd, SFI Properties Ltd, Corner Trading Ltd, Amtex Corporation Ltd, Witrick No 4 Ltd, Hokonui Investments Ltd, Parthenon Investments Ltd, Trio Corporation Ltd, Tanknology (NZ) Ltd, Skippers Canyon Holdings Ltd, Queenstown Bungy Ltd, Auckland Bungy Ltd, AJ Gear Ltd, Bungy New Zealand Ltd, Paddington Investments No 8 Ltd, Fun Innovators NZ Ltd, Southcom Ltd, 595 Frankton Rd Ltd, Auckland Bridge Adventures Ltd, Passage Holdings Ltd, Auckland Bridge Climb Ltd, KBA Limited, Zephyr NZ Ltd, Aviemore Corporation Ltd, H.A.T. Ltd, H.A.T. 2 Ltd, University of Otago Holdings Ltd, Otago Innovation Ltd

External Directorships: Rough Gully Company Ltd, Rakiura Shipping Ltd, Craig Printing Co Ltd (In Rec), Cargill Trustees Ltd, Manchester Enterprises Ltd

## Disclosure Statement for the year ended 31 March 2013

### Directorate continued

KJ (Kathryn) Ball, BCom CA Chartered Accountant	External Directorships: McIntyre Dick & Partners Ltd, I43 Spey Ltd, I42 Spey Ltd
GJ (Greg) Mulvey, BCom FCA FNZIM General Manager	External Directorships: DB South Island Brewery Ltd
JJ (Jeff) Grant Farmer / Company Director	External Directorships: Milford Sound Development Authority Ltd, National Animal Identification and Tracing (NAIT) Ltd, Copper Valley Holdings Ltd
FE (Frank) Spencer, BBS (Val & Pty Mgt) FNZIV FPINZ AREINZ Registered valuer	External Directorships: Verdure Ltd, Apex Data Solutions Ltd, Crighton Stone Ltd, Logan Stone Ltd
AG (Alec) Neill, LLB Solicitor	External Directorships: Canterbury Trust House Ltd, The Canterbury Community Trust Charities Ltd, Canterbury Direct Investments Ltd, Hyde Park Exports & Investments Ltd, Hyde Park Industrial Developments Ltd, Cubic Solutions Ltd

### Executive Directors

RL (Ross) Smith, BCom FNZIM Group Managing Director / CEO Southland Building Society	External Directorships: Electricity Invercargill Ltd, Electricity Southland Ltd, Peak Power Services Ltd, Powernet Ltd, Power Services Ltd, Pylon Ltd
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### Audit & Risk Committee

Members of the Southland Building Society Audit & Risk Committee as at the date of this General Disclosure Statement are as follows:

KJ Ball (Chairperson) - Independent Non-Executive Director  
JF Ward - Independent Non-Executive Director  
GJ Mulvey - Independent Non-Executive Director  
JJ Grant - Independent Non-Executive Director

### Conflicts of Interest Policy

The policy and current practice of the board of directors (as set out in clause 16.6 of the Rules of Southland Building Society) for avoiding or dealing with conflicts of interest which may arise from personal, professional or business interests of the directors, are that, a director, after becoming aware of the fact that he or she is interested in a transaction or proposed transaction with the Society, shall disclose to the board and cause to be entered in the interests register:

- (i) the nature and monetary value of the director's interest in a transaction if its monetary value is able to be quantified; or
- (ii) the nature and extent of the director's interest in a transaction if its monetary value is not able to be quantified.

A director may not vote on a board resolution in respect of any matter in which that director is interested, nor shall the director be counted in the quorum for the purposes of consideration of that matter.

### Interested Transactions

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

### Solicitors

Buddle Findlay  
245 St Asaph Street  
Christchurch

### Auditors

KPMG  
10 Customhouse Quay  
Wellington

## Disclosure Statement for the year ended 31 March 2013

### Credit Rating

As at 31 March 2013, and for the period to the date of this Disclosure Statement, the credit rating assigned to Southland Building Society is BBB stable. This credit rating is applicable to long term unsecured obligations payable in New Zealand, in New Zealand dollars. The credit rating was issued by Fitch Ratings on 17 July 2007 and was reaffirmed on 23 August 2012. There have been no changes made to the rating in the two years preceding 31 March 2013. The rating is not subject to any qualifications.

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

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

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

### Conditions of Registration

The conditions of registration imposed on Southland Building Society by the Reserve Bank of New Zealand pursuant to section 74 of the Reserve Bank of New Zealand Act 1989, and which apply as at the date of signing of this Disclosure Statement are as follows. These conditions of registration have applied from 31 March 2013.

I. That the banking group complies with the following requirements:

- the total capital ratio of the banking group is not less than 8 percent;
- the tier one capital ratio of the banking group is not less than 6 percent;
- the common equity tier one capital ratio of the banking group is not less than 4.5 percent; and
- the total capital of the banking group is not less than \$30 million.
- the process in Subpart 2H of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated March 2013 is followed for the recognition and repayment of capital.

For the purposes of this condition of registration, capital, the total capital ratio, the tier one capital ratio, and the common equity tier one capital ratio must be calculated in accordance with the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated March 2013.

IA. That—

- the bank has an internal capital adequacy assessment process ("ICAAP") that accords with the requirements set out in the document "Guidelines on a Bank's Internal Capital Adequacy Assessment Process ("ICAAP")" (BS12) dated December 2007;
- under its ICAAP, the bank identifies and measures its "other material risks" defined as all material risks of the banking group that are not explicitly captured in the calculation of the common equity tier one capital ratio, the tier one capital ratio and the total capital ratio under the requirements set out in the document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated March 2013; and
- the bank determines an internal capital allocation for each identified and measured "other material risk".

IB. That, if the buffer ratio of the banking group is 2.5% or less, the bank must:

- according to the following table, limit the aggregate distributions of the bank's earnings to the percentage limit to distributions that corresponds to the banking group's buffer ratio:

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

## Conditions of Registration continued

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

For the purposes of this condition of registration, -

"buffer ratio", "distributions", and "earnings" have the same meaning as in Part 3 of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated March 2013.

This condition of registration applies on and after 1 January 2014.

2. That the banking group does not conduct any non-financial activities that in aggregate are material relative to its total activities. In this condition of registration, the meaning of "material" is based on generally accepted accounting practice.

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

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

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

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

- (a) all amounts must relate to on balance sheet items only, and must comply with generally accepted accounting practice; and
- (b) if products or assets of which an insurance business is comprised also contain a non-insurance component, the whole of such products or assets must be considered part of the insurance business.

For the purposes of this condition of registration, -

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

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

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

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

<sup>1</sup> This table uses the rating scales of Standard and Poors, Fitch Ratings and Moody's Investor Service. (Fitch Ratings' scale is identical to Standard and Poors).

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

For the purposes of this condition of registration, compliance with the rating-contingent connected exposure limit is determined in accordance with the Reserve Bank of New Zealand document entitled "Connected Exposures Policy" (BS8) dated March 2013.

5. That exposures to connected persons are not on more favourable terms (e.g. as relates to such matters as credit assessment, tenor, interest rates, amortisation schedules and requirement for collateral) than corresponding exposures to non-connected persons.
6. That the bank complies with the following corporate governance requirements:
  - (a) the board of the bank must have at least five directors;
  - (b) the majority of the board members must be non-executive directors;
  - (c) at least half of the board members must be independent directors;
  - (d) an alternate director;-
    - (i) for a non-executive director must be non-executive; and
    - (ii) for an independent director must be independent;
  - (e) at least half of the independent directors of the bank must be ordinarily resident in New Zealand;
  - (f) the chairperson of the board of the bank must be independent; and
  - (g) the bank's rules must not include any provision permitting a director, when exercising powers or performing duties as a director, to act other than in what he or she believes is the best interests of the society (i.e. the bank).

For the purposes of this condition of registration, "non-executive" and "independent" have the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated March 2011.

7. That no appointment of any director, chief executive officer, or executive who reports or is accountable directly to the chief executive officer, is made in respect of the bank unless:
  - (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
  - (b) the Reserve Bank has advised that it has no objection to that appointment.

### Conditions of Registration *continued*

8. That a person must not be appointed as chairperson of the board of the bank unless:
  - (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
  - (b) the Reserve Bank has advised that it has no objection to that appointment.
9. That the bank has a board audit committee, or other separate board committee covering audit matters, that meets the following requirements:
  - (a) the mandate of the committee must include: ensuring the integrity of the bank's financial controls, reporting systems and internal audit standards;
  - (b) the committee must have at least three members;
  - (c) every member of the committee must be a non-executive director of the bank;
  - (d) the majority of the members of the committee must be independent; and
  - (e) the chairperson of the committee must be independent and must not be the chairperson of the bank.

For the purposes of this condition of registration, "non-executive" and "independent" have the same meaning as in the Reserve Bank document entitled "Corporate Governance" (BS14) dated March 2011.

10. That a substantial proportion of the bank's business is conducted in and from New Zealand.
11. That the banking group complies with the following quantitative requirements for liquidity-risk management:
  - (a) the one-week mismatch ratio of the banking group is not less than zero per cent at the end of each business day;
  - (b) the one-month mismatch ratio of the banking group is not less than zero per cent at the end of each business day; and
  - (c) the one-year core funding ratio of the banking group is not less than 75 per cent at the end of each business day;

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

12. That the bank has an internal framework for liquidity risk management that is adequate in the bank's view for managing the bank's liquidity risk at a prudent level, and that, in particular:
  - (a) is clearly documented and communicated to all those in the organisation with responsibility for managing liquidity and liquidity risk;
  - (b) identifies responsibility for approval, oversight and implementation of the framework and policies for liquidity risk management;
  - (c) identifies the principal methods that the bank will use for measuring, monitoring and controlling liquidity risk; and
  - (d) considers the material sources of stress that the bank might face, and prepares the bank to manage stress through a contingency funding plan.

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

For the purposes of this condition -

"total assets" means all assets of the banking group plus any assets held by any SPV that are not included in the banking group's assets

"SPV" means a person -

- (a) to whom any member of the banking group has sold, assigned, or otherwise transferred any asset;
- (b) who has granted, or may grant, a security interest in its assets for the benefit of any holder of any covered bond; and
- (c) who carries on no other business except for that necessary or incidental to guarantee the obligations of any member of the banking group under a covered bond:

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

14. That -
  - (a) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the notification threshold, and does not meet the non-objection threshold, unless:
    - (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination and at least 10 working days have passed; and
    - (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011; and
  - (b) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the non-objection threshold unless:
    - (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination;
    - (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011; and
    - (iii) the Reserve Bank has given the bank a notice of non-objection to the significant acquisition or business combination.

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

In these conditions of registration, -

"banking group" means Southland Building Society's financial reporting group (as defined in section 2(1) of the Financial Reporting Act 1993);

"generally accepted accounting practice" has the same meaning as in section 2 of the Financial Reporting Act 1993.



# Disclosure Statement for the year ended 31 March 2013

## Conditions of Registration *continued*

### Changes in Conditions of Registration

The following changes have been made to the Bank's conditions of registration during the period since the reporting date of the previous Disclosure Statement:

Conditions 1, 1A and 1B have been updated to reference to the latest version of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A).

### Directors' Statement

The directors of Southland Building Society (the "Bank") state that each director of the Bank believes, after due enquiry, that:

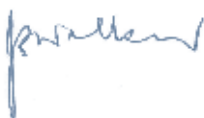
1. As at the date on which the Disclosure Statement is signed:
  - (a) the Disclosure Statement contains all the information that is required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2013; and
  - (b) the Disclosure Statement is not false or misleading;
2. Each director of the Bank believes, after due enquiry, that during the year ending 31 March 2013:
  - (a) Southland Building Society has complied with the conditions of registration; and
  - (b) credit exposures to connected persons were not contrary to the interests of the Banking Group; and
  - (c) the Bank had systems in place to monitor and control adequately the Banking Group's material risks, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk, and other business risks, and that those systems were being properly applied.

This Disclosure Statement is dated 4 June 2013 and has been signed by or on behalf of all the directors.

JF Ward  
(Chairman)



JB Walker  
(Deputy Chairman)



RL Smith  
(Group Managing Director /  
Chief Executive Officer)



KJ Ball



GJ Mulvey



JJ Grant



FE Spencer



AG Neill





# Historical Summary of Financial Statements

All in \$'000's

## Income Statements

BANKING GROUP					
	Year ended 31 Mar 2013	Year ended 31 Mar 2012	Year ended 31 Mar 2011	Year ended 31 Mar 2010	Year ended 31 Mar 2009
Interest income	176,928	185,200	182,286	172,040	237,227
Interest expense	11,497	13,518	16,037	16,897	39,421
Dividends on redeemable shares	93,991	101,726	102,565	95,598	136,808
	105,488	115,244	118,602	112,495	176,229
<b>Net interest income</b>	<b>71,440</b>	<b>69,956</b>	<b>63,684</b>	<b>59,545</b>	<b>60,998</b>
Other income	20,114	18,611	18,235	18,629	12,871
<b>Total operating income</b>	<b>91,554</b>	<b>88,567</b>	<b>81,919</b>	<b>78,174</b>	<b>73,869</b>
Operating expenses	53,343	48,928	47,554	43,068	42,922
Provision for credit impairment	17,304	21,983	17,057	15,727	12,446
<b>Operating surplus</b>	<b>20,907</b>	<b>17,656</b>	<b>17,308</b>	<b>19,379</b>	<b>18,501</b>
Net gain/(loss) from financial instruments designated at fair value	(1,078)	(588)	5,117	980	(2,404)
Revaluation of property	(46)	-	-	200	60
Revaluation of investment properties	(61)	-	(88)	-	-
<b>Surplus before income tax</b>	<b>19,722</b>	<b>17,068</b>	<b>22,337</b>	<b>20,559</b>	<b>16,157</b>
Less income taxation expense	5,383	5,303	8,087	5,522	4,100
<b>Net surplus</b>	<b>14,339</b>	<b>11,765</b>	<b>14,250</b>	<b>15,037</b>	<b>12,057</b>
<b>Attributable to:</b>					
Members' interests	11,733	9,220	11,761	12,723	10,986
Non-controlling interests	2,606	2,545	2,489	2,314	1,071
	<b>14,339</b>	<b>11,765</b>	<b>14,250</b>	<b>15,037</b>	<b>12,057</b>

## Significant Statement of Financial Position Items

BANKING GROUP					
	As at 31 Mar 2013	As at 31 Mar 2012	As at 31 Mar 2011	As at 31 Mar 2010	As at 31 Mar 2009
Total assets	2,829,669	2,841,896	2,813,833	2,627,905	2,541,177
Individually impaired assets	23,758	41,210	38,342	29,907	21,848
Total liabilities	2,598,079	2,626,535	2,611,793	2,450,241	2,385,597
Equity	231,590	215,361	202,040	177,664	155,580
<b>Regulatory capital</b>					
Tier one capital	221,981	215,088	205,191	176,797	162,927
Total capital	238,724	246,562	247,803	228,334	205,949
Tier one capital expressed as a percentage of total risk weighted assets	13.34%	12.52%	11.26%	10.34%	9.85%
Total capital expressed as a percentage of total risk weighted assets	14.34%	14.35%	13.60%	13.35%	12.46%

The amounts included in this summary have been extracted from the audited consolidated financial statements of the Banking Group.

The Banking Group adopted the Basel III "standardised approach" to calculate regulatory capital requirements from 1 January 2013. Prior comparative periods were calculated under the Basel II methodology.

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## Income Statements for the year ended 31 March 2013

All in \$'000's

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
Interest income	(4)	176,928	185,200	157,952	164,203
Interest expense		11,497	13,518	10,978	11,694
Dividends on redeemable shares		93,991	101,726	94,159	101,889
	(5)	105,488	115,244	105,137	113,583
<b>Net interest income</b>		<b>71,440</b>	<b>69,956</b>	<b>52,815</b>	<b>50,620</b>
Other income	(4)	20,114	18,611	5,385	5,955
<b>Total operating income</b>		<b>91,554</b>	<b>88,567</b>	<b>58,200</b>	<b>56,575</b>
Operating expenses	(5)	53,343	48,928	37,340	34,673
Provision for credit impairment	(12)	17,304	21,983	12,977	17,927
<b>Operating surplus</b>		<b>20,907</b>	<b>17,656</b>	<b>7,883</b>	<b>3,975</b>
Dividends from subsidiaries		-	-	6,795	5,486
Net gain/(loss) from financial instruments designated at fair value	(6)	(1,078)	(588)	(1,197)	(764)
Revaluation of property		(46)	-	-	-
Revaluation of investment properties		(61)	-	(61)	-
Subvention payment		-	-	-	(19)
<b>Surplus before income tax</b>		<b>19,722</b>	<b>17,068</b>	<b>13,420</b>	<b>8,678</b>
Less income tax expense	(7)	5,383	5,303	1,855	1,116
<b>Net surplus</b>		<b>14,339</b>	<b>11,765</b>	<b>11,565</b>	<b>7,562</b>
<b>Attributable to:</b>					
Members' interests		11,733	9,220	11,565	7,562
Non-controlling interests		2,606	2,545	-	-
		<b>14,339</b>	<b>11,765</b>	<b>11,565</b>	<b>7,562</b>

## Statements of Comprehensive Income for the year ended 31 March 2013

All in \$'000's

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
<b>Net surplus for the year</b>		<b>14,339</b>	<b>11,765</b>	<b>11,565</b>	<b>7,562</b>
<b>Other comprehensive income</b>					
Net change in property, plant and equipment reserve, net of tax		(371)	27	111	106
Net change in available for sale asset reserve, net of tax		2,584	1,000	2,480	1,023
Net change in cash flow hedging reserve, net of tax		2,641	2,772	2,258	2,168
<b>Other comprehensive income for the year, net of tax</b>		<b>4,854</b>	<b>3,799</b>	<b>4,849</b>	<b>3,297</b>
<b>Total comprehensive income for the year</b>		<b>19,193</b>	<b>15,564</b>	<b>16,414</b>	<b>10,859</b>
<b>Attributable to:</b>					
Members' interests		16,457	12,853	16,414	10,859
Non-controlling interests		2,736	2,711	-	-
		<b>19,193</b>	<b>15,564</b>	<b>16,414</b>	<b>10,859</b>

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

# Statements of Changes in Equity for the year ended 31 March 2013

All in \$'000's

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
<b>Revaluation reserve - property, plant and equipment</b>					
Balance at beginning of the year		825	798	343	237
Other comprehensive income for the year		(371)	27	111	106
Balance at end of the year		454	825	454	343
<b>Revaluation reserve - available for sale assets</b>					
Balance at beginning of the year		2,240	1,236	2,300	1,277
Other comprehensive income for the year		2,563	1,004	2,480	1,023
Balance at end of the year		4,803	2,240	4,780	2,300
<b>Revaluation reserve - cash flow hedging</b>					
Balance at beginning of the year		(5,258)	(7,859)	(4,899)	(7,067)
Other comprehensive income for the year		2,532	2,601	2,258	2,168
Balance at end of the year		(2,726)	(5,258)	(2,641)	(4,899)
<b>Retained earnings</b>					
Balance at beginning of the year		210,667	201,447	196,145	188,583
Net surplus for the year		11,733	9,220	11,565	7,562
Balance at end of the year		222,400	210,667	207,710	196,145
<b>Total equity attributable to members' interests</b>		<b>224,931</b>	<b>208,474</b>	<b>210,303</b>	<b>193,889</b>
<b>Non-controlling interests</b>					
Balance at beginning of the year		6,887	6,418	-	-
Net surplus for the year		2,606	2,545	-	-
Other comprehensive income for the year		130	167	-	-
Dividends		(2,964)	(2,243)	-	-
Balance at end of the year		6,659	6,887	-	-
<b>Total equity at end of the year</b>		<b>231,590</b>	<b>215,361</b>	<b>210,303</b>	<b>193,889</b>
<b>Represented by:</b>					
Equity at beginning of the year		215,361	202,040	193,889	183,030
Net surplus for the year		14,339	11,765	11,565	7,562
Other comprehensive income for the year		4,854	3,799	4,849	3,297
Total comprehensive income for the year		19,193	15,564	16,414	10,859
Dividends		(2,964)	(2,243)	-	-
<b>Total equity at end of the year</b>	(22)	<b>231,590</b>	<b>215,361</b>	<b>210,303</b>	<b>193,889</b>

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

# Statements of Financial Position as at 31 March 2013

All in \$'000's

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
<b>Assets</b>					
Cash on hand and at bank		21,801	22,474	18,790	17,413
Funds with financial institutions	(8)	144,490	90,980	137,241	85,825
Investment securities	(9)	400,233	265,733	397,595	262,848
Derivative financial instruments	(10)	2,396	2,789	2,614	3,756
Current tax assets		1,604	-	2,641	1,143
Advances to customers	(11)	2,225,753	2,425,723	2,116,771	2,262,510
Loans to subsidiaries	(15)	-	-	87,808	89,871
Investments in subsidiaries	(15)	-	-	15,180	15,180
Other assets	(16)	2,454	2,031	2,025	4,572
Investment properties		3,330	3,391	3,330	3,391
Property, plant and equipment	(17)	19,004	18,824	9,208	8,200
Intangible assets	(18)	3,320	2,466	1,738	863
Deferred tax	(19)	5,284	7,485	6,975	9,182
		<b>2,829,669</b>	<b>2,841,896</b>	<b>2,801,916</b>	<b>2,764,754</b>
<b>Liabilities</b>					
Redeemable shares	(24)	2,180,292	2,234,814	2,185,716	2,239,547
Deposits from customers	(24)	251,099	253,500	251,099	253,500
Due to other financial institutions	(24)	80,295	-	80,295	-
Derivative financial instruments	(10)	6,617	10,206	6,617	10,259
Current tax liabilities		-	93	-	-
Other borrowings		-	52,092	-	-
Other liabilities	(20)	18,544	14,588	6,654	6,317
Subordinated redeemable shares	(21)	61,232	61,242	61,232	61,242
		<b>2,598,079</b>	<b>2,626,535</b>	<b>2,591,613</b>	<b>2,570,865</b>
<b>Net assets</b>		<b>231,590</b>	<b>215,361</b>	<b>210,303</b>	<b>193,889</b>
<b>Equity</b>	(22)				
Reserves		2,531	(2,193)	2,593	(2,256)
Retained earnings		222,400	210,667	207,710	196,145
Attributable to members of the society		224,931	208,474	210,303	193,889
Attributable to non-controlling interests		6,659	6,887	-	-
		<b>231,590</b>	<b>215,361</b>	<b>210,303</b>	<b>193,889</b>
Total interest earning and discount bearing assets		2,792,277	2,804,910	2,758,205	2,718,467
Total interest and discount bearing liabilities		2,572,918	2,601,648	2,578,342	2,554,289

For and on behalf of the Board of Directors:



Chairman  
JFWard



Deputy Chairman  
JB Walker

4 June 2013

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

# Statements of Cash Flows for the year ended 31 March 2013

All in \$'000's

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
<b>Cash flows from operating activities</b>					
Interest received		173,108	179,182	157,027	161,563
Fees and other income		25,770	24,855	6,258	7,524
Dividends received		74	50	8,947	5,326
Interest paid		(11,302)	(14,130)	(10,783)	(12,306)
Dividends paid on redeemable shares		(91,583)	(103,259)	(91,744)	(103,428)
Operating expenses		(48,765)	(50,579)	(35,020)	(33,920)
Income taxes received/(paid)		(6,592)	(6,399)	(2,996)	(3,407)
Net cash flows from operating activities before changes in operating assets and liabilities		40,710	29,720	31,689	21,352
<b>Net changes in operating assets and liabilities</b>					
Change in advances		182,018	136,413	131,984	122,268
Change in shares and deposits from customers		(59,241)	80,458	(58,557)	80,580
Change in amounts due to other financial institutions		80,000	-	80,000	-
Change in other borrowings		(52,092)	(55,004)	-	(41,385)
Change in subordinated redeemable shares		-	-	-	-
Change in cash held on behalf of Lifestages Mortgage Portfolio		-	(2,430)	-	(2,430)
<b>Net cash flows provided by/(used in) operating activities</b>	(23)	<b>191,395</b>	<b>189,157</b>	<b>185,116</b>	<b>180,385</b>
<b>Cash flows from investing activities</b>					
Change in investment securities		(129,310)	(142,792)	(129,675)	(142,534)
Change in loans to subsidiaries		-	-	2,063	4,967
Proceeds of property, plant and equipment		46	104	40	24
Purchase of property, plant and equipment		(3,200)	(2,185)	(2,779)	(1,404)
Purchase of intangible assets		(1,817)	(1,319)	(1,386)	(876)
<b>Net cash flows provided by/(used in) investing activities</b>		<b>(134,281)</b>	<b>(146,192)</b>	<b>(131,737)</b>	<b>(139,823)</b>
<b>Cash flows from financing activities</b>					
Dividends paid to non-controlling interests		(3,697)	(2,249)	-	-
<b>Net cash flows provided by/(used in) financing activities</b>		<b>(3,697)</b>	<b>(2,249)</b>	<b>-</b>	<b>-</b>
Net increase/(decrease) in cash held		53,417	40,716	53,379	40,562
Add opening cash and cash equivalents		111,569	70,853	101,413	60,851
<b>Closing cash and cash equivalents</b>		<b>164,986</b>	<b>111,569</b>	<b>154,792</b>	<b>101,413</b>
<b>Reconciliation of cash and cash equivalents</b>					
Cash on hand and at bank		21,801	22,474	18,790	17,413
Funds with financial institutions	(8)	144,490	90,980	137,241	85,825
Interest accrued on available for sale assets		(1,305)	(1,885)	(1,239)	(1,825)
		<b>164,986</b>	<b>111,569</b>	<b>154,792</b>	<b>101,413</b>

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

## I Statement of Accounting Policies

### (a) Basis of Preparation

Southland Building Society (SBS) was established in 1869, is incorporated under the Building Societies Act 1965, and is registered as a bank under the Reserve Bank of New Zealand Act 1989. The consolidated financial statements presented here are for the reporting entity of the Banking Group comprising SBS and its subsidiaries.

The financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 1993 and under New Zealand Generally Accepted Accounting Practice ("NZ GAAP"). They comply with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS") and other applicable Financial Reporting Standards, as appropriate for profit-oriented entities and the Registered Bank Disclosure Statement (New Zealand Incorporated Registered Banks) Order 2013. The financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB).

These financial statements were authorised for issue by the Board of Directors on 4 June 2013.

### (b) Presentation Currency and Rounding

The functional and presentation currency of the Banking Group is New Zealand dollars. All amounts contained in the financial statements are presented in thousands of New Zealand dollars, unless otherwise stated.

### (c) Standards Issued but not yet Effective

The following new standards and amendments to standards relevant to the Banking Group are not yet effective and have not yet been applied in preparing the financial statements. The Banking Group does not currently intend to apply any of these pronouncements until their effective date and is assessing the impact of NZ IFRS 9 on its financial statements. The adoption of the other standards will not have a material impact on the Banking Group's reported profit or financial position.

- NZ IFRS 7 Financial Instruments: Disclosures - will apply to the Banking Group from 1 April 2013.
- NZ IFRS 9 Financial Instruments - It is the intention of the IASB to replace IAS 39 with IFRS 9. This standard will apply to the Banking Group from 1 April 2015.
- NZ IFRS 10 Consolidated Financial Statements - will apply to the Banking Group from 1 April 2013.
- NZ IFRS 12 Disclosure of Interests in Other Entities - will apply to the Banking Group from 1 April 2013.
- NZ IFRS 13 Fair Value Measurement - will apply to the Banking Group from 1 April 2013.
- NZ IAS 1 Presentation of Financial Statements - Presentation of other comprehensive income - will apply to the Banking Group from 1 April 2013.

### (d) Measurement Base

The financial statements have been prepared on a going concern basis in accordance with historical cost concepts except that the following assets and liabilities are stated at their fair value: derivative financial instruments, certain financial assets and liabilities designated at fair value through profit or loss or as available for sale, and the revaluation of certain non-current assets.

### (e) Accounting Estimates

The preparation of the financial statements requires the use of management judgement, estimates and assumptions that affect reported amounts and the application of policies. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable. Actual results may differ from these estimates. For further discussion on judgements and estimates made by the Banking Group, in the process of applying its accounting policies, that have the most effect on the amounts recognised in the financial statements, refer to Note 2 - Critical Estimates and Judgements Used in Applying Accounting Policies.

### (f) Consolidation

The Banking Group financial statements consolidate SBS and the following entities:

- Fraser Properties Limited (wholly owned subsidiary) - owns SBS's head office building;
- Southsure Assurance Limited (80% owned subsidiary) - life insurance and related products;
- Finance Now Limited (71.5% owned subsidiary) - consumer credit and commercial finance;
- Funds Administration New Zealand Limited (57% owned subsidiary) - funds management products and financial advisory services;
- SBS Invercargill W Trust (in substance subsidiary) - special purpose vehicle holding securitised loans purchased from SBS;
- SBS Oreti Trust No 1 (in substance subsidiary) - special purpose vehicle holding securitised loans purchased from SBS; and
- SBS Oreti Trust No 2 (in substance subsidiary) - special purpose vehicle holding securitised loans purchased from SBS.

#### *Subsidiaries*

Subsidiaries are those entities over which the Banking Group has the power to govern the financial and operating policies so as to obtain benefits from their activities.

Where subsidiaries have been sold or acquired during the year, their operating results have been included to the date control ceases or from the date control is transferred to the Banking Group.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and the liabilities assumed are measured at their acquisition date fair values.

On consolidation, all significant inter-company transactions, balances and unrealised gains on transactions have been eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The accounting policies of the subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Parent, SBS.

#### *Special Purpose Entities*

SBS may invest in or establish special purpose entities to enable it to undertake specific types of transactions such as securitisation. Where SBS controls such vehicles, they are consolidated into the Banking Group's financial results.



## I Statement of Accounting Policies continued

### (g) Revenue and Expense Recognition

Revenue is recognised to the extent that it is probable that economic benefits will flow to the Banking Group and that revenue can be reliably measured. Expenses are recognised in the income statement on an accruals basis.

### (h) Interest Income and Interest Expense

Interest income and interest expense (including dividends on redeemable and subordinated redeemable shares) for all instruments measured at amortised cost are recognised in the income statement as they accrue, using the effective interest method. Interest income and interest expense for all instruments measured at fair value are recognised in the income statement on a daily accrual basis.

The effective interest method calculates the amortised cost of a financial asset or financial liability and allocates the interest income or expense, including any fees and directly related transaction costs that are an integral part of the effective interest rate over the expected life of the financial asset or liability. The application of the method has the effect of recognising income and expense evenly in proportion to the amount outstanding over the expected life of the financial asset or liability.

Loan commitment fees are deferred and recognised as an adjustment to the effective interest on the loan once drawn or immediately to the income statement for expired commitments.

Fees and commissions payable to brokers in respect of originating lending business, where these are direct and incremental costs related to the issue of a financial instrument, are included in interest income as part of the effective interest rate.

### (i) Fee and Commission Income

Fee and commission income integral to the effective yield of a financial asset or liability for all instruments measured at amortised cost is recognised as an adjustment to the effective interest calculation and included in net interest income.

Fee and commission income which relates to the execution of a significant act, for example maintaining and administering existing facilities is recognised at the time the services are provided and is recognised as income no later than when the loan is disbursed or the commitment to lend expires.

### (j) Net Gain/(Loss) from Financial Instruments Designated at Fair Value

Net gains/(losses) on financial instruments designated at fair value comprises fair value gains and losses from financial instruments designated at fair value through profit or loss.

Interest income and interest expense on all financial instruments designated at fair value through profit or loss is reported within interest income or interest expense and not included in the fair value of these instruments.

Provision for credit impairment on all financial instruments designated at fair value through profit or loss is reported within provision for credit impairment and not included in the fair value of these instruments.

### (k) Offsetting of Income and Expenses

Income and expenses are not offset unless required or permitted by an accounting standard. This generally arises in the following circumstances:

- where amounts are collected on behalf of third parties where the Banking Group is, in substance, acting as an agent only; or
- where costs are incurred on behalf of customers from whom the Banking Group is reimbursed.

### (l) Recognition and Derecognition of Financial Assets and Financial Liabilities

The Banking Group recognises, on its statement of financial position, loans and receivables, deposits and redeemable shares at origination date and all other financial assets and liabilities at trade date.

The Banking Group derecognises a financial asset from its statement of financial position when, and only when, (i) the contractual rights to the cash flows from the financial asset expire, or (ii) the Banking Group has transferred all or substantially all of the risks and rewards of ownership of the financial asset and no longer controls the asset. The Banking Group derecognises a financial liability from its statement of financial position, when and only when, it is extinguished.

### (m) Fair Value Measurement

The determination of fair values of financial assets and financial liabilities are based on quoted market prices or dealer price quotations for financial instruments traded in active markets, or by using valuation techniques. When entering into a transaction, the financial instrument is recognised initially at the transaction price, which is the best indicator of fair value and subsequently at valuation.

Valuation techniques include the discounted cash flow method and comparison to similar instruments for which market observable prices exist. The Banking Group uses widely recognised valuation models however some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions.

The value produced by a model or other valuation technique is adjusted to allow for a number of factors as appropriate, because valuation techniques may not appropriately reflect all factors market participants take into account when entering a transaction. Valuation adjustments are recorded to allow for liquidity risks as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments at fair value on the statement of financial position.

### (n) Financial Instruments

The Banking Group classifies its financial instruments into the following categories at initial recognition: Financial assets at fair value through profit or loss, available for sale financial assets, loans and receivables, held to maturity financial assets, financial liabilities at fair value through profit or loss, and other financial liabilities. Designation of financial assets and liabilities into instrument categories is determined by the business purpose of the financial instruments, policies and practices for their management, their relationship with other instruments and the reporting costs and benefits associated with each designation.

#### *Financial Assets at Fair Value through Profit or Loss*

Financial assets at fair value through profit or loss are financial assets acquired principally for the purpose of selling in the short term (held for trading), financial assets designated as fair value through profit or loss, and derivative financial instruments which are not designated as a cash flow hedge.

The Banking Group may designate financial assets at fair value through profit or loss when doing so significantly reduces measurement or recognition inconsistencies (accounting mismatch) that would arise from measuring assets and liabilities or recognising the gains and losses on them on different bases. Under this criterion the Banking Group has designated certain advances to customers as fair value through profit or loss. Where derivative financial instruments have been transacted to risk manage these, an accounting inconsistency would arise if such advances were accounted on an

## I Statement of Accounting Policies *continued*

amortised cost basis, as the derivatives are measured at fair value with movements in fair value recognised in the income statement. By designating these advances at fair value through profit or loss, fair value movements on the instrument will substantially offset the fair value movements on risk management derivatives in the income statement.

Other financial assets may be classified at fair value through profit or loss where they are part of a group of financial assets that are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis.

Once a financial asset has been designated at fair value through profit or loss upon initial recognition, the Banking Group cannot subsequently change the designation. Financial assets at fair value through profit or loss are measured at fair value with realised and unrealised gains and losses included in the income statement. Assets classified in this category include certain advances to customers, certain investment securities, and derivative financial assets.

### *Available for Sale Financial Assets*

Available for sale financial assets are non-derivative financial assets that are designated as available for sale. The Banking Group may designate financial assets as available for sale when they may be sold prior to maturity in response to needs for liquidity or due to changes in interest rates.

Available for sale financial assets are initially recognised at fair value plus transaction costs that are directly attributable to acquisition and are subsequently carried at fair value. Gains and losses (not attributable to accrued interest) arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity, until the financial asset is derecognised or impaired. At this time, the cumulative gain or loss previously recognised in equity is recognised in the income statement. Assets classified in this category include certain funds with financial institutions and investment securities.

### *Loans and Receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, not available for sale, and not designated as fair value through profit or loss. Loans and receivables are initially recognised at fair value including direct and incremental transaction costs and are subsequently measured at amortised cost using the effective interest method, less any impairment loss.

Assets classified in this category include cash on hand and at bank, investment securities which are not managed on a fair value basis, advances to customers other than those classified at fair value through profit or loss, and loans to subsidiaries.

### *Held to Maturity Financial Assets*

Held to maturity financial assets are non-derivative financial assets where management has the intention and ability to hold to maturity. Held to maturity financial assets are initially recognised at fair value including direct and incremental transaction costs, and subsequently measured at amortised cost using the effective interest rate method. The Banking Group has not classified any financial assets as held to maturity.

### *Other Financial Liabilities*

Other financial liabilities includes all financial liabilities other than those classified at fair value through profit or loss. Other financial liabilities are initially recognised at fair value including direct and incremental transaction costs, and subsequently measured at amortised cost. Liabilities classified in this category include redeemable shares, deposits from customers, due to other financial institutions, current tax liabilities and subordinated redeemable shares.

## (o) Derivative Financial Instruments held for Risk Management Purposes

Derivative financial instruments are contracts whose value is derived from changes in one or more underlying financial instruments or indices. They include swaps, options and combinations of these instruments.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently measured at their fair value. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Banking Group designates certain derivatives as hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge).

Hedge accounting is used for derivatives designated in this way, provided certain criteria are met.

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

### *Cash Flow Hedge*

A fair value gain or loss associated with the effective portion of a derivative designated as a cash flow hedge is recognised initially in the cash flow hedging reserve. The ineffective portion of a fair value gain or loss is recognised immediately in the income statement. When the transaction or item that the derivative is hedging (including cash flows from the transaction that were forecast when the derivative was effected) affects the income or expense then the associated gain or loss on the hedging derivative is simultaneously transferred from the cash flow hedging reserve to the corresponding income or expenses item in the income statement.

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

### *Derivative Financial Instruments at Fair Value through Profit or Loss*

Certain derivative financial instruments that do not meet the criteria for hedge accounting under NZ IAS 39 are classified as at fair value through profit or loss. Changes in the fair value are reflected in the income statement immediately.

The movement in the fair value of derivative financial instruments is included in the income statement as 'net gain/(loss) from financial instruments designated at fair value'.

## I Statement of Accounting Policies continued

### (p) Asset Quality

#### *Credit Assessment*

All advances and loans are subject to regular scrutiny of credit risk.

The Banking Group has classified its impaired assets into the following categories:

#### *Impaired assets*

Impaired assets are credit exposures where a credit event has occurred and for which it is probable the Banking Group will not be able to collect all amounts owing in terms of the contract and includes:

- advances and loans that are not contractually past due but where there is insufficient security to cover principal outstanding and where recovery is doubtful;
- advances and loans which are past due with insufficient security to cover principal and arrears of interest;
- restructured advances and loans where the interest rate charged is below that of the Banking Group's average cost of funds.

An individual provision is raised to cover the expected loss, where full recovery is doubtful.

#### *Restructured assets*

Restructured assets are defined as advances and loans on which the original contractual terms have been concessionally modified due to the financial difficulties of borrowers, and on which interest continues to be accrued at a rate which is equal to or greater than the Banking Group's average cost of funds at the date of restructuring.

#### *Real estate or other assets acquired through security enforcement*

Real estate or other assets acquired through security enforcement are those assets which are legally owned by the Banking Group as a result of enforcing security.

#### *Past due assets*

Advances and loans are designated as past due assets where a counterparty has failed to make a payment when contractually due and which are not impaired assets.

### (q) Impairment of Financial Assets

Advances and loans are regularly reviewed for impairment loss. Credit impairment provisions are raised for exposures that are known to be impaired. Advances and loans are impaired and impairment losses incurred if there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the advance or loan and that loss event (or events) has had a reliably measurable impact on the estimated future cash flows of the individual advance or loan or the collective portfolio of advances and loans.

Impairment is assessed initially for assets that are individually significant (or on a portfolio basis for small value loans), and then on a collective basis for those exposures not individually known to be impaired.

For those exposures that are assessed collectively, these are placed in pools of similar assets with similar risk characteristics. The required provision is estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the collective pool. The historical loss experience is adjusted based on current observable data.

The estimated individual impairment loss is measured as the difference between the asset's carrying amount and the estimated future cash flows discounted to their present value at the original effective interest rate. As this discount unwinds during the period between recognition of impairment and recovery of the written down amount, it is recognised in the income statement. The process of estimating the amount and timing of cash flows involves considerable management judgement. These judgements are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The provision for credit impairment (individual and collective) is deducted from advances and loans in the statement of financial position and the movement in the provision for the reporting period is reflected in the income statement as 'provision for credit impairment'.

When an advance or loan is uncollectible, it is written-off against the related provision for impairment. Subsequent recoveries of amounts previously written-off are taken to the income statement.

Where impairment losses recognised in previous periods are subsequently decreased or no longer exist, such impairments are reversed in the income statement.

### (r) Investment Properties

Investment properties are properties which are held either to earn rental income or for capital appreciation or both. Investment property has been acquired through the enforcement of security over advances and loans.

Investment property is measured initially at cost, including transaction costs.

After initial recognition, investment properties are measured annually at fair value by an independent valuer. The fair values are based on market values, being the estimated amount for which a property could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's length transaction at the date of valuation.

Any gain or loss arising from a change in fair value is recognised in the income statement. There is no depreciation on investment properties.

Rental income from investment property is accounted for as described in the accounting policy for operating leases.

### (s) Property, Plant and Equipment

#### *Asset Recognition*

Land and buildings are initially recognised at cost and are subsequently valued by independent registered valuers. Land and buildings are carried at the revalued amount less accumulated depreciation and impairment losses. Items of property, plant and equipment are carried at cost less accumulated depreciation and impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of internally developed assets includes the cost of materials and direct labour; and any other costs directly attributable to bringing the asset to a working condition for its intended use.

## I Statement of Accounting Policies continued

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the period the item is derecognised.

### *Revaluation*

Land and buildings are carried at the revalued amount which is the market value at the date of the revaluation less any subsequent accumulated depreciation of buildings and accumulated impairment losses.

Where the land and building is revalued, any revaluation surplus net of tax is credited to the asset revaluation reserve included in equity unless it reverses a revaluation decrease of the same asset previously recognised in the income statement. Any revaluation deficit is recognised in the income statement unless it directly offsets a previous surplus of the same asset recognised in the asset revaluation reserve. Any accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Upon disposal, any revaluation reserve relating to a particular asset being disposed is transferred to retained earnings.

Valuations of land and buildings are carried out annually, at market value.

### *Depreciation*

Depreciation is provided in the financial statements on all property, plant and equipment other than land, on a basis which will write down the net cost or revalued amount of each item of property, plant and equipment over its expected useful life on a straight line basis.

The estimated useful lives are:

	Useful Life
Buildings	50 years
Building Alterations	3 - 11 years
Computer Equipment	2 - 5 years
Other Assets	2 - 5 years

At each reporting date, the carrying amounts of property, plant and equipment are reviewed for indications of impairment in light of commercial and technological developments. If any such indication exists, the recoverable amount of the assets are estimated and compared against the existing carrying value. Where the asset's existing carrying value exceeds its recoverable amount the difference is charged to the income statement. An impairment loss recognised in prior periods may be reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

## (t) Intangible Assets

### *Goodwill*

Goodwill arising on the acquisition of subsidiary shares represents the excess of the cost of acquisition over the fair value of the Banking Group's share of the net identifiable assets acquired, at the date of acquisition. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed annually for impairment or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

### *Software*

Software comprises acquired and internally developed computer software and is amortised over its expected useful life to the Banking Group. The period of amortisation is between 1 and 3 years. At each reporting date, the software assets are reviewed for impairment against impairment indicators. If any indication of impairment exists, the recoverable amount of the assets are estimated and compared against the existing carrying value. Where the existing carrying value exceeds the recoverable amount, the difference is charged to the income statement. Costs incurred in planning or evaluating software proposals, or in maintaining systems after implementation, are not capitalised.

## (u) Redeemable Shares, Deposits and Subordinated Redeemable Shares

Redeemable shares, deposits and subordinated redeemable shares are recorded in the statement of financial position inclusive of accrued interest. Redeemable shares and subordinated redeemable shares are considered to be compound instruments. Interest income on deposits and dividends on redeemable and subordinated redeemable shares are recorded in the income statement on an accruals basis using the effective interest method.

## (v) Repurchase Agreements

Securities sold under repurchase agreements are retained in the financial statements when substantially all the risks and rewards of ownership remain with the Banking Group, and counterparty liability is disclosed under the classification of due to other financial institutions or other liabilities, depending on the term of the agreement and the counterparty.

The difference between the sale price and the repurchase price is amortised over the life of the repurchase agreement and charged to interest expense in the income statement.

## (w) Operating Leases

### *Leases as lessee*

The leases entered in to by the Banking Group are primarily operating leases. Operating leases are recognised as an expense on a systematic basis over the lease term.

### *Leases as lessor*

Operating lease rentals are included in the income statement on a systematic basis over the lease term. Gross operating lease income comprises amounts received under the lease contracts. Operating lease assets are stated at market value and are included as property, plant and equipment or investment properties.

## (x) Income Tax

### *Income Tax Expense*

Income tax expense for the year comprises current and deferred tax. It is recognised in the income statement as tax expense, except when it relates to items credited directly to equity, in which case it is recorded in equity.

## I Statement of Accounting Policies continued

### *Current Tax*

Current tax is the expected tax payable on taxable income for the year, based on tax rates (and tax laws) which are enacted or substantively enacted by the reporting date and including any adjustment for tax payable in previous periods. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

### *Deferred Tax*

Deferred tax is accounted for using the balance sheet method. Deferred tax arises by providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes 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 period(s) when the asset or liability giving rise to them are realised or settled, based on 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 Banking Group, at the reporting date, recovers or settles the carrying amount of its assets and liabilities.

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.

### (y) **Employee Benefits**

The amounts expected to be paid in respect of employee's entitlements to annual leave are accrued at expected salary rates. Liability for long service leave is calculated and accrued for in respect of all applicable employees using an actuarial valuation.

### (z) **Goods and Services Tax**

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

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the IRD is included as 'other assets' or 'other liabilities' in the statement of financial position.

Cash flows are included in the cash flow statement on a net basis. The GST components of cash flows arising from investing and financing activities, which are recoverable from, or payable to, the IRD are classified as operating cash flows.

### (aa) **Offsetting of Assets and Liabilities**

Assets and liabilities are offset and the net amount reported in the statement of financial position only where:

- There is a current enforceable legal right to offset the asset and liability; and
- There is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

### (ab) **Contingent Liabilities**

Liabilities are no longer contingent, and are recognised on the statement of financial position, when the following requirements are met:

- The transaction is probable in that a contingency is likely to occur; and
- The contingency can be reasonably estimated.

Further disclosure is made within Note 25 - Contingent Liabilities and Credit Related Commitments, where the above requirements are not met but there is a possible obligation that is higher than remote. Specific details are provided together with an estimate of the range or a statement that such an estimate is not possible.

### (ac) **Statement of Cash Flows**

#### *Basis of Preparation*

The statement of cash flows has been prepared using the direct approach modified by the netting of certain items as disclosed below.

#### *Cash and Cash Equivalents*

Cash and cash equivalents reflect the balance of cash and liquid assets used in the day to day cash management of the Banking Group, which are unconditionally convertible at the Banking Group's option within three months.

#### *Netting of Cash Flows*

Certain cash flows have been netted in order to provide more meaningful disclosure, as many of the cash flows are received and disbursed on behalf of customers and reflect the activities of the customers rather than those of the Banking Group. These include customer loans and advances, customer shares and deposits and parent company funding.

### (ad) **Ranking of Securities**

Deposits rank equally amongst themselves and equally with other unsecured creditors and behind creditors given priority by law. Redeemable shares rank equally amongst themselves and behind deposits, unsecured creditors and those creditors given priority by law. Subordinated redeemable shares rank equally amongst themselves and behind redeemable shares, deposits, unsecured creditors and those creditors given priority by law.

### (ae) **Lifestages Superannuation Scheme**

SBS has entered into a trust deed made between SBS and Trustees Executors Limited as Trustee of a registered superannuation scheme known as the Lifestages Superannuation Scheme (previously known as Lifestages Capital Stable Portfolio). Under a Deed of Novation dated 31 March 2007, SBS novated its rights and obligations under this trust deed to Funds Administration New Zealand Limited (FANZ). From this date, FANZ is the founder and promoter of the Lifestages Superannuation Scheme. SBS accepts investments made through SBS's branch network. The majority of the funds invested in the Lifestages Superannuation Scheme are invested with or managed by SBS. The Lifestages Superannuation Scheme funds that are invested with SBS are included in the statements of financial position as deposits. FANZ is the investment and administration manager of the Lifestages Superannuation Scheme.

## I Statement of Accounting Policies continued

### (af) Lifestages Portfolio Funds

FANZ has entered into a trust deed made between FANZ and Trustee Executors Limited as Trustee of six unit trusts registered under the Unit Trusts Act 1960, known as Lifestages Corporate Bond Portfolio (previously known as the Lifestages Mortgage Distributing Portfolio), Lifestages Income Portfolio (previously known as the Lifestages Mortgage Non-Distributing Portfolio), Lifestages Australasian Equity Portfolio, Lifestages World Equity Portfolio, Lifestages World Bond Portfolio and the Lifestages Deposit Portfolio. FANZ is the issuer and manager of the above Portfolios. The fixed interest asset allocations of the Lifestages Portfolio funds have investments invested with SBS.

The Lifestages Portfolio funds that are invested with SBS are included in the statements of financial position as deposits.

### (ag) Lifestages KiwiSaver Scheme

The Lifestages KiwiSaver Scheme was established by trust deed on 1 June 2007 and is a registered KiwiSaver scheme under the KiwiSaver Act 2006. FANZ & SBS are the "Promoter" of the scheme. FANZ is also the investment and administration manager.

The majority of the fixed interest portion of the investments of this scheme are invested with or managed by SBS. The Lifestages KiwiSaver Scheme funds that are invested with SBS are included in the statements of financial position as deposits.

### (ah) Loan Securitisation

SBS sells its interest in certain loans (principally housing mortgage loans) to a trust known as the SBS Invercargill W Trust by way of an equitable assignment. At the time of the sale all legal, equitable and beneficial interests in the mortgages are transferred to the purchaser. SBS consolidates the financial statements of SBS Invercargill W Trust within the Parent on the basis that SBS retains some of the risks and rewards of ownership through the provision of a subordinated loan. The subordinated loan has been in place since September 2007 and removes the need to purchase lenders mortgage insurance on loans assigned to the Trust.

The SBS Invercargill W Trust also sells its interest in certain loans (principally housing mortgage loans) to a trust known as the SBS Oreti Trust No. 2 by way of an equitable assignment. At the time of the sale all legal, equitable and beneficial interests in the mortgages are transferred to the purchaser. The SBS Oreti Trust No. 2 issues residential mortgage backed securities that qualify as acceptable collateral under the RBNZ liquidity management arrangements. SBS consolidates the financial statements of the SBS Oreti Trust No. 2 within the Parent on the basis that SBS retains a continuing involvement in the transferred assets by holding the securities issued by the trust.

The SBS Invercargill W Trust also has previously sold its interest in certain loans (principally housing mortgage loans) to a trust known as the SBS Oreti Trust No. 1 by way of an equitable assignment. At the time of the sale all legal, equitable and beneficial interests in the mortgages were transferred to the purchaser. The financial statements of SBS Oreti Trust No. 1 were consolidated at a Banking Group level. The SBS Oreti Trust No. 1 is currently being wound up.

SBS is the manager and servicer of mortgages assigned to the SBS Invercargill W Trust, the SBS Oreti Trust No. 1, and the SBS Oreti Trust No. 2. SBS receives a fee for providing these management services. This fee is recognised when earned.

### (ai) Comparative Data

To ensure consistency with the current period, comparative figures have been restated where appropriate.

### (aj) Changes in Accounting Policies and Estimates

There have been no changes in accounting policies and all accounting policies adopted are consistent with those used in previous periods.

## 2 Critical Estimates and Judgements Used in Applying Accounting Policies

These financial statements are prepared in accordance with stated accounting policies which are based on New Zealand equivalents of International Financial Reporting Standards ('NZ IFRS') and other authoritative accounting pronouncements. Notwithstanding the existence of relevant accounting standards, there are a number of critical accounting treatments which include complex or subjective judgements and estimates that may affect the reported amounts of assets and liabilities in the financial statements. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

An explanation of the judgements and estimates made by the Banking Group in the process of applying its accounting policies, that have the most significant effect on the amounts recognised in the financial statements are set out below.

### *Credit Loss Provisioning*

Provisions are raised for losses on exposures that are known to be impaired. The estimates of the cash flows on impaired exposures are then discounted to their present value. As this discount unwinds, there is a resulting recognition of a reduced specific provision and interest in the income statement during the period between recognition of impairment and recovery of the written down amount.

Exposures found not to be impaired are placed into pools of similar assets with similar risk characteristics to be collectively assessed for losses that have been incurred, but not yet identified. The required provision is estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the collective pool. The historical loss experience is adjusted based on current observable data. This may include data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Banking Group.

At 31 March 2013 the Banking Group's total provision for credit impairment was \$24.3 million (31 March 2012 \$29.6 million) representing 1.1% of total net loans and advances (31 March 2012 1.2%). The provisions represent provisions against individual loans and collective provisions.

Management regularly reviews and adjusts the estimates and methodologies as improved analysis becomes available. Changes in these assumptions and methodologies could have a direct impact on the level of credit provision and credit impairment charge recorded in the financial statements.

### *Fair Value of Derivatives*

The Banking Group enters derivative agreements to hedge its interest rate risk, credit risk and other exposures relating to non-trading positions. The derivative instruments used to hedge the Banking Group's exposures include:



### 2 Critical Estimates and Judgements Used in Applying Accounting Policies *continued*

- swaps;
- options; and
- combinations of the above instruments.

The Banking Group enters into derivatives for risk management purposes.

Derivatives which are entered into as part of the Banking Group's interest rate risk management strategies are measured at fair value, with any changes in fair value recognised in the income statement. The fair value of all derivatives are based on quoted market prices.

#### *Hedge Accounting*

A hedging instrument is a designated derivative, the changes in fair value or cash flows of which are expected to offset changes in the fair value or cash flows of a designated hedged item. A hedged item is an asset, liability, firm commitment or highly probable forecast transaction that exposes the Banking Group to risk of changes in fair value or cash flows, and that is designated as being hedged. The Banking Group hedges a portion of its floating rate risk in the funding and lending books.

For a relationship to qualify for hedge accounting, a number of criteria must be met including:

- the hedging relationship must be formally designated and documented at inception of the hedge;
- effectiveness testing must be carried out to ensure the hedge is effective consistent with the originally documented risk management strategy; and
- the instruments must involve a party external to the Banking Group.

Judgement is required by management in selecting and designating hedging relationships and assessing hedge effectiveness. NZ IAS 39 does not specify a single method for assessing hedge effectiveness. The Banking Group adopts the hypothetical derivative approach to determine hedge effectiveness. Hedge ineffectiveness can arise for a number of reasons, and whilst a hedge may pass the effectiveness tests it may not be perfectly effective, thus creating volatility within the income statement through recognition of this ineffectiveness.

#### *Securitisation and Special Purpose Entities*

The Banking Group has formed special purpose entities (SPEs) primarily for the purpose of allowing clients to hold investments and for asset securitisation transactions. The Banking Group does not consolidate SPEs that it does not control. As it can sometimes be difficult to determine whether the Banking Group controls an SPE, it makes judgements about its exposure to the risks and rewards, as well as about its ability to make operational decisions for the SPE in question. In many instances, elements are present that considered in isolation indicate control or lack of control over an SPE, but when considered together make it difficult to reach a clear conclusion. In such cases, the SPE is consolidated.

### 3 Risk Management Policies

SBS's objective is to appropriately manage all the risks that arise from its activities. SBS does not naturally seek treasury and financial risk from its involvement in the financial markets and consequently minimises risks wherever possible. Reviews of risk management policies, systems and reporting are conducted on a regular basis.

#### **Risk Governance Structure**

The Board has responsibility for reviewing all aspects of risk management. The Board receives comprehensive monthly reporting covering each area of risk management as outlined below. In addition SBS has specific policies in relation to liquidity and capital management which contain trigger points at which Board involvement is required.

#### *Audit and Risk Committee*

The Audit and Risk Committee is a sub committee of the Board and has the responsibility of:

- overseeing the quality of financial information presented to the Board;
- the effectiveness and integrity of the internal control environment;
- SBS's compliance with regulatory requirements that impact on the business; and
- the external and internal audit functions.

The committee consists of four directors. In addition the Chief Executive Officer, General Manager Finance and the General Manager Risk & Support are in attendance at meetings. The Audit and Risk Committee meets at least five times a year; and reports directly to the Board.

#### *Lending Committee*

The Lending Committee is a sub committee of the Board and has the responsibility of reviewing and approving all lending proposals in excess of \$1 million. The committee is made up of the full Board with senior management in attendance as requested. The Lending Committee usually meets at least twice a month.

#### *Asset and Liability Committee (ALCO)*

The ALCO has responsibility for the assessment of exposure to treasury counterparty, credit, market, liquidity and interest rate risk. This includes:

- reviewing SBS past performance with respect to asset and liability growth, yields, cost of funds, interest rate risk management and net interest margin;
- monitoring the interest rate risk position, liquidity, maturity, funding and credit position, financial investments portfolio, and financial performance;
- reviewing the current and recommended future hedging positions and risk profiles within risk control limits;
- monitoring interest rate pricing levels and interest margin levels for all assets and funding products;
- considering and evaluating the sensitivity of particular asset and liability classes to changes in market interest rates and yield curve shape;
- reviewing the liquidity position, investment and funding activity and making recommendations on future action;
- reviewing the funding strategy and funding risk mitigation;
- considering the level of capital employed, capital adequacy levels and the risk weighting of statement of financial position items;
- reviewing wholesale counterparty credit exposures; and
- monitoring SBS's credit risk position and trends.

The ALCO is made up of members of the senior management team and treasury function. The ALCO usually meets at least twice a month and reports directly to the Board.



## 3 Risk Management Policies *continued*

### *Credit Risk Committee (CRC)*

The CRC has responsibility for monitoring and reviewing exposure to credit risks in SBS's lending portfolios. This includes:

- monitoring maximum exposure to individual counterparties;
- reviewing the analysis and reporting of individual watch list and impaired loans; and
- monitoring the performance of lending portfolios in relation to excesses and past dues, industry and geographic concentrations.

The CRC is made up of members of the senior management team and credit risk management function. The CRC usually meets monthly and reports to the Board.

### *Operational Risk Committee (ORC)*

The ORC has responsibility for monitoring and reviewing exposure to operational risks arising from SBS's day to day activities. This includes:

- regular measurement, monitoring and reporting of operational risk;
- ensuring appropriate strategies are in place to manage and mitigate operational risks; and
- monitoring compliance with legislative and regulatory obligations.

The ORC is made up of members of the senior management team and the risk & support function. The ORC usually meets bi-monthly and reports to the Board.

### *Internal Audit*

SBS's internal audit function conducts independent reviews that assist the board of directors and management to meet their statutory and other obligations. The internal audit function has no reporting line to SBS management. The function reports directly to the chairman of the Audit and Risk Committee. The internal audit function has been carried out by the Dunedin based firm of Chartered Accountants, Deloitte. In performing this role, the internal audit function adopts a risk-based approach, encompassing reviews of the major risks that could impact upon SBS. Significant findings are reported quarterly to the Audit and Risk Committee.

An audit plan is prepared annually covering each business area of SBS, with greater emphasis placed on those areas with perceived higher risk. The plan is endorsed by the Audit and Risk Committee.

### *Specialist Support Functions*

Primary responsibility for the identification, control and mitigation of risk rests with each business unit. Oversight and governance are provided through specialist support functions including Risk and Support, Finance and Treasury. The role of these functional specialists is to maintain and review policies, establish limits which are consistent with the Board's risk appetite, monitor and report on compliance with those limits and generally to provide an oversight role in relation to the management of risk.

## **Specific Areas of Risk Management**

### *Credit Risk Management*

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 controlled through a combination of approvals, limits, reviews and monitoring procedures that are carried out on a regular basis, the frequency of which is dependent on the level of risk. Credit risk management involves a thorough evaluation of the credit risk associated with potential borrowers, the taking of security against the loan and close ongoing monitoring of account performance. Loans which show signs of adverse performance are managed by the credit risk management function which is responsible for the restructuring, collections and recovery process. For wholesale arrangements, credit risk is managed with reference to specific limits as outlined in detailed treasury management policies and reported to the Board on a monthly basis.

### *Interest Rate Risk Management*

Interest rate risk is the risk of loss arising from adverse changes in interest rates. Management's objective is to produce strong and stable net interest income over time. Interest rate risk management focuses on mismatches between the repricing dates of interest bearing assets and liabilities. Interest rate risk is managed using financial instruments to manage the risks within set limits as defined by SBS treasury policy. Regular reporting of interest rate risk against limits is provided to the Board.

### *Liquidity Risk Management*

Liquidity risk is the risk that under certain conditions, cash outflows can exceed cash inflows in a given period. SBS 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, use of committed wholesale funding facilities, utilisation of securitisation vehicles and management control of the growth of the business.

The Banking 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 Banking Group is subject to RBNZ's liquidity requirements as set out in the RBNZ's "Liquidity Policy" (BS13/BS13A), which took effect from 1 April 2010.

### *Operational Risk Management*

Operational risk is the risk arising from day to day operational activities which may result in direct or indirect loss. These losses may result from failure to comply with policies, procedures, laws and regulations, from fraud or forgery, from a breakdown in the availability or integrity of services, systems and information, or damage to SBS's reputation. 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.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 4 Income

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Interest income</b>				
Cash at bank	596	592	495	432
Funds with financial institutions - available for sale	3,692	3,299	3,466	3,115
Investment securities - available for sale	12,156	8,706	12,118	8,694
Investment securities - designated at fair value through profit or loss	158	137	-	-
Derivative financial instruments	(2,872)	(8,419)	(2,085)	(6,906)
Advances to customers - at amortised cost	159,935	176,854	134,616	147,597
Advances to customers - designated at fair value through profit or loss	388	1,518	387	1,488
Advances to customers - impaired	2,875	2,513	2,875	2,513
Loans to subsidiaries	-	-	6,080	7,270
	<b>176,928</b>	<b>185,200</b>	<b>157,952</b>	<b>164,203</b>
<b>Other operating income</b>				
Loan fees	936	996	2,294	2,463
Management fees	4,261	3,106	257	1,334
Other fee and commission income	8,102	7,697	1,964	1,910
Net insurance income	5,018	5,217	-	-
Dividends	74	50	-	-
Sundry income	1,723	1,545	870	248
	<b>20,114</b>	<b>18,611</b>	<b>5,385</b>	<b>5,955</b>

## 5 Expenses

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Interest expense</b>				
Redeemable shares	89,762	97,485	89,762	97,485
Deposits from customers	9,805	10,578	9,805	10,578
Other financial institutions	50	39	50	39
Subsidiary companies	-	-	167	163
Other borrowings	1,642	2,901	1,124	1,077
Subordinated redeemable shares	4,229	4,241	4,229	4,241
	<b>105,488</b>	<b>115,244</b>	<b>105,137</b>	<b>113,583</b>
<b>Other operating expenses</b>				
Auditors remuneration	341	314	232	231
Computer expenses	2,552	2,241	1,951	1,727
Fees and commissions	40	149	18	-
Fees to directors	684	638	638	592
Marketing	5,137	4,439	3,465	3,164
Personnel	27,849	26,224	19,193	18,073
Actuarial life adjustment	233	(332)	-	-
Amortisation and depreciation	3,083	3,599	2,167	2,758
Rent and leases	2,535	2,201	2,235	1,970
Write off of property, plant and equipment	259	153	190	107
Other expenses	10,630	9,302	7,251	6,051
	<b>53,343</b>	<b>48,928</b>	<b>37,340</b>	<b>34,673</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 5 Expenses continued

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Amounts received, or due and receivable by the auditors:				
KPMG auditing the financial statements	300	289	225	221
KPMG other assurance services <sup>1</sup>	41	25	7	10
	<b>341</b>	<b>314</b>	<b>232</b>	<b>231</b>

<sup>1</sup> Other assurance services includes regulatory reporting and other accounting related assistance.

Amounts received, or due and receivable by directors:				
JWA Smith (Retired July 2012)	250	121	250	121
JF Ward (Chairman)	104	81	93	70
JB Walker (Deputy Chairman)	72	66	60	55
KJ Ball	66	66	66	66
GJ Mulvey	61	61	55	55
JJ Grant	61	61	55	55
FE Spencer	66	65	55	57
AG Neill (Appointed August 2012)	41	-	41	-
GJ Diack (retired July 2011)	-	22	-	18
RL Smith <sup>2</sup>	-	-	-	-
	<b>721</b>	<b>543</b>	<b>675</b>	<b>497</b>
Provision for directors retiring allowance	(37)	95	(37)	95
	<b>684</b>	<b>638</b>	<b>638</b>	<b>592</b>

<sup>2</sup> RL Smith is an executive director and received no directors fees in addition to his salary.

Personnel expenses includes key management personnel compensation which comprised:				
Salaries and short-term employee benefits	4,094	3,949	1,668	1,768
Post-employment benefits	139	140	114	116
Other long term benefits	27	41	27	41
	<b>4,260</b>	<b>4,130</b>	<b>1,809</b>	<b>1,925</b>

## 6 Net Gain/(Loss) from Financial Instruments Designated at Fair Value

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Net gain/(loss) arising on:				
Investment securities	(31)	(21)	-	-
Derivative financial instruments	(750)	(381)	(900)	(578)
Hedge ineffectiveness on cash flow hedging	(19)	8	(19)	8
Advances to customers	(278)	(194)	(278)	(194)
	<b>(1,078)</b>	<b>(588)</b>	<b>(1,197)</b>	<b>(764)</b>

## Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

### 7 Taxation

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Reconciliation of the prima facie income tax payable on profit with income tax expense in the income statement</b>				
Surplus before income tax	19,722	17,068	13,420	8,678
Prima facie income tax	5,528	4,848	3,758	2,488
Adjust for the tax effect of:				
Imputed dividends	(18)	298	(1,903)	(1,255)
Revaluation property	30	-	17	-
Loss offset/subvention	-	-	-	5
Other permanent items	(136)	178	(19)	(106)
Prior period adjustments	(21)	(21)	2	(16)
	(145)	455	(1,903)	(1,372)
<b>Taxation expense/(benefit)</b>	<b>5,383</b>	<b>5,303</b>	<b>1,855</b>	<b>1,116</b>
<b>The major components of the income tax expense comprise:</b>				
<b>Amounts recognised in the income statement</b>				
<b>Current income tax</b>				
Current income tax charge	4,127	6,393	535	3,032
Adjustments recognised in the current period in relation to current tax of prior periods	(57)	(5)	(2)	-
<b>Deferred income tax</b>				
Deferred tax expenses relating to the origination and reversal of temporary differences	1,313	(1,085)	1,322	(1,916)
<b>Total income tax expense recognised in the income statement</b>	<b>5,383</b>	<b>5,303</b>	<b>1,855</b>	<b>1,116</b>
<b>The following amounts were charged/(credited) direct to equity:</b>				
Current income tax	964	398	964	398
Deferred income tax	888	1,081	885	885
<b>Total income tax expense recognised directly in equity</b>	<b>1,852</b>	<b>1,479</b>	<b>1,849</b>	<b>1,283</b>

### 8 Funds with Financial Institutions

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Call funds	39,234	10,137	36,510	9,001
Term deposits	105,256	80,843	100,731	76,824
	<b>144,490</b>	<b>90,980</b>	<b>137,241</b>	<b>85,825</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 9 Investment Securities

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Managed funds	-	672	-	-
NZ government securities	1,031	1,112	-	-
Equity securities	1,299	1,000	-	-
Local authority bonds	101,731	77,163	101,630	77,062
Bank bonds	164,938	129,252	164,938	129,252
Other bonds	131,234	56,534	131,027	56,534
	<b>400,233</b>	<b>265,733</b>	<b>397,595</b>	<b>262,848</b>

## 10 Derivative Financial Instruments

The Banking Group uses the following derivative instruments for economic or risk management purposes:

Interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of interest rates (for example, fixed rate for floating rate). No exchange of principal takes place. The Banking Group's credit risk represents the potential cost to replace the swap contracts if counterparties fail to fulfil their obligation. This risk is monitored on an ongoing basis within treasury policy guidelines, and with reference to a proportion of the notional amount of the contracts and the term to expiry of the contracts. To control the level of credit risk taken, the Banking Group assesses counterparties based on their published credit rating compared with treasury policy limits.

Interest rate options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of interest rate risk. The Banking Group is exposed to credit risk on purchased options only, and only to the extent of their carrying amount, which is their fair value.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Banking Group's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates relative to their terms. The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities, can fluctuate significantly from time to time. The fair values of derivative instruments held are set out below.

The Banking Group undertakes 100% of its transactions in interest rate contracts with other financial institutions. Management has established limits such that, at any time, less than 60% of equity is at risk with any individual counterparty.

The risk management practices and accounting treatment are disclosed in the Statement of Accounting Policies. The movement in fair value of derivative financial instruments are included in the income statement as 'net gain/(loss) from financial instruments designated at fair value' except when the derivative is in a cash flow hedge.

### Hedge Accounting

#### Cash Flow Hedges

The Banking Group hedges the forecasted interest cash flows from floating rate loans and deposits using interest rate swaps and interest rate options. There were no transactions where cash flow hedge accounting ceased in the year ended 31 March 2013 as a result of highly probable cash flows no longer expected to occur (31 March 2012 \$nil).

The gain and loss from re-measuring the hedging instruments at fair value is deferred in equity in the hedging reserve, to the extent that the hedge is effective. This amount is re-classified into the income statement on the maturity of the interest rate swap. The ineffective portion is recognised in the income statement immediately. Effectiveness of the hedges is tested on a monthly basis.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 10 Derivative Financial Instruments continued

	BANKING GROUP			PARENT		
	Notional principal	Fair value assets	Fair value liabilities	Notional principal	Fair value assets	Fair value liabilities
<b>As at 31 March 2013</b>						
<b>Held for risk management - at fair value</b>						
<i>Interest rate related contracts</i>						
Swaps	100,868	503	547	100,868	503	547
Options	-	-	-	-	-	-
<b>Total held for risk management at fair value</b>	<b>100,868</b>	<b>503</b>	<b>547</b>	<b>100,868</b>	<b>503</b>	<b>547</b>
<b>Held for hedging - cash flow hedges</b>						
<i>Interest rate related contracts</i>						
Swaps	745,750	1,893	6,070	795,750	2,111	6,070
Options	-	-	-	-	-	-
<b>Total held for hedging</b>	<b>745,750</b>	<b>1,893</b>	<b>6,070</b>	<b>795,750</b>	<b>2,111</b>	<b>6,070</b>
<b>Total derivative financial instruments</b>	<b>846,618</b>	<b>2,396</b>	<b>6,617</b>	<b>896,618</b>	<b>2,614</b>	<b>6,617</b>
<b>As at 31 March 2012</b>						
<b>Held for risk management - at fair value</b>						
<i>Interest rate related contracts</i>						
Swaps	145,030	601	634	157,114	751	636
Options	-	-	-	-	-	-
<b>Total held for risk management at fair value</b>	<b>145,030</b>	<b>601</b>	<b>634</b>	<b>157,114</b>	<b>751</b>	<b>636</b>
<b>Held for hedging - cash flow hedges</b>						
<i>Interest rate related contracts</i>						
Swaps	871,750	2,188	9,572	931,750	3,005	9,623
Options	-	-	-	-	-	-
<b>Total held for hedging</b>	<b>871,750</b>	<b>2,188</b>	<b>9,572</b>	<b>931,750</b>	<b>3,005</b>	<b>9,623</b>
<b>Total derivative financial instruments</b>	<b>1,016,780</b>	<b>2,789</b>	<b>10,206</b>	<b>1,088,864</b>	<b>3,756</b>	<b>10,259</b>

## 11 Advances to Customers

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
Residential		1,635,579	1,749,462	1,635,579	1,703,874
Agricultural		334,934	385,419	334,934	385,419
Commercial		172,337	211,364	166,989	199,578
Consumer		109,194	111,628	-	-
<b>Gross advances</b>		<b>2,252,044</b>	<b>2,457,873</b>	<b>2,137,502</b>	<b>2,288,871</b>
Provisions for credit impairment	(12)	(24,283)	(29,563)	(20,460)	(25,795)
Deferred fee revenue and expenses		(2,008)	(2,587)	(271)	(566)
<b>Total net advances</b>	(28)	<b>2,225,753</b>	<b>2,425,723</b>	<b>2,116,771</b>	<b>2,262,510</b>

As at 31 March 2013 \$6 million of advances to customers are designated at fair value through profit or loss (31 March 2012 \$20 million). There have been no changes in the fair value recognised on these advances on account of credit risk.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 12 Provision for Credit Impairment

### BANKING GROUP as at 31 March 2013

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>Individual provisions against advances and loans</b>				
Balance at beginning of the year	1,075	-	19,172	20,247
New provisions during the year	2,352	-	10,022	12,374
Balances written off during the year	(2,542)	-	(15,167)	(17,709)
Recoveries/reversals of previously recognised provision	-	-	-	-
Balance at end of the year	885	-	14,027	14,912
<b>Collective provisions against advances and loans</b>				
Balance at beginning of the year	4,190	3,446	1,680	9,316
Charged to income statement	-	198	(143)	55
Balance at end of the year	4,190	3,644	1,537	9,371
<b>Total provisions for credit impairment</b>	<b>5,075</b>	<b>3,644</b>	<b>15,564</b>	<b>24,283</b>

### Reconciliation of provision movements

Bad debts written off during the year	417	4,222	236	4,875
Individual provisions	2,352	-	10,022	12,374
Collective provision	-	198	(143)	55
<b>Provision for credit impairment to income statement</b>	<b>2,769</b>	<b>4,420</b>	<b>10,115</b>	<b>17,304</b>

- Residential mortgages comprise advances to individuals and corporates that are secured against residential properties. They include investments in residential property as well as owner-occupied housing
- Retail exposures comprise consumer personal and consumer finance lending
- Corporate exposures comprise primarily advances to individuals, corporates or small to medium enterprises that are secured against commercial or agricultural properties

### PARENT as at 31 March 2013

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>Individual provisions against advances and loans</b>				
Balance at beginning of the year	1,075	-	19,172	20,247
New provisions during the year	2,352	-	10,022	12,374
Balances written off during the year	(2,542)	-	(15,167)	(17,709)
Recoveries/reversals of previously recognised provision	-	-	-	-
Balance at end of the year	885	-	14,027	14,912
<b>Collective provisions against advances and loans</b>				
Balance at beginning of the year	4,190	-	1,358	5,548
Charged to income statement	-	-	-	-
Balance at end of the year	4,190	-	1,358	5,548
<b>Total provisions for credit impairment</b>	<b>5,075</b>	<b>-</b>	<b>15,385</b>	<b>20,460</b>

### Reconciliation of provision movements

Bad debts written off during the year	417	-	186	603
Individual provisions	2,352	-	10,022	12,374
Collective provision	-	-	-	-
<b>Provision for credit impairment to income statement</b>	<b>2,769</b>	<b>-</b>	<b>10,208</b>	<b>12,977</b>



# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 12 Provision for Credit Impairment continued

### BANKING GROUP as at 31 March 2012

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>Individual provisions against advances and loans</b>				
Balance at beginning of the year	2,469	-	10,211	12,680
New provisions during the year	716	-	16,100	16,816
Balances written off during the year	(2,110)	-	(7,139)	(9,249)
Recoveries/reversals of previously recognised provision	-	-	-	-
Balance at end of the year	<b>1,075</b>	<b>-</b>	<b>19,172</b>	<b>20,247</b>
<b>Collective provisions against advances and loans</b>				
Balance at beginning of the year	3,800	3,591	1,637	9,028
Charged to income statement	390	(145)	43	288
Balance at end of the year	<b>4,190</b>	<b>3,446</b>	<b>1,680</b>	<b>9,316</b>
<b>Total provisions for credit impairment</b>	<b>5,265</b>	<b>3,446</b>	<b>20,852</b>	<b>29,563</b>

<b>Reconciliation of provision movements</b>				
Bad debts written off during the year	374	4,335	170	4,879
Individual provisions	716	-	16,100	16,816
Collective provision	390	(145)	43	288
<b>Provision for credit impairment to income statement</b>	<b>1,480</b>	<b>4,190</b>	<b>16,313</b>	<b>21,983</b>

### PARENT as at 31 March 2012

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>Individual provisions against advances and loans</b>				
Balance at beginning of the year	2,469	-	10,211	12,680
New provisions during the year	716	-	16,100	16,816
Balances written off during the year	(2,110)	-	(7,139)	(9,249)
Recoveries/reversals of previously recognised provision	-	-	-	-
Balance at end of the year	<b>1,075</b>	<b>-</b>	<b>19,172</b>	<b>20,247</b>
<b>Collective provisions against advances and loans</b>				
Balance at beginning of the year	3,800	-	1,248	5,048
Charged to income statement	390	-	110	500
Balance at end of the year	<b>4,190</b>	<b>-</b>	<b>1,358</b>	<b>5,548</b>
<b>Total provisions for credit impairment</b>	<b>5,265</b>	<b>-</b>	<b>20,530</b>	<b>25,795</b>

<b>Reconciliation of provision movements</b>				
Bad debts written off during the year	396	-	215	611
Individual provisions	716	-	16,100	16,816
Collective provision	390	-	110	500
<b>Provision for credit impairment to income statement</b>	<b>1,502</b>	<b>-</b>	<b>16,425</b>	<b>17,927</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 13 Asset Quality

### BANKING GROUP as at 31 March 2013

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>(a) Asset quality - advances to customers</b>				
Neither past due or impaired	1,622,225	98,177	475,550	2,195,952
Individually impaired	1,912	-	21,846	23,758
Past due	11,243	9,785	9,298	30,326
Provision for credit impairment	(5,075)	(3,644)	(15,564)	(24,283)
Carrying amount	<b>1,630,305</b>	<b>104,318</b>	<b>491,130</b>	<b>2,225,753</b>
<b>(b) Ageing of past due but not impaired assets</b>				
Past due 0-29 days	6,632	7,087	5,375	19,094
Past due 30-59 days	2,179	1,575	33	3,787
Past due 60-89 days	970	882	457	2,309
Past due 90 days +	1,462	241	3,433	5,136
Carrying amount	<b>11,243</b>	<b>9,785</b>	<b>9,298</b>	<b>30,326</b>
<b>(c) Impaired assets</b>				
Balance at beginning of the year	2,334	-	38,876	41,210
Additions to individually impaired assets	1,100	-	5,855	6,955
Reductions to individually impaired assets	(1,522)	-	(22,885)	(24,407)
Balance at end of the year	1,912	-	21,846	23,758
Provision at end of the year	(885)	-	(14,027)	(14,912)
Net carrying amount at end of the year	<b>1,027</b>	<b>-</b>	<b>7,819</b>	<b>8,846</b>
Undrawn balances on individually impaired lending commitments	-	-	-	-

#### (d) Other assets under administration

There are no other assets under administration as at 31 March 2013.

### PARENT as at 31 March 2013

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>(a) Asset quality - advances to customers</b>				
Neither past due or impaired	1,622,225	-	470,835	2,093,060
Individually impaired	1,912	-	21,846	23,758
Past due	11,243	-	9,170	20,413
Provision for credit impairment	(5,075)	-	(15,385)	(20,460)
Carrying amount	<b>1,630,305</b>	<b>-</b>	<b>486,466</b>	<b>2,116,771</b>
<b>(b) Ageing of past due but not impaired assets</b>				
Past due 0-29 days	6,632	-	5,280	11,912
Past due 30-59 days	2,179	-	-	2,179
Past due 60-89 days	970	-	457	1,427
Past due 90 days +	1,462	-	3,433	4,895
Carrying amount	<b>11,243</b>	<b>-</b>	<b>9,170</b>	<b>20,413</b>
<b>(c) Impaired assets</b>				
Balance at beginning of the year	2,334	-	38,876	41,210
Additions to individually impaired assets	1,100	-	5,855	6,955
Reductions to individually impaired assets	(1,522)	-	(22,885)	(24,407)
Balance at end of the year	1,912	-	21,846	23,758
Provision at end of the year	(885)	-	(14,027)	(14,912)
Net carrying amount at end of the year	<b>1,027</b>	<b>-</b>	<b>7,819</b>	<b>8,846</b>
Undrawn balances on individually impaired lending commitments	-	-	-	-

#### (d) Other assets under administration

There are no other assets under administration as at 31 March 2013.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 13 Asset Quality continued

### BANKING GROUP as at 31 March 2012

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>(a) Asset quality - advances to customers</b>				
Neither past due or impaired	1,726,561	101,503	542,689	2,370,753
Individually impaired	2,334	-	38,876	41,210
Past due	20,160	8,751	14,412	43,323
Provision for credit impairment	(5,265)	(3,446)	(20,852)	(29,563)
Carrying amount	<b>1,743,790</b>	<b>106,808</b>	<b>575,125</b>	<b>2,425,723</b>
<b>(b) Ageing of past due but not impaired assets</b>				
Past due 0-29 days	7,923	6,459	4,033	18,415
Past due 30-59 days	4,869	1,348	840	7,057
Past due 60-89 days	3,238	676	2,264	6,178
Past due 90 days +	4,130	268	7,275	11,673
Carrying amount	<b>20,160</b>	<b>8,751</b>	<b>14,412</b>	<b>43,323</b>
<b>(c) Impaired assets</b>				
Balance at beginning of the year	5,915	-	32,427	38,342
Additions to individually impaired assets	557	-	17,984	18,541
Reductions to individually impaired assets	(4,138)	-	(11,535)	(15,673)
Balance at end of the year	2,334	-	38,876	41,210
Provision at end of the year	(1,075)	-	(19,172)	(20,247)
Net carrying amount at end of the year	<b>1,259</b>	<b>-</b>	<b>19,704</b>	<b>20,963</b>
Undrawn balances on individually impaired lending commitments	-	-	-	-

#### (d) Other assets under administration

There are no other assets under administration as at 31 March 2012.

### PARENT as at 31 March 2012

	Residential Mortgages	Retail Exposures	Corporate Exposures	Total
<b>(a) Asset quality - advances to customers</b>				
Neither past due or impaired	1,681,577	-	531,645	2,213,222
Individually impaired	2,334	-	38,876	41,210
Past due	19,556	-	14,317	33,873
Provision for credit impairment	(5,265)	-	(20,530)	(25,795)
Carrying amount	<b>1,698,202</b>	<b>-</b>	<b>564,308</b>	<b>2,262,510</b>
<b>(b) Ageing of past due but not impaired assets</b>				
Past due 0-29 days	7,537	-	3,965	11,502
Past due 30-59 days	4,651	-	819	5,470
Past due 60-89 days	3,238	-	2,262	5,500
Past due 90 days +	4,130	-	7,271	11,401
Carrying amount	<b>19,556</b>	<b>-</b>	<b>14,317</b>	<b>33,873</b>
<b>(c) Impaired assets</b>				
Balance at beginning of the year	5,915	-	32,427	38,342
Additions to individually impaired assets	557	-	17,984	18,541
Reductions to individually impaired assets	(4,138)	-	(11,535)	(15,673)
Balance at end of the year	2,334	-	38,876	41,210
Provision at end of the year	(1,075)	-	(19,172)	(20,247)
Net carrying amount at end of the year	<b>1,259</b>	<b>-</b>	<b>19,704</b>	<b>20,963</b>
Undrawn balances on individually impaired lending commitments	-	-	-	-

#### (d) Other assets under administration

There are no other assets under administration as at 31 March 2012.

## Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

### 14 Loan Securitisation

Mortgages assigned by SBS to the SBS Invercargill W Trust during the year ended 31 March 2013 amounted to \$150.45 million (31 March 2012 \$nil). SBS retains some of the risks and rewards of ownership through the provision of a subordinated loan and accordingly it is appropriate to consolidate the financial statements of SBS Invercargill W Trust within the Parent.

Mortgages assigned by the SBS Invercargill W Trust to the SBS Oreti Trust No. 2 during the year ended 31 March 2013 amounted to \$nil (31 March 2012 \$nil). SBS retains some of the risks and rewards of this trust by holding the securities issued by the trust and accordingly it is appropriate to consolidate the financial statements of SBS Oreti Trust No. 2 within the Parent.

The SBS Oreti Trust No. 1 is in the process of being wound up. There have been no mortgages assigned by the SBS Invercargill W Trust to the SBS Oreti Trust No. 1 since the year ended March 2008.

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Securitised loan balances</b>				
SBS Invercargill W Trust	130,114	-	130,114	-
SBS Oreti Trust No. 1	-	45,588	-	-
SBS Oreti Trust No. 2	125,542	164,950	125,542	164,950
	<b>255,656</b>	<b>210,538</b>	<b>255,656</b>	<b>164,950</b>

### 15 Investments in Subsidiaries

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Investments in subsidiaries	-	-	15,180	15,180
	<b>-</b>	<b>-</b>	<b>15,180</b>	<b>15,180</b>
Loans to subsidiaries (at amortised cost)	-	-	87,808	89,871
	<b>-</b>	<b>-</b>	<b>87,808</b>	<b>89,871</b>

	Percentage Held		Balance Date	Nature of Business
	31/3/13	31/3/12		
<b>Subsidiaries:</b>				
Fraser Properties Limited	100.0%	100.0%	31 March	Property Holding
Southsure Assurance Limited	80.0%	80.0%	31 March	Insurance
Finance Now Limited	71.5%	71.5%	31 March	Finance Company
Funds Administration New Zealand Limited	57.0%	57.0%	31 March	Funds Administration
<b>In-substance subsidiaries:</b>				
SBS Invercargill W Trust	-	-	31 March	Mortgage Securitisation
SBS Oreti Trust No. 1	-	-	31 March	Mortgage Securitisation
SBS Oreti Trust No. 2	-	-	31 March	Mortgage Securitisation

All subsidiaries and in-substance subsidiaries are incorporated in New Zealand. For all subsidiaries, the ownership percentage equates to the voting power held. Refer to Note 33 - Related Parties for further details of loans to subsidiaries.

### 16 Other Assets

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Prepayments	637	812	410	676
Receivables from related parties	-	-	596	3,403
Other receivables	1,817	1,219	1,019	493
	<b>2,454</b>	<b>2,031</b>	<b>2,025</b>	<b>4,572</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 17 Property, Plant and Equipment

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Freehold land (at valuation)	2,140	2,085	1,140	1,085
Buildings (at valuation)	8,989	9,762	1,489	1,462
Total carrying amount	11,129	11,847	2,629	2,547
Leasehold assets (at cost)	5,998	5,593	5,473	5,086
Accumulated depreciation	(2,773)	(2,715)	(2,710)	(2,616)
Total carrying amount	3,225	2,878	2,763	2,470
Computer equipment (at cost)	7,629	6,961	6,990	5,628
Accumulated depreciation	(5,411)	(5,296)	(4,912)	(4,157)
Total carrying amount	2,218	1,665	2,078	1,471
Other assets (at cost)	7,874	7,519	4,916	4,722
Accumulated depreciation	(5,442)	(5,085)	(3,178)	(3,010)
Total carrying amount	2,432	2,434	1,738	1,712
<b>Total property, plant and equipment</b>	<b>19,004</b>	<b>18,824</b>	<b>9,208</b>	<b>8,200</b>

Other assets include plant, furniture and fittings and motor vehicles.

### Land and Buildings

Independent valuations of freehold land and buildings were carried out as at 31 March 2013 by Tony Chadderton, a registered valuer with Chadderton & Associates and by Max Plested, a registered valuer with Telfer Young. The valuations were based on capitalisation of net market rental. Such valuations are performed on an open market basis, being the amounts for which the assets could be exchanged between a knowledgeable, willing seller in an arm's length transaction at the valuation date.

The aggregate of the latest government valuations for all land and buildings owned by the Banking Group as at 31 March 2013 is \$10.58 million (31 March 2012 \$10.58 million).

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>The carrying amount of land and buildings had they been recognised under the cost model are as follows:</b>				
Freehold land	1,910	1,910	569	569
Buildings	8,072	8,249	958	1,039
	<b>9,982</b>	<b>10,159</b>	<b>1,527</b>	<b>1,608</b>

<b>Reconciliation of the carrying amounts for each class of property, plant and equipment are set out below:</b>				
<b>Freehold land and buildings</b>				
Balance at beginning of the year	11,847	11,930	2,547	2,430
Additions	-	-	-	-
Revaluation	(597)	37	115	148
Disposals	-	-	-	-
Depreciation	(121)	(120)	(33)	(31)
Balance at end of the year	<b>11,129</b>	<b>11,847</b>	<b>2,629</b>	<b>2,547</b>
<b>Leasehold assets</b>				
Balance at beginning of the year	2,878	2,495	2,470	2,371
Additions	877	800	713	434
Disposals	(212)	(81)	(141)	(35)
Depreciation	(318)	(336)	(279)	(300)
Balance at end of the year	<b>3,225</b>	<b>2,878</b>	<b>2,763</b>	<b>2,470</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 17 Property, Plant and Equipment continued

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Computer equipment</b>				
Balance at beginning of the year	1,665	1,961	1,471	1,833
Additions	1,626	741	1,552	575
Disposals	(15)	(16)	(15)	(15)
Depreciation	(1,058)	(1,021)	(930)	(922)
Balance at end of the year	<b>2,218</b>	<b>1,665</b>	<b>2,078</b>	<b>1,471</b>
<b>Other assets</b>				
Balance at beginning of the year	2,434	2,544	1,712	1,799
Additions	700	643	514	395
Disposals	(77)	(158)	(74)	(80)
Depreciation	(625)	(595)	(414)	(402)
Balance at end of the year	<b>2,432</b>	<b>2,434</b>	<b>1,738</b>	<b>1,712</b>
<b>Total property, plant and equipment</b>	<b>19,004</b>	<b>18,824</b>	<b>9,208</b>	<b>8,200</b>

## 18 Intangible Assets

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Goodwill (at cost)</b>				
Accumulated impairment	1,160	1,160	-	-
	(145)	(145)	-	-
Total carrying amount	<b>1,015</b>	<b>1,015</b>	<b>-</b>	<b>-</b>
<b>Software (at cost)</b>				
Accumulated depreciation	13,298	11,490	9,169	7,784
	(10,993)	(10,039)	(7,431)	(6,921)
Total carrying amount	<b>2,305</b>	<b>1,451</b>	<b>1,738</b>	<b>863</b>
<b>Total intangible assets</b>	<b>3,320</b>	<b>2,466</b>	<b>1,738</b>	<b>863</b>

No impairment losses have been recognised against the gross carrying amount of software and other intangible assets for the year ended 31 March 2013 (31 March 2012 \$nil). Testing for impairment of goodwill is undertaken using models which calculate the valuation with reference to applicable price to earnings ratios.

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Reconciliation of the carrying amounts for intangible assets are set out below:</b>				
<b>Goodwill</b>				
Balance at beginning of the year	1,015	1,015	-	-
Additions	-	-	-	-
Impairment	-	-	-	-
Balance at end of the year	<b>1,015</b>	<b>1,015</b>	<b>-</b>	<b>-</b>
<b>Software</b>				
Balance at beginning of the year	1,451	1,659	863	1,090
Additions	1,817	1,319	1,386	876
Disposals	(2)	-	-	-
Amortisation for the year	(961)	(1,527)	(511)	(1,103)
Impairment	-	-	-	-
Balance at end of the year	<b>2,305</b>	<b>1,451</b>	<b>1,738</b>	<b>863</b>
<b>Total intangible assets</b>	<b>3,320</b>	<b>2,466</b>	<b>1,738</b>	<b>863</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 19 Deferred Tax Assets and Liabilities

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Provision for deferred tax</b>				
Balance at beginning of the year	7,485	7,481	9,182	8,151
(Charged)/credited to income statement	(1,313)	1,085	(1,322)	1,916
(Charged)/credited to equity	(888)	(1,081)	(885)	(885)
<b>Balance at end of the year</b>	<b>5,284</b>	<b>7,485</b>	<b>6,975</b>	<b>9,182</b>
<b>Recognised deferred tax assets and liabilities:</b>				
<b>Deferred tax assets/(liabilities) comprise the following temporary differences:</b>				
Provision for credit impairment	6,601	8,079	5,488	6,982
Derivative financial instruments	1,073	2,149	1,027	1,905
Funds with financial institutions - available for sale	(12)	29	-	-
Property, plant and equipment	(2,295)	(2,436)	(175)	(285)
Revaluation of property	(100)	(280)	(100)	(93)
Provisions	486	517	407	428
Other	(469)	(573)	328	245
<b>Net deferred tax assets</b>	<b>5,284</b>	<b>7,485</b>	<b>6,975</b>	<b>9,182</b>
<b>Movements in temporary differences during the year (charged)/credited to the income statement:</b>				
Provision for credit impairment	(1,478)	2,261	(1,494)	2,259
Derivative financial instruments	(49)	(169)	-	(102)
Advances at fair value through profit or loss	-	41	-	41
Property, plant and equipment	141	56	110	28
Provisions	(31)	80	(21)	57
Other	104	(1,184)	83	(367)
<b>Total deferred tax (charged)/credited to the income statement</b>	<b>(1,313)</b>	<b>1,085</b>	<b>(1,322)</b>	<b>1,916</b>
<b>Movements in temporary differences during the year (charged)/credited to equity:</b>				
Funds with financial institutions - available for sale	(41)	7	-	-
Derivative financial instruments	(1,027)	(1,078)	(878)	(844)
Revaluation of property	180	(10)	(7)	(41)
<b>Total deferred tax (charged)/credited to equity</b>	<b>(888)</b>	<b>(1,081)</b>	<b>(885)</b>	<b>(885)</b>

There are no unrecognised deferred tax assets as at 31 March 2013 (31 March 2012 \$nil).



# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 20 Other Liabilities

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Sundry creditors	10,103	5,764	4,172	3,924
Employee entitlements	3,361	3,244	2,482	2,393
Insurance policy liability	4,816	4,582	-	-
Provision for dividend	264	998	-	-
	<b>18,544</b>	<b>14,588</b>	<b>6,654</b>	<b>6,317</b>

## 21 Subordinated Redeemable Shares

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
SBS Premier Bond	61,232	61,242	61,232	61,242
	<b>61,232</b>	<b>61,242</b>	<b>61,232</b>	<b>61,242</b>

These five-year fixed rate bonds are issued continuously as subordinated redeemable shares and rank behind redeemable shareholders, depositors and other unsecured creditors of SBS.

At 31 March 2013 \$16.29 million of subordinated redeemable shares qualify as lower tier 2 capital for Reserve Bank of New Zealand capital adequacy purposes (31 March 2012 \$28.41 million).

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 22 Equity

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Revaluation reserve - property, plant and equipment	454	825	454	343
Revaluation reserve - available for sale assets	4,803	2,240	4,780	2,300
Revaluation reserve - cash flow hedging	(2,726)	(5,258)	(2,641)	(4,899)
Reserves	2,531	(2,193)	2,593	(2,256)
Retained earnings	222,400	210,667	207,710	196,145
	224,931	208,474	210,303	193,889
Non-controlling interests	6,659	6,887	-	-
<b>Total equity</b>	<b>231,590</b>	<b>215,361</b>	<b>210,303</b>	<b>193,889</b>
<b>Movement in reserves:</b>				
<b>Revaluation reserve - property, plant and equipment</b>				
Balance at beginning of the year	825	798	343	237
Surplus on revaluation of land and buildings	(551)	38	118	147
Deferred tax on revaluation	180	(11)	(7)	(41)
Net movement for the year	(371)	27	111	106
Balance at end of the year	<b>454</b>	<b>825</b>	<b>454</b>	<b>343</b>
<b>Revaluation reserve - available for sale assets</b>				
Balance at beginning of the year	2,240	1,236	2,300	1,277
Net gains/(losses) from changes in fair value	3,589	1,390	3,445	1,421
Current/deferred tax on changes in fair value	(1,005)	(391)	(965)	(398)
Non-controlling interests share of net gains/(losses) from changes in fair value	(29)	6	-	-
Non-controlling interests share of current/deferred tax in fair value	8	(1)	-	-
Net movement for the year	2,563	1,004	2,480	1,023
Balance at end of the year	<b>4,803</b>	<b>2,240</b>	<b>4,780</b>	<b>2,300</b>
<b>Revaluation reserve - cash flow hedging reserve</b>				
Balance at beginning of the year	(5,258)	(7,859)	(4,899)	(7,067)
Net gains/(losses) from changes in fair value	3,668	3,850	3,136	3,012
Deferred tax on changes in fair value	(1,027)	(1,078)	(878)	(844)
Non-controlling interests share of net gains/(losses) from changes in fair value	(152)	(238)	-	-
Non-controlling interests share of deferred tax on changes in fair value	43	67	-	-
Net movement for the year	2,532	2,601	2,258	2,168
Balance at end of the year	<b>(2,726)</b>	<b>(5,258)</b>	<b>(2,641)</b>	<b>(4,899)</b>
<b>Retained earnings</b>				
Balance at beginning of the year	210,667	201,447	196,145	188,583
Net surplus for the year	14,339	11,765	11,565	7,562
Non-controlling interests	(2,606)	(2,545)	-	-
Balance at end of the year	<b>222,400</b>	<b>210,667</b>	<b>207,710</b>	<b>196,145</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 23 Reconciliation of Net Surplus to Net Operating Cash Flows

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Net surplus for year</b>	14,339	11,765	11,565	7,562
<b>Add/(less) non cash items</b>				
Depreciation and amortisation	3,083	3,599	2,167	2,758
Provision for credit impairment	17,304	21,983	12,977	17,927
Write off of property, plant and equipment	259	153	190	107
Property revaluations	107	-	61	-
Actuarial life adjustment	233	(332)	-	-
Dividend provision	-	-	2,152	(160)
Dividend provision - non-controlling interest	733	5	-	-
Deferred fee revenue and expenses	(582)	(406)	(295)	(232)
Derivatives fair value adjustment	769	373	919	570
Advances fair value adjustment	278	194	278	193
Investment securities fair value adjustment	31	21	-	-
Interest free loans fair value adjustment	(1)	(7)	(1)	(7)
Net deferred tax assets	348	(1,490)	360	(2,316)
	<b>22,562</b>	<b>24,093</b>	<b>18,808</b>	<b>18,840</b>
<b>Deferral or accruals of past or future operating cash receipts or payments</b>				
Change in income tax payable/receivable	(1,697)	387	(1,498)	23
Change in sundry debtors	(423)	477	395	1,148
Change in sundry creditors	3,722	(2,675)	337	(2,001)
Change in accruals relating to interest receivable	(976)	(460)	(1,114)	(384)
Change in accruals relating to accrued interest and dividends payable to customers	2,308	(2,145)	2,315	(2,151)
Change in accruals relating to accrued interest payable to financial institutions	295	-	295	-
Change in net advances	182,018	136,413	131,984	122,268
Change in shares and deposits	(59,241)	80,458	(58,557)	80,580
Change in amounts due to other financial institutions	80,000	-	80,000	-
Change in other borrowings	(52,092)	(55,004)	-	(41,385)
Change in subordinated redeemable shares	-	-	-	-
Change in cash held on behalf of Lifestages Mortgage Portfolio	-	(2,430)	-	(2,430)
	<b>153,914</b>	<b>155,021</b>	<b>154,157</b>	<b>155,668</b>
<b>Items classified as cash</b>				
Change in accruals relating to funds with financial institutions	580	(1,722)	586	(1,685)
<b>Net cash flows from operating activities</b>	<b>191,395</b>	<b>189,157</b>	<b>185,116</b>	<b>180,385</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 24 Analysis of Funding

BANKING GROUP					
		Total	Weighted average interest rate	Total	Weighted average interest rate
	Note	31/3/13	%	31/3/12	%
<b>Redeemable shares</b>					
Between 0 and 1 year		2,020,518	3.95	2,030,748	4.15
Between 1 and 2 years		122,296	4.55	168,570	4.71
Between 2 and 3 years		30,709	5.24	25,833	5.72
Between 3 and 4 years		3,396	5.86	6,580	6.62
Between 4 and 5 years		3,373	5.18	3,083	6.79
Over 5 years		-	-	-	-
Total redeemable shares	(28)	<b>2,180,292</b>	<b>4.01</b>	<b>2,234,814</b>	<b>4.21</b>
<b>Deposits from customers</b>					
Between 0 and 1 year		245,983	3.89	243,596	3.96
Between 1 and 2 years		2,981	4.62	7,842	4.99
Between 2 and 3 years		1,305	4.74	1,466	5.02
Between 3 and 4 years		630	5.70	-	-
Between 4 and 5 years		200	5.05	596	5.70
Over 5 years		-	-	-	-
Total deposits from customers	(28)	<b>251,099</b>	<b>3.91</b>	<b>253,500</b>	<b>4.01</b>
<b>Due to other financial institutions</b>					
Between 0 and 1 year		-	-	-	-
Between 1 and 2 years		-	-	-	-
Between 2 and 3 years		-	-	-	-
Between 3 and 4 years		-	-	-	-
Between 4 and 5 years		-	-	-	-
Over 5 years		80,295	3.45	-	-
Total due to other financial institutions	(28)	<b>80,295</b>	<b>3.45</b>	<b>-</b>	<b>-</b>
<b>Subordinated redeemable shares</b>					
Between 0 and 1 year		42,225	6.95	-	-
Between 1 and 2 years		17,082	7.00	42,233	6.95
Between 2 and 3 years		1,925	7.00	17,084	7.00
Between 3 and 4 years		-	-	1,925	7.00
Between 4 and 5 years		-	-	-	-
Over 5 years		-	-	-	-
Total subordinated redeemable shares	(28)	<b>61,232</b>	<b>6.97</b>	<b>61,242</b>	<b>6.97</b>
		<b>2,572,918</b>	<b>4.05</b>	<b>2,549,556</b>	<b>4.25</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 24 Analysis of Funding continued

	Note	PARENT		Total	Weighted average interest rate
		Total	Weighted average interest rate		
		31/3/13	%	31/3/12	%
<b>Redeemable shares</b>					
Between 0 and 1 year		2,025,942	3.95	2,035,481	4.15
Between 1 and 2 years		122,296	4.55	168,570	4.71
Between 2 and 3 years		30,709	5.24	25,833	5.72
Between 3 and 4 years		3,396	5.86	6,580	6.62
Between 4 and 5 years		3,373	5.18	3,083	6.79
Over 5 years		-	-	-	-
Total redeemable shares	(28)	<b>2,185,716</b>	<b>4.01</b>	<b>2,239,547</b>	<b>4.21</b>
<b>Deposits from customers</b>					
Between 0 and 1 year		245,983	3.89	243,596	3.96
Between 1 and 2 years		2,981	4.62	7,842	4.99
Between 2 and 3 years		1,305	4.74	1,466	5.02
Between 3 and 4 years		630	5.70	-	-
Between 4 and 5 years		200	5.05	596	5.70
Over 5 years		-	-	-	-
Total deposits from customers	(28)	<b>251,099</b>	<b>3.91</b>	<b>253,500</b>	<b>4.01</b>
<b>Due to other financial institutions</b>					
Between 0 and 1 year		-	-	-	-
Between 1 and 2 years		-	-	-	-
Between 2 and 3 years		-	-	-	-
Between 3 and 4 years		-	-	-	-
Between 4 and 5 years		-	-	-	-
Over 5 years		80,295	3.45	-	-
Total due to other financial institutions	(28)	<b>80,295</b>	<b>3.45</b>	<b>-</b>	<b>-</b>
<b>Subordinated redeemable shares</b>					
Between 0 and 1 year		42,225	6.95	-	-
Between 1 and 2 years		17,082	7.00	42,233	6.95
Between 2 and 3 years		1,925	7.00	17,084	7.00
Between 3 and 4 years		-	-	1,925	7.00
Between 4 and 5 years		-	-	-	-
Over 5 years		-	-	-	-
Total subordinated redeemable shares	(28)	<b>61,232</b>	<b>6.97</b>	<b>61,242</b>	<b>6.97</b>
		<b>2,578,342</b>	<b>4.05</b>	<b>2,554,289</b>	<b>4.25</b>

Redeemable shares, deposits and subordinated redeemable shares are unsecured.

Floating rate redeemable shares and deposits have been included above, therefore the weighted average interest rates provided are only meaningful at the balance date noted. No analysis of other borrowings has been included above on the basis that these amounts relate to the loan securitisation vehicles discussed in Notes 14 and 15.

At 31 March 2013 \$44.77 million of deposits from customers relate to commercial paper issued by the Bank (31 March 2012 \$39.85 million). All commercial paper has a maturity of less than one year.

## Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

### 25 Contingent Liabilities and Credit Related Commitments

	BANKING GROUP			
	Contract or notional amt 31/3/13	Credit equivalent 31/3/13	Contract or notional amt 31/3/12	Credit equivalent 31/3/12
<b>Commitments</b>				
Commitments with uncertain drawdown	28,862	14,431	12,734	6,367
Commitments to extend credit which can be unconditionally cancelled	190,930	-	175,030	-
<b>Total credit related commitments</b>	<b>219,792</b>	<b>14,431</b>	<b>187,764</b>	<b>6,367</b>

	PARENT			
	Contract or notional amt 31/3/13	Credit equivalent 31/3/13	Contract or notional amt 31/3/12	Credit equivalent 31/3/12
<b>Commitments</b>				
Commitments with uncertain drawdown	33,565	16,783	27,544	13,772
Commitments to extend credit which can be unconditionally cancelled	190,930	-	175,030	-
<b>Total credit related commitments</b>	<b>224,495</b>	<b>16,783</b>	<b>202,574</b>	<b>13,772</b>

There are no material contingent liabilities.

### 26 Commitments

#### Lease Commitments

As at 31 March 2013 the value of the residual portion of lease commitments between Southland Building Society and its wholly owned subsidiary company, Fraser Properties Ltd was \$2.34 million (31 March 2012 \$2.22 million).

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Lease commitments payable after balance date:				
0-12 Months	2,254	2,295	2,005	2,016
12-24 Months	1,922	2,034	1,766	1,786
24-60 Months	3,421	3,986	3,302	3,567
>60 Months	2,246	3,034	1,430	1,818
	<b>9,843</b>	<b>11,349</b>	<b>8,503</b>	<b>9,187</b>

The Banking Group leases land and buildings under operating leases expiring from one to ten years. Leases generally provide the Banking Group with a right of renewal at which time all terms are renegotiated. There are no restrictions placed upon the lessee by entering into these leases.

### 27 Fair Value

The estimated fair value of the Banking Group's financial instruments is disclosed below. It is intended to provide an indication of the fair value of financial instruments and not the fair value of the Banking Group's business as a whole. It specifically excludes certain non-financial instruments and a range of intangible and relationship benefits which are integral to a full assessment of the Banking Group's financial position and the value of its business.

#### Methodologies

The methodologies and assumptions used when determining fair value depend on the terms and risk characteristics of the various instruments. The following methods have been used:

#### Cash on hand and at bank

These assets are short term in nature and the related carrying amount is equivalent to their fair value.

#### Funds with financial institutions

Funds with financial institutions are recognised in the financial statements as available for sale therefore carrying amount equals fair value. The fair values are based on market prices.

#### Investment securities

Investment securities are recognised in the financial statements as either fair value through profit or loss or available for sale, therefore carrying amount equals fair value. The fair values are based on quoted market prices.

#### Advances to customers

##### *Advances at amortised cost*

For variable rate advances the carrying amount is a reasonable estimate of fair value as they can be settled the following day at balance outstanding. For fixed rate advances fair values have been estimated using the discounted cash flow approach by reference to relative wholesale rates for the term at original fixing and the wholesale rate for the remaining term at balance date.

Advances include some interest free advances made in support of community projects. As at 31 March 2013 total interest free advances were \$nil (31 March 2012 \$0.06 million). These advances have been estimated using the discounted cash flow approach by reference to current rates at which similar advances would be made to other borrowers with a similar credit rating and the same remaining maturities. As at 31 March 2013 the fair value of these interest free advances as reported in the statement of financial position were \$nil (31 March 2012 \$0.06 million).

##### *Advances at fair value through profit or loss*

Designated advances are recognised in the financial statements at fair value through profit or loss, therefore carrying amount equals fair value. Fair value is based on valuation techniques including the use of a discounted cash flow model based on wholesale rates adjusted with a retail lending margin.

#### Redeemable shares, deposits and subordinated redeemable shares

The fair value of demand deposits is the amount payable on demand at the reporting date. For other liabilities with maturities of less than three months, the carrying amount is a reasonable estimate of fair value.

For liabilities with maturities of three months or longer, fair values have been based on quoted market prices, where such prices exist. Otherwise, fair values have been estimated using the discounted cash flow approach by reference to rates currently offered for similar liabilities of similar remaining maturities.

#### Derivative financial instruments

##### *Interest rate contracts*

Interest rate contracts are recognised in the financial statements at fair value, therefore carrying amount equals fair value.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate.

For unrecognised financial instruments which include financial guarantees and lending commitments, no secondary market exists, so no fair value can be calculated. The face value of these items are given in Notes 25 and 31.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 27 Fair Value continued

BANKING GROUP				
	31/3/13		31/3/12	
	Carrying amount	Fair value	Carrying amount	Fair value
<b>Financial assets</b>				
Cash on hand and at bank	21,801	21,801	22,474	22,474
Funds with financial institutions	144,490	144,490	90,980	90,980
Investment securities	400,233	400,233	265,733	265,733
Derivative financial instruments	2,396	2,396	2,789	2,789
Current tax assets	1,604	1,604	-	-
Advances to customers	2,225,753	2,228,653	2,425,723	2,429,492
Other assets	2,454	2,454	2,031	2,031
<b>Total financial assets</b>	<b>2,798,731</b>	<b>2,801,631</b>	<b>2,809,730</b>	<b>2,813,499</b>
<b>Financial liabilities</b>				
Redeemable shares	2,180,292	2,181,054	2,234,814	2,237,584
Deposits from customers	251,099	250,934	253,500	253,670
Due to other financial institutions	80,295	80,295	-	-
Derivative financial instruments	6,617	6,617	10,206	10,206
Current tax liabilities	-	-	93	93
Other borrowings	-	-	52,092	52,092
Other liabilities	10,367	10,367	6,762	6,762
Subordinated redeemable shares	61,232	63,363	61,242	63,894
<b>Total financial liabilities</b>	<b>2,589,902</b>	<b>2,592,630</b>	<b>2,618,709</b>	<b>2,624,301</b>

PARENT				
	31/3/13		31/3/12	
	Carrying amount	Fair value	Carrying amount	Fair value
<b>Financial assets</b>				
Cash on hand and at bank	18,790	18,790	17,413	17,413
Funds with financial institutions	137,241	137,241	85,825	85,825
Investment securities	397,595	397,595	262,848	262,848
Derivative financial instruments	2,614	2,614	3,756	3,756
Current tax assets	2,641	2,641	1,143	1,143
Advances to customers	2,116,771	2,119,671	2,262,510	2,266,182
Loans to subsidiaries	87,808	87,808	89,871	89,871
Other assets	2,025	2,025	4,572	4,572
<b>Total financial assets</b>	<b>2,765,485</b>	<b>2,768,385</b>	<b>2,727,938</b>	<b>2,731,610</b>
<b>Financial liabilities</b>				
Redeemable shares	2,185,716	2,186,478	2,239,547	2,242,317
Deposits from customers	251,099	250,934	253,500	253,670
Due to other financial institutions	80,295	80,295	-	-
Derivative financial instruments	6,617	6,617	10,259	10,259
Other borrowings	-	-	-	-
Other liabilities	4,172	4,172	3,924	3,924
Subordinated redeemable shares	61,232	63,363	61,242	63,894
<b>Total financial liabilities</b>	<b>2,589,131</b>	<b>2,591,859</b>	<b>2,568,472</b>	<b>2,574,064</b>



# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 27 Fair Value continued

The Banking Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

**Level 1:** Fair values are determined using quoted (unadjusted) prices in active markets for identical assets and liabilities;

**Level 2:** Fair values are determined using other techniques where all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

**Level 3:** Fair values are determined using techniques that use inputs which have a significant effect on the recorded fair value and are not based on observable market data.

	31/3/13			
BANKING GROUP	Level 1	Level 2	Level 3	Total
<b>Financial assets</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	2,396	-	2,396
Interest rate options	-	-	-	-
<b>Financial assets designated at fair value through profit or loss</b>				
Loans and advances to customers	-	-	6,121	6,121
NZ government securities	1,031	-	-	1,031
Equity securities	317	-	-	317
Managed funds	-	-	-	-
<b>Financial assets designated as available for sale</b>				
Call funds	39,234	-	-	39,234
Term deposits	-	105,256	-	105,256
Local authority bonds	-	101,731	-	101,731
Bank bonds	-	164,938	-	164,938
Other bonds	-	131,234	-	131,234
Equity securities	983	-	-	983
<b>Total financial assets</b>	<b>41,565</b>	<b>505,555</b>	<b>6,121</b>	<b>553,241</b>
<b>Financial liabilities</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	6,617	-	6,617
Interest rate options	-	-	-	-
<b>Total financial liabilities</b>	<b>-</b>	<b>6,617</b>	<b>-</b>	<b>6,617</b>
<b>PARENT</b>				
<b>Financial assets</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	2,614	-	2,614
Interest rate options	-	-	-	-
<b>Financial assets designated at fair value through profit or loss</b>				
Loans and advances to customers	-	-	6,121	6,121
<b>Financial assets designated as available for sale</b>				
Call funds	36,510	-	-	36,510
Term deposits	-	100,731	-	100,731
Local authority bonds	-	101,630	-	101,630
Bank bonds	-	164,938	-	164,938
Other bonds	-	131,027	-	131,027
<b>Total financial assets</b>	<b>36,510</b>	<b>500,940</b>	<b>6,121</b>	<b>543,571</b>
<b>Financial liabilities</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	6,617	-	6,617
Interest rate options	-	-	-	-
<b>Total financial liabilities</b>	<b>-</b>	<b>6,617</b>	<b>-</b>	<b>6,617</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 27 Fair Value continued

	31/3/12			
BANKING GROUP	Level 1	Level 2	Level 3	Total
<b>Financial assets</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	2,789	-	2,789
Interest rate options	-	-	-	-
<b>Financial assets designated at fair value through profit or loss</b>				
Loans and advances to customers	-	-	20,277	20,277
NZ government securities	1,112	-	-	1,112
Equity securities	313	-	-	313
Managed funds	-	673	-	673
<b>Financial assets designated as available for sale</b>				
Call funds	10,137	-	-	10,137
Term deposits	-	80,843	-	80,843
Local authority bonds	-	77,163	-	77,163
Bank bonds	-	129,252	-	129,252
Other bonds	-	56,534	-	56,534
Equity securities	687	-	-	687
<b>Total financial assets</b>	<b>12,249</b>	<b>347,254</b>	<b>20,277</b>	<b>379,780</b>
<b>Financial liabilities</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	10,206	-	10,206
Interest rate options	-	-	-	-
<b>Total financial liabilities</b>	<b>-</b>	<b>10,206</b>	<b>-</b>	<b>10,206</b>
<b>PARENT</b>				
<b>Financial assets</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	3,756	-	3,756
Interest rate options	-	-	-	-
<b>Financial assets designated at fair value through profit or loss</b>				
Loans and advances to customers	-	-	20,277	20,277
<b>Financial assets designated as available for sale</b>				
Call funds	9,001	-	-	9,001
Term deposits	-	76,824	-	76,824
Local authority bonds	-	77,062	-	77,062
Bank bonds	-	129,252	-	129,252
Other bonds	-	56,534	-	56,534
<b>Total financial assets</b>	<b>9,001</b>	<b>343,428</b>	<b>20,277</b>	<b>372,706</b>
<b>Financial liabilities</b>				
<b>Derivative financial instruments</b>				
Interest rate swaps	-	10,259	-	10,259
Interest rate options	-	-	-	-
<b>Total financial liabilities</b>	<b>-</b>	<b>10,259</b>	<b>-</b>	<b>10,259</b>

### Loans and advances designated at fair value through profit or loss

For loans and advances designated at fair value through profit or loss, a discounted cash flow model is used based on various assumptions, including prepayments and wholesale interest rates adjusted for retail lending margin. At balance date, a one basis point movement in retail margin or the underlying interest rate would impact the income statement by \$500 (31 March 2012 \$2,000).

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 27 Fair Value continued

The following table presents the changes in level 3 instruments:

	Note	BANKING GROUP		PARENT	
		31/3/13	31/3/12	31/3/13	31/3/12
<b>Loans and advances at fair value through profit or loss</b>					
Balance at beginning of the year		20,277	50,983	20,277	50,983
Total losses recorded in income statement	(6)	(278)	(194)	(278)	(194)
Loan repayments		(13,878)	(30,512)	(13,878)	(30,512)
Balance at end of the year		<b>6,121</b>	<b>20,277</b>	<b>6,121</b>	<b>20,277</b>

There were no transfers in or out of level 3, or between levels 1 and 2 during the year.

## 28 Liquidity Risk

Liquidity risk is the risk that the Banking Group will encounter difficulty in meeting commitments associated with its financial liabilities, e.g. overnight deposits, current accounts, maturing deposits, and future commitments such as loan draw-downs and guarantees.

The Banking Group has 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 Banking Group is subject to the RBNZ's liquidity requirements as set out in the RBNZ's "Liquidity Policy" (BS13/BS13A), which took effect from 1 April 2010.

Consistent with the requirements of the RBNZ's Liquidity Policy, liquidity risk is managed in the Banking Group on a cash flow mismatch and also core funding basis to ensure that the Banking Group exceeds RBNZ specified minimum standards for those metrics. This information is measured daily and reported to the Board monthly.

To meet both expected and unexpected patterns in operating cash flows the Banking Group maintains a stock of core liquid assets to adequately meet day-to-day operational requirements, a potential crisis, or 'funding stress' scenario.

Total liquidity includes committed but undrawn funding lines. As at 31 March 2013, the Banking Group had total committed funding lines with other registered banks of \$110 million (31 March 2012 \$85 million). Of these facilities, \$80 million were drawn down at 31 March 2013 (31 March 2012 \$nil).

The Banking Group also has an in-house residential mortgage backed security (RMBS) facility (the SBS Oreti Trust No. 2) that issues securities which can be used as collateral for borrowing from the RBNZ under its liquidity management arrangements. Whilst not intended to be used for standard daily liquidity requirements, this facility is available as contingent funding and accordingly core liquid assets includes this RMBS. The eligible RMBS collateral is discounted for the 'haircut'<sup>1</sup> that applies to those securities under the RBNZ's Domestic Operations for the purposes of those operations.

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Core liquid assets</b>				
Cash on hand and at bank	21,801	22,474	18,790	17,413
Funds with financial institutions	144,490	90,980	137,241	85,825
Investment securities	400,233	265,733	397,595	262,848
Committed and undrawn funding lines	30,000	85,000	30,000	85,000
Eligible RMBS collateral (less haircut <sup>1</sup> )	98,495	130,047	98,495	130,047
<b>Total liquidity</b>	<b>695,019</b>	<b>594,234</b>	<b>682,121</b>	<b>581,133</b>

<sup>1</sup> A "haircut" is a percentage that is subtracted from the par value of the assets that are being used as collateral. The size of the haircut reflects the perceived risk associated with holding the assets.

## Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

### 28 Liquidity Risk continued

The maturity profiles of assets and liabilities and loan commitments show the cash flows and have been prepared on both a contractual and undiscounted maturity basis as at balance date. These have been created using a run-off scenario which assumes no further origination of assets or liabilities.

The maturity profiles reflect the remaining period to contractual maturity of assets and liabilities as at balance date. This is not considered by the Banking Group to be in any way indicative of future cash flows. This is primarily because a significant proportion of the Banking Group's redeemable shares and deposits are renewed at maturity and therefore do not have a cash flow impact. Historical experience has shown that such balances are a stable source of funding for the Banking Group. The maturity profile has also been prepared on the basis of the agreed terms of the advance with the customer. However, SBS mortgages include a term giving SBS the ability to call mortgage advances which are repayable on demand, or repayable on three months notice of demand, at the Banking Group's discretion. While the Banking Group is not likely to call advances on demand the contractual maturity date is not indicative of future cash flows due to early repayments, further drawdowns and principal reductions.

The maturity profiles include interest cash flows expected to maturity. Note that the resulting undiscounted financial assets and liabilities do not reflect how the Bank or Banking Group manages its liquidity risk. As set out on the previous page, the Bank and Banking Group manages liquidity through the maintenance of a portfolio of liquid assets and committed funding lines and as such no expected maturity profile is presented.

#### Monetary assets receivable matched against liabilities payable as at 31 March 2013 (contractual cash flows including expected interest to maturity)

BANKING GROUP							
	On demand	0-6 Months	6-12 Months	12-24 Months	24-60 Months	> 60 Months	Total
<b>Assets</b>							
Cash on hand and at bank	21,801	-	-	-	-	-	21,801
Funds with financial institutions	39,238	83,746	21,292	-	-	214	144,490
Investment securities	1,299	16,773	29,720	84,745	182,481	85,215	400,233
Current tax assets	1,604	-	-	-	-	-	1,604
Advances to customers	17,554	103,085	74,295	100,396	205,909	1,724,514	2,225,753
Other assets	2,454	-	-	-	-	-	2,454
<b>Total assets</b>	<b>83,950</b>	<b>203,604</b>	<b>125,307</b>	<b>185,141</b>	<b>388,390</b>	<b>1,809,943</b>	<b>2,796,335</b>
Interest	684	80,605	74,832	124,793	427,408	791,945	1,500,267
<b>Total assets (inclusive of interest)</b>	<b>84,634</b>	<b>284,209</b>	<b>200,139</b>	<b>309,934</b>	<b>815,798</b>	<b>2,601,888</b>	<b>4,296,602</b>
<b>Liabilities</b>							
Redeemable shares	372,990	1,092,589	554,939	122,296	37,478	-	2,180,292
Deposits from customers	32,871	140,137	72,975	2,981	2,135	-	251,099
Due to other financial institutions	-	-	-	-	-	80,295	80,295
Current tax liabilities	-	-	-	-	-	-	-
Other borrowings	-	-	-	-	-	-	-
Other liabilities	10,367	-	-	-	-	-	10,367
Subordinated redeemable shares	-	-	42,225	17,082	1,925	-	61,232
<b>Total liabilities</b>	<b>416,228</b>	<b>1,232,726</b>	<b>670,139</b>	<b>142,359</b>	<b>41,538</b>	<b>80,295</b>	<b>2,583,285</b>
Interest	71	13,728	22,731	14,236	15,435	2,891	69,092
<b>Total liabilities (inclusive of interest)</b>	<b>416,299</b>	<b>1,246,454</b>	<b>692,870</b>	<b>156,595</b>	<b>56,973</b>	<b>83,186</b>	<b>2,652,377</b>
<b>Derivatives</b>							
Net derivative cash flows	-	(1,778)	(1,723)	(1,763)	442	786	(4,036)
<b>Unrecognised loan commitments</b>	<b>28,862</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>28,862</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 28 Liquidity Risk continued

Monetary assets receivable matched against liabilities payable as at 31 March 2013  
(contractual cash flows including expected interest to maturity)

	PARENT						Total
	On demand	0-6 Months	6-12 Months	12-24 Months	24-60 Months	> 60 Months	
<b>Assets</b>							
Cash on hand and at bank	18,790	-	-	-	-	-	18,790
Funds with financial institutions	36,510	80,696	20,035	-	-	-	137,241
Investment securities	-	16,672	29,720	84,745	181,449	85,009	397,595
Current tax assets	2,641	-	-	-	-	-	2,641
Advances to customers	17,554	96,747	54,591	62,733	160,733	1,724,413	2,116,771
Loans to subsidiaries	-	-	-	87,808	-	-	87,808
Other assets	2,025	-	-	-	-	-	2,025
<b>Total assets</b>	<b>77,520</b>	<b>194,115</b>	<b>104,346</b>	<b>235,286</b>	<b>342,182</b>	<b>1,809,422</b>	<b>2,762,871</b>
Interest	666	83,150	77,403	130,074	427,193	791,859	1,510,345
<b>Total assets (inclusive of interest)</b>	<b>78,186</b>	<b>277,265</b>	<b>181,749</b>	<b>365,360</b>	<b>769,375</b>	<b>2,601,281</b>	<b>4,273,216</b>
<b>Liabilities</b>							
Redeemable shares	378,414	1,092,589	554,939	122,296	37,478	-	2,185,716
Deposits from customers	32,871	140,137	72,975	2,981	2,135	-	251,099
Due to other financial institutions	-	-	-	-	-	80,295	80,295
Current tax liabilities	-	-	-	-	-	-	-
Other borrowings	-	-	-	-	-	-	-
Other liabilities	4,172	-	-	-	-	-	4,172
Subordinated redeemable shares	-	-	42,225	17,082	1,925	-	61,232
<b>Total liabilities</b>	<b>415,457</b>	<b>1,232,726</b>	<b>670,139</b>	<b>142,359</b>	<b>41,538</b>	<b>80,295</b>	<b>2,582,514</b>
Interest	71	13,728	22,731	14,236	15,435	2,891	69,092
<b>Total liabilities (inclusive of interest)</b>	<b>415,528</b>	<b>1,246,454</b>	<b>692,870</b>	<b>156,595</b>	<b>56,973</b>	<b>83,186</b>	<b>2,651,606</b>
<b>Derivatives</b>							
Net derivative cash flows	118	(1,560)	(1,696)	(1,754)	444	786	(3,662)
<b>Unrecognised loan commitments</b>	<b>33,565</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>33,565</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 28 Liquidity Risk *continued*

Monetary assets receivable matched against liabilities payable as at 31 March 2012  
(contractual cash flows including expected interest to maturity)

BANKING GROUP							
	On demand	0-6 Months	6-12 Months	12-24 Months	24-60 Months	> 60 Months	Total
<b>Assets</b>							
Cash on hand and at bank	22,474	-	-	-	-	-	22,474
Funds with financial institutions	10,646	69,762	10,358	-	-	214	90,980
Investment securities	1,672	-	2,050	41,932	207,318	12,761	265,733
Advances to customers	18,999	161,884	91,298	138,477	191,855	1,823,210	2,425,723
Other assets	2,031	-	-	-	-	-	2,031
<b>Total assets</b>	<b>55,822</b>	<b>231,646</b>	<b>103,706</b>	<b>180,409</b>	<b>399,173</b>	<b>1,836,185</b>	<b>2,806,941</b>
Interest	536	93,322	89,010	175,398	492,852	769,589	1,620,707
<b>Total assets (inclusive of interest)</b>	<b>56,358</b>	<b>324,968</b>	<b>192,716</b>	<b>355,807</b>	<b>892,025</b>	<b>2,605,774</b>	<b>4,427,648</b>
<b>Liabilities</b>							
Redeemable shares	357,700	1,143,755	529,293	168,570	35,496	-	2,234,814
Deposits from customers	43,225	173,048	27,323	7,842	2,062	-	253,500
Current tax liabilities	93	-	-	-	-	-	93
Other borrowings	-	-	-	-	-	52,092	52,092
Other liabilities	6,762	-	-	-	-	-	6,762
Subordinated redeemable shares	-	-	-	42,233	19,009	-	61,242
<b>Total liabilities</b>	<b>407,780</b>	<b>1,316,803</b>	<b>556,616</b>	<b>218,645</b>	<b>56,567</b>	<b>52,092</b>	<b>2,608,503</b>
Interest	63	24,241	8,515	18,031	14,908	49,307	115,065
<b>Total liabilities (inclusive of interest)</b>	<b>407,843</b>	<b>1,341,044</b>	<b>565,131</b>	<b>236,676</b>	<b>71,475</b>	<b>101,399</b>	<b>2,723,568</b>
<b>Derivatives</b>							
Net derivative cash flows	-	(3,348)	(2,299)	(1,824)	(826)	-	(8,297)
<b>Unrecognised loan commitments</b>	<b>12,734</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>12,734</b>

## Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

### 28 Liquidity Risk continued

Monetary assets receivable matched against liabilities payable as at 31 March 2012  
(contractual cash flows including expected interest to maturity)

	PARENT						Total
	On demand	0-6 Months	6-12 Months	12-24 Months	24-60 Months	> 60 Months	
<b>Assets</b>							
Cash on hand and at bank	17,413	-	-	-	-	-	17,413
Funds with financial institutions	9,000	66,718	10,107	-	-	-	85,825
Investment securities	-	-	2,049	41,832	206,206	12,761	262,848
Current tax assets	1,143	-	-	-	-	-	1,143
Advances to customers	18,999	153,456	71,724	90,999	143,396	1,783,936	2,262,510
Loans to subsidiaries	-	-	-	89,871	-	-	89,871
Other assets	4,572	-	-	-	-	-	4,572
<b>Total assets</b>	<b>51,127</b>	<b>220,174</b>	<b>83,880</b>	<b>222,702</b>	<b>349,602</b>	<b>1,796,697</b>	<b>2,724,182</b>
Interest	524	95,952	91,523	179,502	494,204	808,517	1,670,222
<b>Total assets (inclusive of interest)</b>	<b>51,651</b>	<b>316,126</b>	<b>175,403</b>	<b>402,204</b>	<b>843,806</b>	<b>2,605,214</b>	<b>4,394,404</b>
<b>Liabilities</b>							
Redeemable shares	362,433	1,143,755	529,293	168,570	35,496	-	2,239,547
Deposits from customers	43,225	173,048	27,323	7,842	2,062	-	253,500
Other borrowings	-	-	-	-	-	-	-
Other liabilities	3,924	-	-	-	-	-	3,924
Subordinated redeemable shares	-	-	-	42,233	19,009	-	61,242
<b>Total liabilities</b>	<b>409,582</b>	<b>1,316,803</b>	<b>556,616</b>	<b>218,645</b>	<b>56,567</b>	<b>-</b>	<b>2,558,213</b>
Interest	45	12,876	18,473	16,624	10,688	-	58,706
<b>Total liabilities (inclusive of interest)</b>	<b>409,627</b>	<b>1,329,679</b>	<b>575,089</b>	<b>235,269</b>	<b>67,255</b>	<b>-</b>	<b>2,616,919</b>
<b>Derivatives</b>							
Net derivative cash flows	-	(2,879)	(1,926)	(1,693)	(863)	-	(7,361)
<b>Unrecognised loan commitments</b>	<b>27,544</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>27,544</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 29 Credit Risk Exposure

The nature of SBS's activities as a financial intermediary necessitates SBS dealing in financial instruments that contain an inherent element of credit risk. Credit exposure means the amount of the maximum loss that SBS could incur as a result of the counterparty to a contract failing to discharge its obligations, without taking into account the value of collateral, guarantees, indemnities, other support arrangements and any potential recoveries. SBS's activities are conducted within the bounds of prudent and conservative banking practice.

The Banking Group's dominant activity is the provision of residential mortgage finance which comprises 73% (31 March 2012 72%) of the Banking Group's loan portfolio and is undertaken throughout New Zealand. Rural loans which comprise 15% (31 March 2012 15%) of the Banking Group's loan portfolio are predominantly concentrated in the Southland/Otago region.

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>(a) The maximum exposures to credit risk at the relevant reporting dates are:</b>				
Cash on hand and at bank	21,801	22,474	18,790	17,413
Funds with financial institutions	144,490	90,980	137,241	85,825
Investment securities	400,233	265,733	397,595	262,848
Derivative financial instruments	2,396	2,789	2,614	3,756
Current tax assets	1,604	-	2,641	1,143
Advances to customers	2,225,753	2,425,723	2,116,771	2,262,510
Loans to subsidiaries	-	-	87,808	89,871
Other assets	2,454	2,031	2,025	4,572
<b>Total on-balance sheet credit exposures</b>	<b>2,798,731</b>	<b>2,809,730</b>	<b>2,765,485</b>	<b>2,727,938</b>
<b>(b) Concentrations of credit risk by sector</b>				
Residential	1,372,920	1,460,486	1,372,920	1,424,334
Residential investing	257,385	283,304	257,385	273,868
Agricultural	326,763	372,572	326,763	372,572
Commercial finance	2,525	3,525	87,808	89,871
Commercial other	161,597	198,768	159,458	191,476
Consumer lending	104,318	106,808	-	-
Local authority	101,976	77,423	101,875	77,322
Corporate investments	467,189	304,813	454,610	292,780
Other	4,058	2,031	4,666	5,715
<b>Total concentrations of credit risk by sector</b>	<b>2,798,731</b>	<b>2,809,730</b>	<b>2,765,485</b>	<b>2,727,938</b>
<b>(c) Concentrations of credit risk by geographical location</b>				
North Island	1,022,127	911,249	925,132	818,404
Canterbury	565,853	608,279	555,292	568,394
Otago	521,801	547,017	517,697	534,858
Southland	505,153	520,518	586,440	605,571
South Island other	183,797	222,667	180,924	200,711
Overseas	-	-	-	-
<b>Total concentrations of credit risk by geographical location</b>	<b>2,798,731</b>	<b>2,809,730</b>	<b>2,765,485</b>	<b>2,727,938</b>

### (d) Currency risk

The Banking Group is not exposed to currency risk.



# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 29 Credit Risk Exposure continued

### (e) Credit exposures to individual counterparties and groups of closely related counterparties

The Banking Group's disclosure of concentrations of credit exposure to individual counterparties and groups of closely related counterparties, which equalled or exceeded 10% of the Banking Group's equity, is based on actual credit exposures and calculated on a gross basis (net of specific provisions). Credit exposures to the central government of any country with a long term credit rating of A- or A3 or above, or its equivalent, banks with a long term credit rating of A- or A3 or above, or its equivalent, and connected persons are excluded. Peak end of day credit exposures to individual counterparties are calculated over the last quarter using the Banking Group's end of period equity.

End of Period Exposure	31 March 2013			31 March 2012		
	Number of Non Bank Counterparties			Number of Non Bank Counterparties		
Percentage of equality	"A" Rated	"B" Rated	Total	"A" Rated	"B" Rated	Total
10%-14%	1	-	1	-	-	-
15%-19%	2	-	2	-	-	-
20%-24%	-	-	-	-	-	-
Total	3	-	3	-	-	-

#### Peak Exposure

Percentage of equality	"A" Rated	"B" Rated	Total	"A" Rated	"B" Rated	Total
10%-14%	1	-	1	-	-	-
15%-19%	2	-	2	-	-	-
20%-24%	-	-	-	-	-	-
Total	3	-	3	-	-	-

Note:

"A" Rated - those counterparties that have a long term credit rating of A- or A3 or above

"B" Rated - those counterparties that have a long term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent

There were no peak or balance date credit exposures to bank counterparties with a credit rating below A- or A3, or its equivalent, which exceeded 10% of the Banking Group's equity for the three months ended 31 March 2013.

### (f) Credit exposures to connected persons

Credit exposure concentrations are disclosed on the basis of actual credit exposures and calculated on a gross basis (net of individual credit impairment allowances and excluding advances of a capital nature). The Banking Group does not have credit exposures to connected persons other than non-bank connected persons. Peak end of day credit exposures to non-bank connected persons have been calculated using the Banking Group's tier 1 capital at the end of the period. The rating-contingent limit, which is applicable to the Banking Group, based on the conditions of registration imposed by the RBNZ is 15%. There have been no rating-contingent limit changes during the last year. Within the rating-contingent limit there is a sub-limit of 15%, which applies to non-bank connected persons. All limits on aggregate credit exposure to all connected persons and non-bank connected persons in the Banking Group's conditions of registration have been complied with at all times over the last year. There are no individual credit impairment allowances against credit exposures to non-bank connected persons as at 31 March 2013 (31 March 2012 \$nil).

	BANKING GROUP	
	31/3/13	31/3/12
Credit exposures to non-bank connected persons at year end	477	538
Credit exposures to non-bank connected persons at period end expressed as a % of total tier 1 capital	0.21%	0.25%
Peak credit exposures to non-bank connected persons during the quarter	492	804
Peak credit exposures to non-bank connected persons during the quarter expressed as a % of total tier 1 capital	0.22%	0.37%

(g) Percentage of borrowers owing the six largest amounts	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
The six largest borrowers as a percentage of monetary assets receivable	1.76%	2.01%	4.72%	5.09%

(h) Monetary assets with arrears	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Monetary assets receivable with repayments in arrears in excess of three months	0.50%	1.16%	0.50%	1.19%

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 29 Credit Risk Exposure continued

### (i) Collateral held

SBS takes collateral where it is considered necessary to support credit risk on financial instruments including both recognised and unrecognised financial instruments. An evaluation is undertaken of the customer's credit risk on a case by case basis and the amount of collateral taken if deemed necessary, is based on management's credit evaluation of the counterparty. The collateral taken varies but could include cash deposits, mortgages, debentures, investments and financial covenants.

In terms of SBS retail lending activity, credit is extended within predetermined loan to security valuation ratios, which vary depending on the class of an advance, and within established and proven repayment to income ratios. Independent credit evaluations are undertaken where this is deemed necessary. Additionally some advances are insured with an independent third party mortgage insurer. In excess of 95% of SBS advances are secured by first mortgage over real property as a minimum. Once established, loan performance is monitored regularly. The debt management team monitor exposures to non-performing loans on a daily basis and provide monthly reports to senior management and the board.

Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired.

An estimate of the fair value of collateral and other security enhancements held against financial assets that are individually impaired or past due are shown below:

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Against individually impaired property	10,627	22,542	10,627	22,542
Against past due but not impaired property	54,812	85,291	54,515	83,067
	<b>65,439</b>	<b>107,833</b>	<b>65,142</b>	<b>105,609</b>

## 30 Market Risk

Market risk is the risk that changes in market prices, such as interest rate, and credit spreads will affect the Banking Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

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

The Banking Group's exposure to market risk is managed operationally by Treasury. Treasury manages market risk by using appropriate risk management instruments. Market risk is managed within a clearly defined framework of policy limits. Treasury reports to and is represented on the ALCO.

Market risk is measured and reported using a variety of techniques, according to the appropriateness of the technique to the exposure concerned. The techniques used include interest rate gap analysis, scenario analysis and Value at Risk (VaR).

### Policies for Managing Interest Rate Risk

Interest rate risk is the risk of loss to the Banking Group arising from adverse changes in interest rates. The Banking Group is exposed to interest rate risk in respect of the following activities: borrowing from and lending to customers, investing in physical money market instruments as well as derivatives such as interest rate contracts used for risk management purposes. Changes in interest rates can impact the Banking Group's financial results by affecting the spread earned on interest earning assets and interest paying liabilities and impacting on the market value of other financial instruments held.

Exposure to interest rate risk is measured primarily through the analysis of repricing maturities of the Banking Group's assets, liabilities and unrecognised financial instruments. Exposure to interest rate risk is also measured, managed and monitored using VaR, scenario analysis (to a 1% shock) and interest rate sensitivity gap. Exposures are monitored continuously and reported to the board on a monthly basis.

Effective interest rates on risk management transactions within classes of financial assets or liabilities are disclosed exclusive of the impact of the derivative transaction. The financial assets or liabilities carrying values do not incorporate the values of the derivative transactions.

The interest rate repricing schedule reflects statement of financial position financial assets and liabilities and has been prepared on the basis of the next repricing date.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 30 Market Risk continued

The following schedule details the Banking Group's interest rate repricing profile:

BANKING GROUP							
As at 31 March 2013	Less than 3 Months	3-6 Months	6-12 Months	12-24 Months	>24 Months	Non- interest sensitive	Total
<b>Assets</b>							
Cash on hand and at bank	21,801	-	-	-	-	-	21,801
Funds with financial institutions	111,196	11,788	21,292	-	214	-	144,490
Investment securities	117,160	-	29,719	64,541	188,813	-	400,233
Derivative financial instruments	-	-	-	-	-	2,396	2,396
Current tax assets	-	-	-	-	-	1,604	1,604
Advances to customers	1,485,062	155,964	207,012	232,372	145,343	-	2,225,753
Other assets	-	-	-	-	-	33,392	33,392
	<b>1,735,219</b>	<b>167,752</b>	<b>258,023</b>	<b>296,913</b>	<b>334,370</b>	<b>37,392</b>	<b>2,829,669</b>
<b>Liabilities and equity</b>							
Redeemable shares	957,955	507,624	554,939	122,296	37,478	-	2,180,292
Deposits from customers	126,700	46,308	72,975	2,981	2,135	-	251,099
Due to other financial institutions	80,295	-	-	-	-	-	80,295
Derivative financial instruments	-	-	-	-	-	6,617	6,617
Other liabilities	-	-	-	-	-	18,544	18,544
Subordinated redeemable shares	-	-	42,225	17,082	1,925	-	61,232
Equity	-	-	-	-	-	231,590	231,590
	<b>1,164,950</b>	<b>553,932</b>	<b>670,139</b>	<b>142,359</b>	<b>41,538</b>	<b>256,751</b>	<b>2,829,669</b>
On-balance sheet interest sensitivity gap	570,269	(386,180)	(412,116)	154,554	292,832	(219,359)	-
Net balance of derivative financial instruments	288,500	196,250	(91,000)	(184,000)	(209,750)	-	-
<b>Total interest rate sensitivity gap</b>	<b>858,769</b>	<b>(189,930)</b>	<b>(503,116)</b>	<b>(29,446)</b>	<b>83,082</b>	<b>(219,359)</b>	<b>-</b>

PARENT							
<b>Assets</b>							
Cash on hand and at bank	18,790	-	-	-	-	-	18,790
Funds with financial institutions	107,196	10,010	20,035	-	-	-	137,241
Investment securities	115,553	-	29,719	64,541	187,782	-	397,595
Derivative financial instruments	-	-	-	-	-	2,614	2,614
Current tax assets	-	-	-	-	-	2,641	2,641
Advances to customers	1,483,131	151,558	187,308	194,708	100,066	-	2,116,771
Loans to subsidiaries	87,808	-	-	-	-	-	87,808
Other assets	-	-	-	-	-	38,456	38,456
	<b>1,812,478</b>	<b>161,568</b>	<b>237,062</b>	<b>259,249</b>	<b>287,848</b>	<b>43,711</b>	<b>2,801,916</b>
<b>Liabilities and equity</b>							
Redeemable shares	963,379	507,624	554,939	122,296	37,478	-	2,185,716
Deposits from customers	126,700	46,308	72,975	2,981	2,135	-	251,099
Due to other financial institutions	80,295	-	-	-	-	-	80,295
Derivative financial instruments	-	-	-	-	-	6,617	6,617
Other liabilities	-	-	-	-	-	6,654	6,654
Subordinated redeemable shares	-	-	42,225	17,082	1,925	-	61,232
Equity	-	-	-	-	-	210,303	210,303
	<b>1,170,374</b>	<b>553,932</b>	<b>670,139</b>	<b>142,359</b>	<b>41,538</b>	<b>223,574</b>	<b>2,801,916</b>
On-balance sheet interest sensitivity gap	642,104	(392,364)	(433,077)	116,890	246,310	(179,863)	-
Net balance of derivative financial instruments	307,803	189,172	(98,365)	(189,533)	(209,077)	-	-
<b>Total interest rate sensitivity gap</b>	<b>949,907</b>	<b>(203,192)</b>	<b>(531,442)</b>	<b>(72,643)</b>	<b>37,233</b>	<b>(179,863)</b>	<b>-</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 30 Market Risk continued

BANKING GROUP							
As at 31 March 2012	Less than 3 Months	3-6 Months	6-12 Months	12-24 Months	>24 Months	Non- interest sensitive	Total
<b>Assets</b>							
Cash on hand and at bank	22,474	-	-	-	-	-	22,474
Funds with financial institutions	78,888	1,520	10,358	-	214	-	90,980
Investment securities	69,958	-	2,049	41,832	151,894	-	265,733
Derivative financial instruments	-	-	-	-	-	2,789	2,789
Advances to customers	1,727,152	136,842	170,856	294,964	95,909	-	2,425,723
Other assets	-	-	-	-	-	34,197	34,197
	<b>1,898,472</b>	<b>138,362</b>	<b>183,263</b>	<b>336,796</b>	<b>248,017</b>	<b>36,986</b>	<b>2,841,896</b>
<b>Liabilities and equity</b>							
Redeemable shares	831,811	669,644	529,293	168,570	35,496	-	2,234,814
Deposits from customers	174,743	41,530	27,323	7,842	2,062	-	253,500
Due to other financial institutions	-	-	-	-	-	-	-
Derivative financial instruments	-	-	-	-	-	10,206	10,206
Current tax liabilities	-	-	-	-	-	93	93
Other borrowings	-	52,092	-	-	-	-	52,092
Other liabilities	-	-	-	-	-	14,588	14,588
Subordinated redeemable shares	-	-	-	42,233	19,009	-	61,242
Equity	-	-	-	-	-	215,361	215,361
	<b>1,006,554</b>	<b>763,266</b>	<b>556,616</b>	<b>218,645</b>	<b>56,567</b>	<b>240,248</b>	<b>2,841,896</b>
On-balance sheet interest sensitivity gap	891,918	(624,904)	(373,353)	118,151	191,450	(203,262)	-
Net balance of derivative financial instruments	157,000	49,750	32,000	(93,000)	(145,750)	-	-
<b>Total interest rate sensitivity gap</b>	<b>1,048,918</b>	<b>(575,154)</b>	<b>(341,353)</b>	<b>25,151</b>	<b>45,700</b>	<b>(203,262)</b>	<b>-</b>

PARENT							
<b>Assets</b>							
Cash on hand and at bank	17,413	-	-	-	-	-	17,413
Funds with financial institutions	75,718	-	10,107	-	-	-	85,825
Investment securities	68,185	-	2,049	41,832	150,782	-	262,848
Derivative financial instruments	-	-	-	-	-	3,756	3,756
Current tax assets	-	-	-	-	-	1,143	1,143
Advances to customers	1,690,115	128,693	149,126	244,205	50,371	-	2,262,510
Loans to subsidiaries	89,871	-	-	-	-	-	89,871
Other assets	-	-	-	-	-	41,388	41,388
	<b>1,941,302</b>	<b>128,693</b>	<b>161,282</b>	<b>286,037</b>	<b>201,153</b>	<b>46,287</b>	<b>2,764,754</b>
<b>Liabilities and equity</b>							
Redeemable shares	831,811	674,377	529,293	168,570	35,496	-	2,239,547
Deposits from customers	174,743	41,530	27,323	7,842	2,062	-	253,500
Due to other financial institutions	-	-	-	-	-	-	-
Derivative financial instruments	-	-	-	-	-	10,259	10,259
Other liabilities	-	-	-	-	-	6,317	6,317
Subordinated redeemable shares	-	-	-	42,233	19,009	-	61,242
Equity	-	-	-	-	-	193,889	193,889
	<b>1,006,554</b>	<b>715,907</b>	<b>556,616</b>	<b>218,645</b>	<b>56,567</b>	<b>210,465</b>	<b>2,764,754</b>
On-balance sheet interest sensitivity gap	934,748	(587,214)	(395,334)	67,392	144,586	(164,178)	-
Net balance of derivative financial instruments	206,303	52,672	24,635	(128,533)	(155,077)	-	-
<b>Total interest rate sensitivity gap</b>	<b>1,141,051</b>	<b>(534,542)</b>	<b>(370,699)</b>	<b>(61,141)</b>	<b>(10,491)</b>	<b>(164,178)</b>	<b>-</b>

## Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

### 30 Market Risk *continued*

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Banking Group's financial assets and liabilities to various standard interest rate scenarios. The Banking Group's market risk model determines the mismatch between assets and liabilities after taking derivatives into account. The present value of the mismatched cash flows are discounted using the current yield curve at period end and the assessed most probable scenarios as well as a 100 basis point (bp) parallel rise or fall in the New Zealand yield curve. The difference in the present value of the scenario and the present value of the current yield curve are identified for each of the scenarios. Differences between equity and profit and loss are a result of interest rate derivatives designated in cash flow relationships which have most of the fair value movements in the derivatives taken directly to the cash flow hedge reserve in equity. An analysis of the Banking Group's sensitivity to an increase or decrease in market interest rates is as follows:

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>Impact on equity of increase or decrease to market interest rates</b>				
100 bp parallel increase	1,281	(53)	1,043	(828)
100 bp parallel decrease	(1,771)	(194)	(1,528)	599
<b>Impact on profit and loss of increase or decrease to market interest rates</b>				
100 bp parallel increase	(61)	(265)	(61)	(386)
100 bp parallel decrease	62	269	62	393

### 31 Capital Adequacy

The Banking Group's objectives in relation to the management of capital adequacy are to comply at all times with the regulatory capital requirements set out by the Reserve Bank of New Zealand (RBNZ); to maintain a strong capital base to cover the inherent risks of the business and maintain a targeted credit rating; and to support future business development and growth.

The Banking Group is subject to regulation by the RBNZ. The RBNZ has set minimum regulatory capital requirements for banks that are consistent with the internationally agreed framework developed by the Basel Committee on Banking Supervision. These requirements define what is acceptable as capital and provide for methods of measuring the risks incurred by the Banking Group. The Banking Group must comply with RBNZ minimum capital adequacy ratios as determined in its Conditions of Registration which are as follows:

- Total capital ratio of the banking group is not less than 8%;
- Tier 1 capital ratio of the banking group is not less than 6%;
- Common equity tier 1 capital ratio of the banking group is not less than 4.5%;
- Total capital of the banking group is not less than NZ \$30 million.

For regulatory purposes, capital comprises two elements, eligible tier 1 and tier 2 capital, from which certain deductions are made to arrive at regulatory tier 1 and tier 2 capital as documented in the RBNZ's "Capital Adequacy Framework (Standardised Approach)" document (BS2A). Tier 1 capital is divided into two levels. Common equity tier 1 capital consists of retained profits, revenue and similar reserves, less intangible assets, deferred tax assets, cash flow hedge reserve and certain other deductions. Additional tier 1 capital consists of eligible non-controlling interests net of certain deductions. Tier 2 capital includes term subordinated debt and the property, plant and equipment revaluation reserve. The tangible element of investments in subsidiaries that are not wholly owned or funded is deducted from the sum of tier one and tier two capital to arrive at total regulatory capital.

Regulatory capital adequacy ratios are calculated by expressing capital as a percentage of risk weighted assets. Risk weighted assets are derived by assigning risk weight percentages to certain material risk categories of exposures. These exposures are measured or estimated from selected balance sheet assets and off balance sheet exposures and market contracts. It should be noted that the regulatory risk weightings may not necessarily be consistent with the loss experience of the Banking Group.

The Banking Group has adopted the Basel III "standardised approach" as per BS2A to calculate regulatory capital requirements from 1 January 2013. Prior periods were calculated under the Basel II methodology. Basel III consists of 3 pillars - Pillar One covers the capital requirements for banks for credit, operational, and market risks. Pillar Two covers all other material risks not already included in Pillar One, and Pillar Three relates to market disclosure.

The Board of Directors has ultimate responsibility for capital adequacy, approves capital policy and establishes minimum internal capital levels and limits. These are typically higher than the regulatory minimum.

The capital adequacy calculations summarise the composition of regulatory capital and capital adequacy ratios. For the purposes of calculating the capital adequacy ratios for the Registered Bank, wholly-owned and wholly-funded subsidiaries of the Banking Group are consolidated with the Registered Bank. In this context, wholly funded by the Registered Bank means that there are no liabilities (including off-balance sheet obligations) to anyone other than the Registered Bank, the Inland Revenue Department, and trade creditors, where aggregate exposure to trade creditors does not exceed 5% of the subsidiary's equity. Wholly owned means that all the equity issued by the subsidiary is held by the Registered Bank.

During the periods shown the Banking Group fully complied with all RBNZ capital requirements as set out in the relevant Banking Group's conditions of registration.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 31 Capital Adequacy continued

		BANKING GROUP		REGISTERED BANK	
		Unaudited 31/03/13	Unaudited 31/03/12	Unaudited 31/03/13	Unaudited 31/03/12
	Minimum ratio requirement				
<b>Regulatory capital ratios</b>					
Common equity tier I capital ratio	4.50%	13.13%	-	12.70%	-
Tier I capital ratio	6.00%	13.34%	12.52%	12.70%	11.83%
Total capital ratio	8.00%	14.34%	14.35%	13.24%	13.12%
Buffer ratio	2.50%	8.63%			

The regulatory capital ratios for the year ended 31 March 2013 are calculated under the Basel III "standardised approach". The 31 March 2012 comparative period ratios are calculated under the Basel II methodology. Note that some items of capital cannot be compared as they have been adjusted and/or reallocated in the 2013 year in accordance with the new Basel III methodology.

	BANKING GROUP	
	Unaudited 31/3/13	Unaudited 31/3/12
<b>(i) Qualifying capital</b>		
<b>Tier I capital</b>		
<b>Common equity tier I (CETI) capital</b>		
Retained earnings	210,667	201,447
Current year's retained earnings	11,733	9,220
Available for sale assets reserve	4,803	-
Cash flow hedging reserve	(2,726)	(5,258)
<b>Less deductions from CETI capital</b>		
Intangible assets	(3,320)	(2,466)
Deferred tax assets	(5,284)	-
Cash flow hedging reserve	2,726	5,258
<b>Total CETI capital</b>	<b>218,599</b>	
<b>Additional tier I (ATI) capital</b>		
Non-controlling interests (net of deductions and surplus ATI capital)	3,382	6,887
<b>Total ATI capital</b>	<b>3,382</b>	
<b>Total tier I capital</b>	<b>221,981</b>	<b>215,088</b>
<b>Tier 2 capital</b>		
Revaluation reserves	454	3,065
Subordinated redeemable shares	16,289	28,409
<b>Total tier 2 capital</b>	<b>16,743</b>	<b>31,474</b>
<b>Total capital</b>	<b>238,724</b>	<b>246,562</b>

The subordinated redeemable shares recognised within Tier 2 capital are subject to phase-out from Tier 2 capital under the RBNZ's Basel III transitional arrangements. As such, recognition of these instruments will be capped at 80% of \$25.2m, being the nominal amount outstanding at 1 January 2013, with this reducing to 60% from 1 January 2015 and 40% from 1 January 2016. Further information on this capital instrument is included in Note 21.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 31 Capital Adequacy continued

### (ii) Total risk weighted assets

BANKING GROUP						
	Total exposure after credit risk mitigation		Risk weighting	Risk weighted exposure	Minimum pillar one capital requirement	
	Unaudited 31/3/13		Unaudited 31/3/13	Unaudited 31/3/13	Unaudited 31/3/13	
<b>On balance sheet credit exposures</b>						
Cash	589		0%	-	-	
Sovereigns and central banks	1,031		0%	-	-	
Public sector entities	101,731		20%	20,346	1,628	
Banks	330,957		20%	66,191	5,295	
Corporates (rating grade 1)	59,956		20%	11,991	959	
Corporates (rating grade 2)	51,290		50%	25,645	2,052	
Corporates (rating grade 3)	19,988		100%	19,988	1,599	
Residential mortgages < 80% loan to value ratio (LVR)	1,235,850		35%	432,548	34,604	
Residential mortgages 80 < 90% LVR	109,693		50%	54,847	4,388	
Residential mortgages 90 < 100% LVR	27,257		75%	20,443	1,635	
Residential mortgages welcome home loans	255,265		50%	127,633	10,211	
Past due residential mortgages	1,207		100%	1,207	97	
Impaired residential mortgages	1,032		100%	1,032	83	
Equity holdings	983		300%	2,949	236	
Other assets	631,211		100%	631,211	50,497	
Non-risk weighted assets	1,629		0%	-	-	
<b>Total on balance sheet credit exposures</b>	<b>2,829,669</b>			<b>1,416,031</b>	<b>113,284</b>	
	Total exposure after credit risk mitigation	Credit conversion factor	Credit equivalent amount	Average risk weighting	Risk weighted exposure / implied risk weighted exposure	Minimum pillar one capital requirement
	Unaudited 31/3/13	Unaudited 31/3/13	Unaudited 31/3/13	Unaudited 31/3/13	Unaudited 31/3/13	Unaudited 31/3/13
<b>Off balance sheet credit exposures</b>						
Commitments with uncertain drawdown	28,862	50%	14,431	63%	9,146	732
Commitments to extend credit which can be unconditionally cancelled	190,930	0%	-	0%	-	-
<b>Market related contracts<sup>1</sup></b>						
Interest rate contracts	846,618	n/a	6,731	20%	1,346	108
Credit valuation adjustment (CVA)					167	13
<b>Total off balance sheet credit exposures</b>	<b>1,066,410</b>		<b>21,162</b>		<b>10,659</b>	<b>853</b>
<b>Total credit risk</b>	<b>3,896,079</b>		<b>21,162</b>		<b>1,426,690</b>	<b>114,137</b>
<b>Operational risk</b>	n/a				<b>174,923</b>	<b>13,994</b>
<b>Market risk</b>	n/a				<b>62,907</b>	<b>5,033</b>
<b>Total risk weighted assets</b>	<b>3,896,079</b>				<b>1,664,520</b>	<b>133,164</b>

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

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 31 Capital Adequacy continued

BANKING GROUP					
	Total exposure after credit risk mitigation		Risk weighting	Risk weighted exposure	Minimum pillar one capital requirement
	Unaudited 31/3/12		Unaudited 31/3/12	Unaudited 31/3/12	Unaudited 31/3/12
<b>On balance sheet credit exposures</b>					
Cash	476		0%	-	-
Sovereigns and central banks	1,112		0%	-	-
Public sector entities	77,163		20%	15,433	1,235
Banks	242,543		20%	48,509	3,881
Corporates (rating grade 1)	56,534		20%	11,307	905
Residential mortgages < 80% loan to value ratio (LVR)	1,359,304		35%	475,756	38,060
Residential mortgages 80 < 90% LVR	49,933		50%	24,967	1,997
Residential mortgages 90 < 100% LVR	51,969		75%	38,977	3,118
Residential mortgages welcome home loans	278,236		50%	139,118	11,129
Past due residential mortgages	3,831		100%	3,831	306
Impaired residential mortgages	518		100%	518	41
Equity holdings	687		300%	2,061	165
Other assets	723,653		100%	723,653	57,892
Non-risk weighted assets	(4,063)		0%	-	-
<b>Total on balance sheet credit exposures</b>	<b>2,841,896</b>			<b>1,484,130</b>	<b>118,729</b>

	Total exposure after credit risk mitigation	Credit conversion factor	Credit equivalent amount	Average risk weighting	Risk weighted exposure / implied risk weighted exposure	Minimum pillar one capital requirement
	Unaudited 31/3/12	Unaudited 31/3/12	Unaudited 31/3/12	Unaudited 31/3/12	Unaudited 31/3/12	Unaudited 31/3/12
<b>Off balance sheet credit exposures</b>						
Commitments with uncertain drawdown	12,734	50%	6,367	65%	4,078	326
Commitments to extend credit which can be unconditionally cancelled	175,030	0%	-	0%	-	-
<b>Market related contracts<sup>1</sup></b>						
Interest rate contracts	1,016,780	n/a	7,801	20%	1,560	125
<b>Total off balance sheet credit exposures</b>	<b>1,204,544</b>		<b>14,168</b>		<b>5,638</b>	<b>451</b>
<b>Total credit risk</b>	<b>4,046,440</b>		<b>14,168</b>		<b>1,489,768</b>	<b>119,180</b>
<b>Operational risk</b>	<b>n/a</b>				<b>177,174</b>	<b>14,174</b>
<b>Market risk</b>	<b>n/a</b>				<b>51,270</b>	<b>4,102</b>
<b>Total risk weighted assets</b>	<b>4,046,440</b>				<b>1,718,212</b>	<b>137,456</b>

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



# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 31 Capital Adequacy continued

### (iii) Residential mortgages by loan-to-valuation ratio

	BANKING GROUP			
	On balance sheet	Off balance sheet	On balance sheet	Off balance sheet
	Unaudited 31/3/13	Unaudited 31/3/13	Unaudited 31/3/12	Unaudited 31/3/12
LVR range				
0 - 80%	1,237,865	134,640	1,363,351	133,519
80 - 90%	109,872	6,515	50,081	1,016
90% +	282,567	3,603	330,359	774
Total Residential Mortgages	<b>1,630,304</b>	<b>144,758</b>	<b>1,743,791</b>	<b>135,309</b>

Welcome Home Loans make up 90% of the residential mortgages in the 90% + loan to valuation grouping. The Welcome Home Loan product is fully insured by Housing New Zealand Corporation. In addition all loans written with a loan to valuation ratio greater than 85% are required to have lenders mortgage insurance.

### (iv) Market risk exposures

Market risk exposures have been calculated in accordance with the methodology detailed in Part 10 of the RBNZ's BS2A Capital Adequacy Framework, and Schedule 9 of the Registered Bank Disclosure Statement (New Zealand Incorporated Registered Banks) Order 2013. Peak exposures are calculated using the Banking Group's equity at the end of the period.

	BANKING GROUP			
	End of period		Peak end of day	
	Unaudited 31/3/13	Unaudited 31/3/12	Unaudited 31/3/13	Unaudited 31/3/12
<b>Interest rate exposures</b>				
Implied risk weighted exposure	62,907	51,270	64,350	65,150
Aggregate capital charge	5,033	4,102	5,148	5,212

### (v) Pillar two capital for other material risks

Pillar Two of Basel II is intended to ensure that banks have adequate capital to support all material risks inherent in their business activities and includes the requirement on banks to have an "Internal Capital Adequacy Assessment Process (ICAAP)" for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining adequate capital to support risk. Southland Building Society's ICAAP has identified other areas of risk and requires it to hold capital against them. These risks include but are not limited to:

- Earnings risk - The risk due to uncertainty in future reported earnings arising from adverse changes in the business environment and from adverse business decisions.
- Liquidity risk - The risk that the Bank cannot meet or generate sufficient cash resources to meet its cash out goings as they fall due. Capital is not held for day to day liquidity. Instead a portfolio of cash, highly liquid instruments and committed funding lines is held. This largely mitigates the requirement to hold additional capital for liquidity risk, however capital is held to allow for excessive costs of raising suitable funds in adverse market conditions.
- Access to capital - The risk that the Bank may not be able to raise additional capital as required in a timely manner; particularly arising from the mutual status of SBS.
- Reputational risk - The potential that negative publicity regarding the banks business practices or financial position, whether true or not, will cause a decline in the customer base, costly litigation or impact future earnings and funding.

The Bank has made an internal capital allocation of \$22.50 million to cover these identified risks (31 March 2012 \$22.50 million).

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 32 Concentrations of Funding

	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
<b>(a) Concentrations of funding by geographical location</b>				
North Island	568,347	487,417	568,347	487,417
Canterbury	557,059	595,991	557,059	595,991
Otago	452,237	463,337	452,237	463,337
Southland	783,318	824,765	788,742	777,406
South Island other	153,331	170,583	153,331	170,583
Overseas	58,626	59,555	58,626	59,555
<b>Total concentrations of funding by geographical location</b>	<b>2,572,918</b>	<b>2,601,648</b>	<b>2,578,342</b>	<b>2,554,289</b>
<b>(b) Concentrations of funding by product</b>				
Redeemable shares	2,180,292	2,234,814	2,180,292	2,234,813
Deposits from customers	251,099	253,500	251,099	253,500
Due to other financial institutions	80,295	-	80,295	-
Other borrowings	-	52,092	-	-
Subordinated redeemable shares	61,232	61,242	61,232	61,242
Due to subsidiary companies	-	-	5,424	4,734
<b>Total concentrations of funding by product</b>	<b>2,572,918</b>	<b>2,601,648</b>	<b>2,578,342</b>	<b>2,554,289</b>

## 33 Related Parties

The Banking Group is controlled by SBS who is also the ultimate parent. A number of transactions are entered into with related parties (including key management personnel)<sup>1</sup> in the normal course of business. Details of these transactions are outlined below.

<sup>1</sup> Key management personnel are defined as being directors and senior management of the Banking Group. The information relating to key management personnel disclosed below includes transactions with those individuals, their close family members and their controlled entities.

### (a) Loans and advances to related parties

	BANKING GROUP			
	Directors and other key management personnel		Associated companies	
	31/3/13	31/3/12	31/3/13	31/3/12
Loans and advances outstanding at beginning of year	3,410	3,852	-	-
Net loans issued/(repaid) during the year	(1,231)	(442)	-	-
Loans and advances outstanding at end of year	<b>2,179</b>	<b>3,410</b>	-	-
Interest income earned on amounts due from related parties	<b>148</b>	<b>253</b>	-	-
	PARENT			
	Directors and other key management personnel		Associated companies	
	31/3/13	31/3/12	31/3/13	31/3/12
Loans and advances outstanding at beginning of year	2,583	2,952	89,871	94,838
Net loans issued/(repaid) during the year	(1,134)	(369)	(2,063)	(4,967)
Loans and advances outstanding at end of year	<b>1,449</b>	<b>2,583</b>	<b>87,808</b>	<b>89,871</b>
Interest income earned on amounts due from related parties	<b>107</b>	<b>202</b>	<b>5,292</b>	<b>5,757</b>

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 33 Related Parties continued

Loans and advances with directors of the Banking Group are made in the ordinary course of business on commercial terms and conditions. Loans and advances with key management personnel of the Banking Group are made either:

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

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

No provisions have been recognised in respect of loans given to related parties. There were no debts with any of the above parties written off or forgiven during the year ended 31 March 2013 (31 March 2012 \$nil).

### (b) Deposits from related parties

BANKING GROUP				
	Directors and other key management personnel		Associated companies	
	31/3/13	31/3/12	31/3/13	31/3/12
Deposits at beginning of year	11,491	11,962	-	-
Net deposits received during the year	19,038	(471)	-	-
Deposits at end of year	30,529	11,491	-	-
Interest expense on amounts due to related parties	1,025	443	-	-

PARENT				
	Directors and other key management personnel		Associated companies	
	31/3/13	31/3/12	31/3/13	31/3/12
Deposits at beginning of year	11,255	11,945	4,733	4,616
Net deposits received during the year	17,255	(690)	691	117
Deposits at end of year	28,510	11,255	5,424	4,733
Interest expense on amounts due to related parties	980	439	167	163

The above deposits are unsecured, carry variable interest rates and are repayable on demand.

### (c) Other transactions with related parties

	Associated Companies			
	BANKING GROUP		PARENT	
	31/3/13	31/3/12	31/3/13	31/3/12
Payments received from/(made to) subsidiaries under interest rate swap agreements	-	-	788	1,513
Net rent paid to subsidiaries	-	-	(476)	(465)
Technology services fees received from subsidiaries	-	-	104	99
Net commission received from subsidiaries	-	-	180	201
Management fees received from subsidiaries	-	-	266	1,387
Dividends received/receivable from subsidiaries	-	-	6,795	5,486
Fees received from subsidiaries	-	-	1,360	1,485
	-	-	9,017	9,706

During the year ended 31 March 2013, the Banking Group paid \$2.96 million of dividends to minority interests whom were key management personnel (31 March 2012 \$2.24 million).

All other transactions with key management personnel are conducted on an arm's length basis in the ordinary course of business and on normal terms and conditions.

During the year ended 31 March 2013, the Parent made subvention payments of \$nil (31 March 2012 \$444,066).

### (d) Key management compensation

Details of remuneration paid or payable to the directors and other key management personnel are outlined in Note 5 - Expenses.

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 34 Accounting Classifications

The table below sets out the Banking Group's classification of each class of financial assets and liabilities.

BANKING GROUP						
As at 31 March 2013	Designated at fair value	Available for sale	Loans and receivables	Held to maturity	Other amortised cost	Total carrying amount
<b>Assets</b>						
Cash on hand and at bank	-	-	21,801	-	-	21,801
Funds with financial institutions	-	144,490	-	-	-	144,490
Investment securities	1,656	398,577	-	-	-	400,233
Derivative financial instruments	2,396	-	-	-	-	2,396
Advances to customers	6,121	-	2,219,632	-	-	2,225,753
	10,173	543,067	2,241,433	-	-	2,794,673
<b>Liabilities</b>						
Redeemable shares	-	-	-	-	2,180,292	2,180,292
Deposits from customers	-	-	-	-	251,099	251,099
Due to other financial institutions	-	-	-	-	80,295	80,295
Derivative financial instruments	6,617	-	-	-	-	6,617
Subordinated redeemable shares	-	-	-	-	61,232	61,232
	6,617	-	-	-	2,572,918	2,579,535

PARENT						
As at 31 March 2013	Designated at fair value	Available for sale	Loans and receivables	Held to maturity	Other amortised cost	Total carrying amount
<b>Assets</b>						
Cash on hand and at bank	-	-	18,790	-	-	18,790
Funds with financial institutions	-	137,241	-	-	-	137,241
Investment securities	-	397,595	-	-	-	397,595
Derivative financial instruments	2,614	-	-	-	-	2,614
Advances to customers	6,121	-	2,110,650	-	-	2,116,771
Loans to subsidiaries	-	-	87,808	-	-	87,808
	8,735	534,836	2,217,248	-	-	2,760,819
<b>Liabilities</b>						
Redeemable shares	-	-	-	-	2,185,716	2,185,716
Deposits from customers	-	-	-	-	251,099	251,099
Due to other financial institutions	-	-	-	-	80,295	80,295
Derivative financial instruments	6,617	-	-	-	-	6,617
Subordinated redeemable shares	-	-	-	-	61,232	61,232
	6,617	-	-	-	2,578,342	2,584,959

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$'000's

## 34 Accounting Classifications continued

### BANKING GROUP

As at 31 March 2012	Designated at fair value	Available for sale	Loans and receivables	Held to maturity	Other amortised cost	Total carrying amount
<b>Assets</b>						
Cash on hand and at bank	-	-	22,474	-	-	22,474
Funds with financial institutions	-	90,980	-	-	-	90,980
Investment securities	2,198	263,535	-	-	-	265,733
Derivative financial instruments	2,789	-	-	-	-	2,789
Advances to customers	20,277	-	2,405,446	-	-	2,425,723
	25,264	354,515	2,427,920	-	-	2,807,699
<b>Liabilities</b>						
Redeemable shares	-	-	-	-	2,234,814	2,234,814
Deposits from customers	-	-	-	-	253,500	253,500
Derivative financial instruments	10,206	-	-	-	-	10,206
Other borrowings	-	-	-	-	52,092	52,092
Subordinated redeemable shares	-	-	-	-	61,242	61,242
	10,206	-	-	-	2,601,648	2,611,854

### PARENT

As at 31 March 2012	Designated at fair value	Available for sale	Loans and receivables	Held to maturity	Other amortised cost	Total carrying amount
<b>Assets</b>						
Cash on hand and at bank	-	-	17,413	-	-	17,413
Funds with financial institutions	-	85,825	-	-	-	85,825
Investment securities	-	262,848	-	-	-	262,848
Derivative financial instruments	3,756	-	-	-	-	3,756
Advances to customers	20,277	-	2,242,233	-	-	2,262,510
Loans to subsidiaries	-	-	89,871	-	-	89,871
	24,033	348,673	2,349,517	-	-	2,722,223
<b>Liabilities</b>						
Redeemable shares	-	-	-	-	2,239,547	2,239,547
Deposits from customers	-	-	-	-	253,500	253,500
Derivative financial instruments	10,259	-	-	-	-	10,259
Other borrowings	-	-	-	-	-	-
Subordinated redeemable shares	-	-	-	-	61,242	61,242
	10,259	-	-	-	2,554,289	2,564,548

# Notes to the Financial Statements for the year ended 31 March 2013

All in \$000's

## 35 Fiduciary Activities

### Funds management

The Banking Group markets and manages unit trusts, investment and superannuation funds through its subsidiary Funds Administration New Zealand Limited (FANZ). FANZ is a registered unit trust manager, an approved KiwiSaver provider and also operates a financial advisory business providing custodial services, investment advice and portfolio management called SBS Financial Advisers. The Banking Group derives fee and commission income from these activities but is not responsible for any decline in performance of the underlying assets of the investors due to market forces.

SBS has entered into a trust deed made between SBS and Trustees Executors Limited, as Trustee of a registered superannuation scheme known as the Lifestages Superannuation Scheme (previously known as Lifestages Capital Stable Portfolio). Under a Deed of Novation dated 31 March 2007 SBS novated its rights and obligations under this Trust Deed to FANZ. From this date FANZ is the founder and promoter of the Lifestages Superannuation Scheme. The trust deed was effective from the 1st day of April 1992. The majority of the funds invested in the Lifestages Superannuation Scheme are reinvested with SBS.

The outstanding value of assets related to funds management activities is set out in the table below. These assets are not owned by the Banking Group and are therefore not included on the Banking Group's statement of financial position.

	31/3/13	31/3/12
Funds under management on behalf of customers	401,900	349,800

### Securitised assets

As at 31 March 2013, the Banking Group had securitised assets amounting to \$256 million (31 March 2012 \$211 million). These assets have been sold to the SBS Invercargill W Trust (a special purpose vehicle established for the purpose of purchasing residential mortgages from the Bank and funded through wholesale funding lines), and the SBS Oreti Trust No. 2 (a special purpose vehicle investing in residential mortgages originated and funded by the Bank through issue of residential mortgage backed securities). Note 14 provides further information on securitised assets. The Banking Group receives fees for various services provided to the securitisation vehicles on an arm's length basis, including servicing fees. These fees are recognised as earned. All securitisation vehicles form part of the Banking Group.

The SBS Oreti Trust No. 2 is an in-house residential mortgage backed securities (RMBS) facility that can issue securities that meet the RBNZ criteria to use as collateral in repurchase transactions with the RBNZ. The facility provides the Bank with additional contingent funding from the RBNZ. Further information on liquidity is provided in Note 28.

### Insurance business

The Banking Group markets and distributes insurance products through its subsidiary company Southsure Assurance Limited. The Banking Group derives premium income from the sale of insurance products.

The total assets of Southsure Assurance Limited as at 31 March 2013 are \$11.4 million (31 March 2012 \$9.5 million) which is 0.4% of the total assets of the Banking Group (31 March 2012 0.3%). This complies with the Conditions of Registration of Southland Building Society, which allows a maximum of 1% of the total consolidated assets of the Banking Group to be represented by insurance business assets.

Policies and procedures exist to ensure that the insurance activities of the Banking Group are conducted in an appropriate manner. These include regular reviews of the operations of the insurance business by management. Should adverse conditions arise, these policies and procedures are expected to mitigate the impact of the conditions on the Banking Group.

### Risk management

The Banking Group has in place policies and procedures to ensure that the fiduciary activities identified above are conducted in an appropriate manner. It is considered that these policies and procedures will ensure that any difficulties arising from these activities will not impact adversely on the Banking Group. The policies and procedures include comprehensive and prominent disclosure of information regarding products, and formal and regular review of operations and policies by management and internal auditors. Further information on SBS risk management policies and practices is included in notes 3 and 28 to 30.

### Provision of financial services

Financial services provided by the Banking Group to entities which are involved in trust, custodial, funds management and other fiduciary activities, are provided on arm's length terms and conditions and at fair value. Any assets purchased from such entities have been purchased on an arm's length basis and at fair value.

The Banking Group has not provided any funding to individual unit trusts which the Banking Group distributes on behalf of third parties. All entities involved in securitisation and insurance activities are members of the Banking Group.

## 36 Subsequent Events

During May 2013 the bank purchased a portfolio of reverse equity mortgages. The book value of the portfolio at settlement was \$46 million.

There have been no other material subsequent events after 31 March 2013.

### To the Members of Southland Building Society

#### Report on the Bank and Banking Group Disclosure Statement (excluding Supplementary Information relating to Capital Adequacy)

We have audited the accompanying financial statements and supplementary information of Southland Building Society (the "Bank") and its subsidiaries (the "Banking Group") on pages 10 to 65 of the Disclosure Statement. The financial statements comprise the statements of financial position as at 31 March 2013, the income statements and 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 of the Bank and Banking Group. The supplementary information comprises the information that is required to be disclosed under the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2013 (the "Order").

#### *Directors' Responsibility for the Disclosure Statement*

The directors are responsible for the preparation of the Disclosure Statement, including financial statements prepared in accordance with Clause 24 of the Order and generally accepted accounting practice in New Zealand, and that give a true and fair view of the matters to which they relate. The directors are also responsible for such internal controls as they determine are necessary to enable the preparation of the Bank and Banking Group's financial statements that are free from material misstatement whether due to fraud or error.

The directors are responsible for the preparation and fair presentation of supplementary information, in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order.

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on the Disclosure Statement, including the financial statements prepared in accordance with Clause 24 of the Order and the supplementary information disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order. 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 Bank financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Bank 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 controls relevant to the Bank's preparation of the financial statements that gives 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 Bank's internal controls. 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 provided other assurance services to the Bank. Partners and employees of our firm may also deal with the Bank on normal terms within the ordinary course of trading activities of the business of the Bank. There are, however, certain restrictions on dealings which the partners and employees of our firm can have with the Bank. These matters have not impaired our independence as auditor of the Bank. The firm has no other relationship with, or interest in, the Bank.

#### *Opinion on Financial Statements*

In our opinion the financial statements of Southland Building Society and its subsidiaries ("the Bank and Banking Group") on pages 10 to 65 (excluding the supplementary information):

- complies with generally accepted accounting practice in New Zealand;
- complies with International Financial Reporting Standards; and
- gives a true and fair view of the financial position of the Bank as at 31 March 2013 and of its financial performance and cash flows for the year ended on that date.

#### *Opinion on Supplementary Information*

In our opinion, the supplementary information that is required to be disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order; and is included within notes 12, 13, 28, 29, 30 and 35 of the Disclosure Statement:

- has been prepared, in all material respects, in accordance with the guidelines issued pursuant to section 78(3) of the Reserve Bank of New Zealand Act 1989 and any Conditions of Registration;
- is in accordance with the books and records of the Bank; and
- fairly states the matters to which it relates in accordance with those Schedules.



#### **Report on Capital Adequacy information**

We have reviewed the Capital Adequacy information, as disclosed in note 31 of the Disclosure Statement for the year ended 31 March 2013.

#### ***Directors' Responsibility for the Capital Adequacy information***

The directors are responsible for the preparation of supplementary information relating to Capital Adequacy that is required to be disclosed under Schedule 9 of the Order.

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on the Capital Adequacy information based on our review. We conducted our review in accordance with the Review Engagement Standards issued by the New Zealand Institute of Chartered Accountants. Those standards require that we comply with ethical requirements and plan and perform the review to obtain limited assurance about whether the Capital Adequacy information is, in all material respects:

- prepared in accordance with the Bank's Conditions of Registration; and
- disclosed in accordance with Schedule 9 of the Order.

A review is limited primarily to enquiries of Bank personnel and analytical review procedures applied to the financial data, and thus provides less assurance than an audit. We have not performed an audit in respect of the Capital Adequacy disclosures, and accordingly, we do not express an audit opinion on these disclosures.

#### ***Opinion***

Based on our review, nothing has come to our attention that causes us to believe that the Capital Adequacy information, disclosed in note 31 of the Disclosure Statement, is not, in all material respects:

- prepared in accordance with The Bank's Conditions of Registration; and
- disclosed in accordance with Schedule 9 the Order.

#### **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, and clauses 2(1)(d) and 2(1)(e) of Schedule 1 of the Order, we report that:

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

4 June 2013

KPMG Wellington



## Branch Directory

### SBS Bank

#### Invercargill – Head Office

51 Don Street  
PO Box 835  
Invercargill  
Telephone: 03 211 0700  
Fax: 03 211 0793

#### North Invercargill

54 Windsor Street  
Telephone: 03 211 0745  
Fax: 03 217 7933

#### Gore

80 Main Street  
PO Box 212  
Telephone: 03 209 0080  
Fax: 03 209 0077

#### Dunedin

Cnr George & Hanover Streets  
PO Box 5492  
Telephone: 03 477 5100  
Fax: 03 471 4439

#### Queenstown

7 Shotover Street  
PO Box 710  
Telephone: 03 441 0033  
Fax: 03 441 0279

#### Cromwell

21 The Mall  
PO Box 226  
Telephone: 03 445 0672  
Fax: 03 445 0697

#### Timaru

235 Stafford Street  
PO Box 844  
Telephone: 03 684 9536  
Fax: 03 688 4598

#### Christchurch – Ferrymead

23 Humphreys Drive  
PO Box 19835  
Telephone: 03 376 6198  
Fax: 03 376 6298

#### Christchurch – Riccarton

109 Riccarton Road  
PO Box 80058  
Telephone: 03 982 5700  
Fax: 03 982 5706

#### Christchurch – Papanui

2-6 Main North Road  
PO Box 5038  
Telephone: 03 375 0840  
Fax: 03 375 0841

#### Nelson

126 Trafalgar Street  
PO Box 211  
Telephone: 03 548 9200  
Fax: 03 545 9839

#### Blenheim

Cnr Market & Main Streets  
PO Box 1188  
Telephone: 03 579 5293  
Fax: 03 579 5249

#### Hamilton

Cnr Victoria & Bryce Streets  
PO Box 19222  
Telephone: 07 957 6350  
Fax: 07 957 6351

#### Tauranga

36 Spring Street  
PO Box 13020  
Telephone: 07 578 9217  
Fax: 07 578 9219

#### SBS Bank Rural – Invercargill

66 Don Street  
PO Box 835  
Telephone: 0800 502 442  
Fax: 0508 526 363

### HBS Bank

#### Hastings

Cnr Queen & Market Streets  
PO Box 10  
Telephone: 0800 427 2265  
Fax: 06 878 9631

#### Napier

93 Dalton Street  
PO Box 1041  
Telephone: 0800 427 2265  
Fax: 06 835 4471

#### Havelock North

1 Napier Road  
PO Box 8604  
Telephone: 0800 427 2265  
Fax: 06 877 3902



OUR PEOPLE MAKE THE DIFFERENCE

