CONSULTATION DOCUMENT:

REVIEW OF DISCLOSURE REQUIREMENTS FOR REGISTERED BANKS

Consultation paper

The Reserve Bank invites submission on this consultation paper by 24 September 2010.

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Table of Contents

Executive Summary 4

Section 1: Introduction 6

Section 2: Background 7

2.1 Current regulatory reporting requirements in New Zealand 7

2.2 Comparison with Australia and the United Kingdom 7

Section 3: The Disclosure Review..........9

3.1 Objective 9

3.2 Engagement with key stakeholders 9

3.3 The givens and norms 10

3.4 Analysis overview 11

3.5 High level options 12

3.6 Page count estimates..........17

3.7 Disclosure statement delivery mechanism 17

3.8 Private reporting to the RBNZ 18

3.9 Next steps 18

Section 4: Detailed Analysis 19

4.1 Further design features 19

4.1.1 NZ IAS 34 compliance in off quarters 19

4.1.2 NZ IFRS 7 Appendix E 20

4.1.3 Scope of financial reporting 21

4.1.4 Options for the Supplemental Disclosure Statement 22

4.1.5 Disclosure by branches 23

4.1.6 Improved comparability in certain key areas 26

4.1.7 Nature of audit review 29

4.2 Proposed changes in disclosure of specific subject areas 30

4.2.1 Disclosure of accounting policies 30

4.2.2 Disclosure of risk management approaches....................31

4.2.3 Disclosure of credit risk concentration to individual counterparties 31

4.2.4 Disclosure of credit risk impairment information 32

4.2.5 Disclosure of Basel Pillar 3 information 35

4.2.6 Disclosure relating to liquidity risk 37

4.2.7 Other proposals for revised disclosure in specific subject areas 38

Appendices 41

Appendix 1: List of overlaps and duplications between on quarter OiCs and NZ IFRSs and recommendation 42

Appendix 2: List of items in on quarter OiC that should be kept or removed....................43

Appendix 3: Full list of information currently required by OiCs that will be removed, streamlined or restructured for half-year GDSs 45

Appendix 4: Recommendation to shorten the off-quarter GDSs 46

Appendix 5: KIS – assessment of current contents and possible additions 47

Appendix 6: Assessment of disclosure requirements of NZ IFRS 7 Appendix E 48

Appendix 7: Consolidated questions 51

Consultation document:
Review of Disclosure requirements for registered banks

Executive Summary

a change in the requirement for the financial statements that are included in the half-year disclosure, from being prepared on the annual financial reporting standards basis, to an interim financial reporting basis. This should have two effects: it will align New Zealand with international practice; and it is likely t

SECTION ONE: INTRODUCTION

In 1996, the Reserve Bank put in place comprehensive disclosure requirements for New Zealand banks. The Reserve Bank sees market discipline as an important complement to regulatory discipline, and the disclosure regime aims to ensure that the market has the information it needs to exercise that discipline. Under the existing regime, banks are required to publish quarterly a Key Information Summary (KIS) providing a high-level overview of the bank's financial condition; a General Disclosure Statement (GDS) containing detailed financial information on all aspects of the bank's business, including its conditions of registration and compliance with prudential requirements; and a Supplemental Disclosure Statement (SDS) containing background documents such as guarantee contracts, and, for branches, the financial statements of their overseas banking group.

The requirements for banks to publish quarterly disclosure statements are contained in the Registered Bank Disclosure Statement Orders in Councils[1] (OiCs). These are issued under section 81of the Reserve Bank of New Zealand Act, which deals with the public disclosure of information or data by registered banks. The regime was designed to:

Improve market discipline;
Increase the public's financial awareness; and
Strengthen directors' responsibilities.

Since the regime was introduced, and particularly more recently, there have been some major developments in accounting standards, with the cumulative effect of requiring significantly more disclosure. The current New Zealand equivalents to International Financial Reporting Standards (NZ IFRSs) include several areas of required disclosure that either overlap with, or duplicate what is required by the OiCs. A few recent changes to NZ IFRSs have also resulted in some inconsistencies between the OiC and NZ IFRS requirements.

The Reserve Bank has also added to the information required by the OiCs over time, most notably the expanded disclosure of capital adequacy for locally-incorporated banks, which was added in March 2008 to implement "Pillar 3"[2]. These have put a rising compliance burden on banks in producing their quarterly disclosure statements.

Anecdotal evidence and feedback from users also suggested that some of the disclosure statements were not useful, especially the KIS and SDS.

The above factors have prompted us to undertake a fundamental review of the disclosure regime for registered banks in New Zealand, which commenced in October 2009. The bulk of the work of the review to date has been on the disclosure requirements for locally-incorporated banks. Much of this work is also applicable to branches, but we raise some specific issues and consultation questions for branches in a section 4.1.5.

Throughout the paper we have posed specific questions on particular points on which we would like to hear views. (For ease of reference, these questions are also collected together in Appendix 7.) However, we will be interested to hear views on any aspect of the proposals, or on any alternative suggestions.

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[1] There are four Orders in Councils for disclosure statements: Full and Half year New Zealand Incorporated Registered Banks; Off quarter New Zealand Incorporated Registered Banks; Full and Half Year Overseas Incorporated Registered Banks; and Off quarter Overseas Incorporated Registered Banks. Most of the references to OiCs in the consultation document are to the first two OiCs.

[2] The revised capital adequacy framework issued by the Basel Committee on Banking Supervision – "Basel II" – consists of three "pillars". Pillar 3 deals with market discipline.

Section 3 of this paper (and questions 1-8 in Appendix 7) discusses issues of principle and high-level design. This section contains, for example, a discussion of whether it is appropriate to abandon the disclosure regime altogether, and how far – at a high level – we might go in consolidating and reducing the disclosure requirements in on- and off-quarters.

Inevitably, though, much of the "devil is in the detail" and Section 4 (questions 9-41) covers the detailed requirements that might follow from the preferred high-level options.

SECTION 2: BACKGROUND

2.1 Current Regulatory Reporting Requirements in New Zealand

Banks, as issuers, are required by the Financial Reporting Act 1993 to publish audited financial statements at least annually that comply with New Zealand financial reporting standards approved under that Act. The bulk of these standards comprise New Zealand equivalents to International Financial Reporting Standards and International Accounting Standards. For convenience in this paper, we refer to these as a whole as NZ IFRSs[3].

In addition, banks are also subject to the Securities Act 1978, which in general requires a registered prospectus and investment statement for any issue of debt securities. However, banks are currently exempt from the prospectus requirement in respect of their debt securities. This exemption was granted around the time that the RBNZ disclosure regime was set up, on the basis that the latter would serve as a substitute for the prospectus requirement.

The RBNZ disclosure regime provides a "one-stop shop" for the reporting obligations that banks are faced with, covering the requirements of the accounting standards, Basel Pillar 3 disclosure, and the Securities Act. Currently, it requires banks to publish a disclosure statement every three months. The disclosure statements contain a wide range of financial, corporate and risk-related information. This includes information meeting the requirements of NZ IFRSs and prudential information on matters such as capital adequacy that is driven by Pillar 3. Other prudential information required includes individual credit exposure concentrations, and other matters of interest to depositors such as deposit guarantees and the ranking of creditor claims.

The requirements for "on quarters" (i.e. the annual and half-year periods) are the same, and for "off quarters" (i.e. the 3-month and 9-month periods) a separate set of "slimmer" requirements apply, which focus more on summarised data with less requirement for details.

It is particularly at the half-year and off-quarter reporting periods that the RBNZ regime imposes more disclosure requirements than NZ IFRSs and the Pillar 3 framework. At the half year, the RBNZ regime requires banks to produce financial reports on the basis of NZ IFRSs applicable for full-year reporting. Normally, any entity reporting interim financial results (commonly at the half year) does so on the basis of NZ IAS 34 *Interim Financial Reporting*[4], which requires significantly less information than the full-year reporting standards. The off-quarter reporting is largely a requirement that the Reserve Bank imposes in addition to what is required by NZ IFRSs (although Pillar 3 does require a brief summary of capital adequacy).

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[3] Unless stated, NZ IFRSs includes any New Zealand specific material such as Appendix E of NZ IFRS 7 *Financial Instruments: Disclosure.*

[4] This standard sets the minimum content of an interim report, including condensed financial statements and selected notes. It is to provide an update on the latest complete set of annual statements, and focuses on new activities and events, and does not duplicate information previously reported.

Were a bank to be subject to the Securities Act requirements, it would be required to make "continuous disclosure", i.e. any prospectus issued by the bank would have to be updated whenever it had become incorrect or misleading due to material events taking place. There is no quarterly reporting requirement per se under the Securities Act.

2.2 Comparison with Australia and the United Kingdom

Table 1 below compares the current New Zealand bank disclosure regime to public reporting requirements in Australia and the United Kingdom.

Public reporting obligations

SECTION 3: THE DISCLOSURE REVIEW

3.1 Objective

The objective of the Review is to assess banks' prudential disclosure requirements with a view to better matching the needs of the key stakeholders and reducing compliance burdens where

welcome submissions on this consultation paper from members of the public.) The main focus of these discussions with these three bodies was on the KIS.

Securities Commission and Ministry of Economic Development (MED)

We have had some discussion with the Securities Commission on the interaction between the RBNZ disclosure regime and the Securities Act prospectus requirements for debt issuers. We have also talked to MED about their proposed reform of the Securities Act[6]. It is important that we form a co-ordinated view across government on the appropriate form of disclosure by banks, and the vehicle for that disclosure.

Rating agencies

Rating agencies are key players for market discipline, as their rating assessments can assist bank counterparties in exerting market discipline on banks. We have spoken to the three main rating agencies to gauge their level of interest in the disclosure regime. Although a bank would generally have an interest in providing a rating agency privately with any additional financial or other information requested by the agency to enable it to form its rating opinion, the rating agencies told us that they do to varying extents make use of the information published in banks' GDSs. It has also been valuable for us to hear the agencies' views on which information is most valuable in assessing a bank's soundness.

Financial commentators and journalists

Media commentators and financial advisers are another group that provide public assessments, similarly to rating agencies, but using mainly publicly available data. The general public relies on their comments to a certain extent. We have talked to a few financial commentators to get their views on the usefulness of the data, areas for improvement etc.

3.3 The givens and norms

Before undertaking the detailed analysis of the Review, we assumed a few "givens", as the basic principles or starting points. They are:

1) **NZ IFRSs**: We have taken NZ IFRSs for the most part as a given: they represent New Zealand equivalents to IFRSs promulgated by the IASB, and as such our scope to influence them is very limited[7]. The Financial Reporting Act 1993 requires issuers (i.e. including banks) to publish audited financial statements based on generally accepted accounting practices (i.e. NZ IFRSs) at least annually. Usually banks overseas publish a full set of IFRS-compliant financial statements annually and a smaller set of financial statements based on IAS 34 half-yearly;

2) **Pillar 3**: Public disclosure of detailed information on a bank's capital adequacy ("Pillar 3") is a key component of the recently implemented Basel II capital adequacy framework, and represents a widely-accepted international norm. It would be a complete change of direction for New Zealand to pull back from this just when the

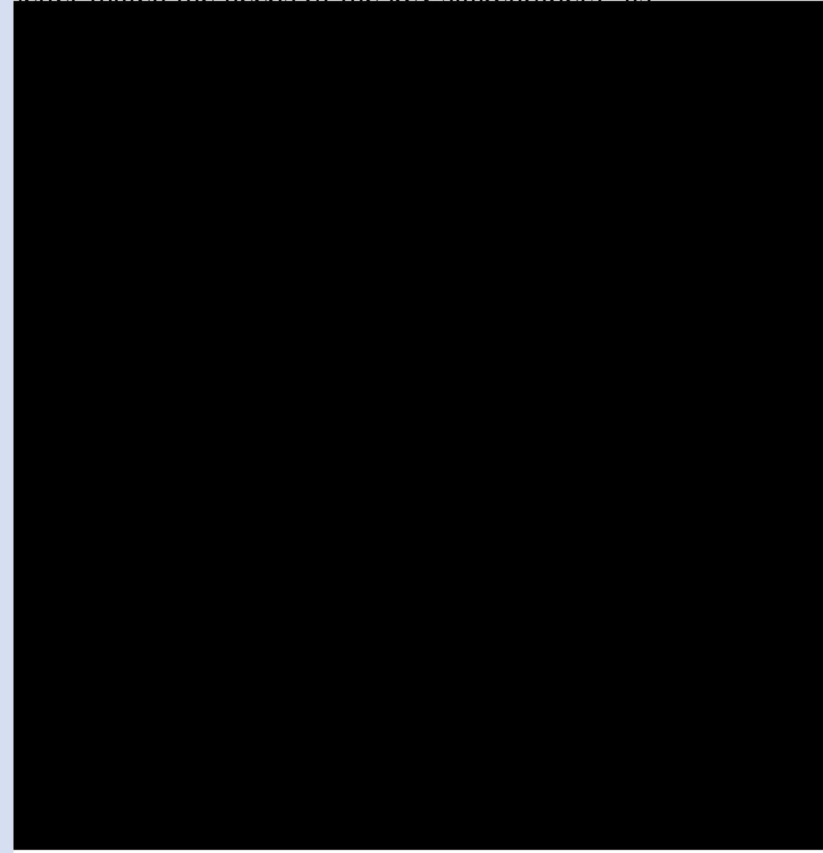
6 MED released a discussion document "Review of Securities Law" on 21 June 2010, available on their website: http://www.med.govt.nz/templates/MultipageDocumentTOC____43741.aspx

7 One exception is the New Zealand-specific Appendix E of NZ IFRS 7, which the Reserve Bank has a realistic chance of influencing (see section 4.1.2).

tep towards greater transparency. We therefore ould continue to comply at least with the broad ıer countries now usually publish their Pillar 3 ɔm their general financial reporting.

: also continue to take as a given that market helping the Reserve Bank achieve its Section 68 a position to exert that discipline need sufficient

ɔetter match the needs of the key stakeholders" as



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information at that frequency, to come to a preliminary view on how the costs and benefits compare. This informs our view on whether a particular requirement should remain, either at the current or a lower frequency, or should be removed from public disclosure, and if so, whether it still needs to be collected privately by the Reserve Bank for prudential supervision purposes. A summary of the findings of this analysis is set out below:

Periodic Reports	Findings
Annual General Disclosure Statements (GDSs)	There are inconsistencies and overlaps between the OiCs and NZ IFRSs, which should be removed[9]. A material portion of the additional OiC requirements is driven by Basel II Pillar 3 capital adequacy disclosures. But among other requirements, some are of doubtful value, or are in fact inconsistent with NZ IFRSs (see Appendix 1).
Half-year GDSs – based on full-year NZ IFRSs	We have identified quite a few areas where the RBNZ's imposition of full-year NZ IFRSs requirements on half-year disclosure is not warranted – such as full disclosure of accounting policies, risk management policies, detailed notes on tax expense, deferred tax, bonds and notes, management remuneration, retirement benefits etc. Some of these notes are lengthy but can be more or less copied from one period to the next, as little usually changes (although these clutter up the disclosure for its users). But some notes are costly to produce even though they are only one table (such as key management remuneration). (See Appendices 2 and 3)
Off-quarter GDSs	The off-quarter OiC requires slightly more information than NZ IAS 34 *Interim Financial Reporting*. In our view some of that extra information is of value, but some may not be (see Appendix 4).
Key Information Summary (KIS)	Our impression is that the current content of the KIS is not useful, and no one uses it. For a short document, it is often filled with legal and technical jargon and hard to comprehend (see Appendix 5).
Supplemental Disclosure Statement (SDS)	A low-benefit item reserved for legal documents (e.g. guarantees). (See further discussion in section 4.1.4 below)

If we succeed in addressing the issues raised in these findings (through one of the options discussed later), it would represent fairly material streamlining of the current OiC requirements that are over and above the NZ IFRSs ones, and as such, a significant reduction of compliance burden on banks – while at the same time better matching disclosure to the needs of the key stakeholders.

3.5 High Level Options

3.5.1 Options that have been considered but are not preferred

Before going into more details on the two preferred options, we note three other options that appear not to achieve the objectives of the review or not to be workable.

Maintain the status quo. The first one is to maintain the status quo. Our analysis and views from stakeholders so far have confirmed significant issues in the existing disclosure regime that need to be addressed. We have identified:

[9] In some cases the RBNZ would achieve this by seeking to have requirements removed from Appendix E of NZ IFRS 7, rather than from the OiCs.

Overlaps and inconsistencies between the OiC and NZ IFRS requirements that can lead to confusion for the banks in preparing the disclosure, and GDSs that are hard for users to understand;

Information that should not have to be published every six months. There is little to be gained, for example,

data that is useful for both purposes, prudential disclosure information needs to include more data relevant to the risk of failure of an individual bank or threats to the soundness of the financial system (for instance, much of the Pillar 3 disclosure meets this need). And although full-year financial statements do require disclosure of measures of the risks arising from financial instruments, to promote market discipline effectively, some of that information is needed at greater than annual frequency.

We are liaising with the Securities Commission to come to an agreed view on what frequency and level of detail of disclosure under our (revised) regime would be needed to allow banks to keep their Securities Act exemptions.

Separate publication of financial reporting and prudential disclosures. A third option that we have considered but are not pursuing further is still requiring additional prudential disclosure on top of that required by financial reporting standards, but requiring the two to be published separately.

Under this option, there would be annual financial reports based on NZ IFRSs ("the given"); plus half-year financial reports based on NZ IAS 34 *Interim Financial Reporting* ("the norm"); plus Pillar 3 disclosure (half-yearly for the quantitative with brief quarterly update, annually for the qualitative material – another "given" in the light of Basel minimum requirements). This option could possibly include a redesigned KIS quarterly or a new quarterly report, to contain summary financial information and some other prudential information such as individual large credit exposures.

This generally represents the 'norm' in other countries, where banks publish financial reports required by financial reporting standards on a half-yearly basis, and have recently started having to publish detailed capital adequacy information under Pillar 3 of Basel II – so in some way this would result in an alignment of the NZ framework with international practice. We might propose that in addition, some form of quarterly disclosure be retained – a quarterly KIS (to be significantly revised), or RBNZ publishing summary quarterly tables allowing comparison of key information across banks[11].

Initial feedback from banks was that they were not attracted to the option of separating public disclosure into two different documents, because of linkages between the two sets of information: for instance, NZ IFRSs require an analysis of impaired assets, but Pillar 3 requires a breakdown of this analysis into the separate Basel II credit risk exposure categories. We also think that it is more helpful for users to be able to see the essential information together in one place (provided that the overall volume of information can at the same time be reduced to make it easier to navigate).

Q1. Do you think any of the above three options should be considered further? If so, which one and why?

3.5.2 Options for consultation

The analysis and feedback from key stakeholders to date have been able to effectively inform and complement the development of two high-level options set out in Table 4 below:

[11] This is already being done to some extent, but the structure could be redesigned to enable easier comparison across the sector.

TABLE 4	*Option A*	*Option B*
Annual	*New KIS, Modified GDS*	*Modified GDS*
Half Year	*New KIS, Streamlined GDS (NZ IAS 34)*	*Streamlined GDS (NZ IAS 34)*
Off quarters	*New KIS*	*Brief GDS (possibly NZ IAS 34)*

Option A – Redesigning the KIS to be the only off-quarter document

Under this option, there will be:

- *Annual – New KIS (redesigned to be more useful), Modified GDS (with inconsistency/overlaps removed);*
- *Half year – New KIS, Streamlined GDS (closer to current off-quarter GDS);*
- *Off quarter – New KIS only.*

One main change from the current regime under this option would be to slim down the half-year GDS from the current on quarter requirements (i.e. applying full-year NZ IFRSs, and comprehensive additional prudential disclosure) to something similar to the current off-quarter requirements (i.e. applying NZ IFRS interim reporting requirements and more summary versions of some of the prudential information, although with the same quantitative Pillar 3 disclosure as at the full year to satisfy Basel standards). For the full-year GDS, the aim would be to improve consistency with NZ IFRSs and minimise duplication. This would include seeking the removal of Appendix E of NZ IFRS 7.

Another emphasis of Option A is on the new KIS. This involves redesigning the content and structure of the KIS to make it more useful for retail depositors. It is also intended that the new KIS will be expanded to include more financial statement items (Profit and Loss and the Balance Sheet) and important ratios, so it could replace the current off-quarter GDSs. Potential [illegible] – 0–

that they do not use the KIS at all. It follows that if RBNZ chooses to pursue raising depositors' awareness, a more realistic approach is to consider either publishing and publicising simplified information on RBNZ's website or make use of other popular websites that are known to be frequently used by the public.

Feedback to date has suggested that having some information updated quarterly has been an important feature of the regime. While Option A does retain the quarterly update through the KIS, it would require a reasonably significant publicity campaign to promote the new KIS for there to be any chance of its being used. Given that it seems that the quarterly GDS has been used while the KIS has not, it seems natural to remove the KIS and retain the quarterly GDS but improve it to make it more useful.

Our preliminary thinking is that Option B might be preferred because:

It retains something that is currently considered useful – i.e. the quarterly GDS.

An attempt to devise an off-quarter document that is accessible enough to encourage general readers to look at it, while containing sufficient information to satisfy the needs of expert analysts, seems likely to end up achieving neither.

From what we have heard, it is unclear to what extent retail depositors in a bank will take an interest in their bank's financial condition regardless of the availability and readability of the KIS. Option B provides financial commentators with better information in the off quarters on which to base analysis and commentary aimed at any interested readers.

Although the compliance burden on banks would be somewhat less in the off quarters under Option A, this would be offset by the need to publish the KIS every quarter.

A variant on Option B would be to dispense with off-quarter disclosure requirements as far as possible. The absolute minimum of what is required for quarterly publication is the Pillar 3 information on capital adequacy, which we think would be satisfied with a summary update as proposed in section 4.2.5. Such a reduction in information would raise the question whether the market would be provided with sufficient information on the bank's overall financial condition frequently enough to justify continued exemption from Securities Act requirements. Some mechanism might therefore need to be found for continuous disclosure of material updates by the banks.

We are not attracted to this variant, as we have heard a fair amount of support for publication of off-quarter financial information on a standardised basis, allowing cross-bank comparison. Among other things, without quarterly disclosure it would not be possible to compare banks' performance over a given quarter, since banks' financial years run to different end-quarter dates. We think that this would be moving too far away from the basic principle of promoting market discipline.

Q2. Do you agree with our assessment that Options A and B are the main options for consideration?

Q3. Is there an alternative approach we should consider?

Q4. What are your views on the relative merits of Options A and B?

Q5. Do you think that replacing off-quarter disclosure with continuous disclosure is a feasible option for consideration?

Under each of these broad options there are numerous detailed decisions to be made on how specific areas of disclosure need to be changed. As well as informing our views on the right options to consult on, our line-by-line analysis of disclosure require bloa on are r

In terms of paper versions, if the KIS is dropped (Option B) we think there is no remaining case for requiring that hard copies of disclosure statements are made available in every bank branch. Even if the KIS is retained, experience suggests that putting copies in every branch is not effective in encouraging depositors to take an interest in the state of their banks, and we think better ways would need to be found to publicise the KIS.

As a backstop we think that hard copies of all disclosure material should be available on request from the registered bank's head office, within a reasonable time frame. The bank would not need to keep a stock of printed disclosure statements available to meet this requirement, but could print off copies as needed from its website. Bank branches should also be able to print out a copy of the disclosure statements upon request by customers.

Q8. What are your views on the appropriate publication mechanism for bank disclosure statements?

3.8 Private reporting to the RBNZ

Both options proposed in this document involve removal of various pieces of information from public disclosure, whether because it is not considered necessary for market discipline, it is not useful in the current prescribed format, or the compliance costs far outweigh the benefits. The information not considered useful from a market discipline perspective may nevertheless remain important for the Reserve Bank to carry out its prudential oversight function. Further work is being progressed to review the nature and scope of private reporting from banks to the Reserve Bank in light of this Review.

3.9 Next steps

The closing date for submissions is Friday 24 September 2010.

Subject to the submissions received, we plan to publish the outcome of the Review early in November 2010, to be followed by draft revised Orders in Council for consultation, for comments by the end of the year. We plan that the changes will take effect for the disclosure period ended 31 March 2011.

Banks have indicated that on the basis of the likely changes in the disclosure regime discussed with them so far, it should take them at most three months to make the necessary systems changes to be ready to begin disclosing under the revised regime. If that proves not to be the case in the light of the details of the review now being published, or in the light of changes to the proposals in response to submissions, we might need to extend the timetable, and consider including a transition period.

SECTION 4: DETAILED ANALYSIS

Following the discussion of the background and the high level options for change, the rest of this consultation paper covers the detail of the analysis we have carried out and deals with the detailed implications of the proposals.

4.1 FURTHER DESIGN FEATURES

4.1.1 NZ IAS 34 compliance in off quarters

A separate question on which we welcome feedback is whether banks' off-quarter disclosure statements or the expanded KIS should have to meet the minimum content requirements of NZ IAS 34 *Interim Financial Reporting*.

NZ IAS 34 prescribes the minimum content of an interim financial report and also prescribes the principles for recognition and measurement in financial statements for an interim period. At present, the OiC for the off quarters (Schedule 3[12], paragraph 4) refers to the content requirements of NZ IAS 34, in that it specifies a list of financial items to be disclosed "to the extent that it is additional to the information that NZ IAS 34 requires the banking group to disclose when publishing interim financial statements". This by no means amounts to a clear instruction that the short form GDS has to comply with the content requirements of NZ IAS 34, and makes no reference to its recognition and measurement requirements. However, as a matter of practice banks' off-quarter disclosure statements do currently comply with NZ IAS 34 and state that they do.

Banks' KISs provide an example of summary financial and other information published by banks that do not satisfy the presentation requirements of NZ IAS 34. However, the nature of the content specified for the KIS is such that it would generally be considered to be outside the mandate of NZ IAS 34.

The rationale for not requiring off-quarter disclosure statements to include all of the content specified by NZ Z

cross-tabulation of assets and liabilities by instrument type and accounting classification, and full detail of the terms of all loan capital issues.

under the option of retaining the KIS, it would be additionally problematic to produce a consumer-focussed document that nevertheless contained all the information required by NZ IAS 34.

Although we would expect banks to be able to produce these classes of information relatively easily since they are prepared for NZ IAS 34 compliance at the half year, removing them from the public disclosure would still represent some compliance savings.

Possible drawbacks of not requiring NZ IAS 34 compliance include the following:

NZ IAS 34 includes guidance on the preparation and the presentation of the financial numbers to be included in an interim report. With no reference to NZ IAS 34, it would not be clear what the required reporting standards would be, and there would be no assurance that banks were preparing the numbers on a consistent basis.

To get round that problem, the disclosure regime could specify that the off-quarter disclosure is to be prepared as if NZ IAS 34 applied, but with the exception of specified items in NZ IAS 34's presentation requirements. In that case banks would not be able to state that the statement was prepared in accordance with NZ IAS 34.

Another possible concern is that NZ IAS 34, as it derives from an internationally-agreed minimum standard, provides a convenient basis for demonstrating sufficiently frequent updates of relevant information. Without this, it would raise the question whether the Securities Act exemptions could continue to be justified.

Q9. Do users of disclosure statements agree with our assessment that the items noted above are of little interest at the off quarters?

Q10. How concerned are you about the additional length of off-quarter disclosure if NZ IAS 34 applies?

Q11. Does not requiring NZ IAS 34 compliance for off-quarter disclosure raise any concerns?

4.1.2 NZ IFRS 7 Appendix E

NZ IFRS 7, the New Zealand implementation of IFRS 7 *Financial Instruments Disclosure*, includes Appendix E *New Zealand-Specific Additional Disclosure Requirements Applicable to Financial Institutions* that applies to banks (among other financial institutions). The disclosure in Appendix E was primarily based on the New Zealand-specific disclosure requirements previously located in NZ IAS 30 *Disclosures in Financial Statements of Banks and Similar Financial Institutions*, and prior to that FRS 33 *Disclosure of Information by Financial Institutions*, to retain regulatory disclosure requirements.

The Basis for Conclusions that accompanies Appendix E notes the FRSB's concerns regarding Appendix E, and the FRSB's acknowledgement that its constituents supported the need for Appendix E. Our view is that in light of the changes that have taken place in the regulatory space over time and the fact that practice has evolved, it is an appropriate time to reconsider the previous rationale for requiring Appendix E.

The case for revisiting the previous rationale for requiring Appendix E is supported by our analysis of what banks disclose. Our analysis has identified significant overlaps between NZ IFRS 7 Appendix E and our on quarter OiC requirements.

We think the most helpful approach is

Under our proposals, NZ IAS 34 will apply to half-year GDSs and may or may not apply to off-quarter disclosure (as discussed above). NZ IAS 34 requires previous period comparisons in interim reporting as noted above, but it does not mandate parent as well as group reporting. Also, the requirements for comparison figures only apply to the financial information that NZ IAS 34 requires to be disclosed. Thus additional information that the Reserve Bank specifies can be for the current period only and also for the banking group only.

In implementing Pillar 3 for the IRB banks[13], we took the view that the volume of additional information required was such that it would not be helpful to require previous period comparisons. We also focused mainly on group rather than solo capital adequacy. We think this is a useful precedent for other areas of disclosure added on by the OiCs. We have not heard any concerns from expert users of GDSs, who can generally carry out their own comparisons with previous GDSs if they need to.

We therefore propose that most of the additional information that we require for the half year and off quarters will be at the current balance date or covering the most recent period only. In some cases this may not be feasible, for instance if we want to specify particular items to be included in the income statement, then NZ IAS 34's requirements on the periods that the income statement should cover will apply.

We also propose that the additional information required by the OiCs will generally be on a consolidated-only basis at the half year and the off quarters, but remaining on the same basis as now at the full year. While publication of the solo information exerts market discipline to prevent any perverse group structures, we think that an annual update for most of the information is sufficient. One exception is solo capital adequacy (see section 4.2.5 below), where summary solo ratios are currently required every quarter: we plan to reduce the frequency of this from quarterly to six-monthly.

This will not make much difference for the full-year disclosure, but can give significant further reductions in the volume of material at the other periods.

Q14. Do you agree that reduced amounts of previous period comparative information will on balance be beneficial for users of disclosure statements?

Q15. Do you agree that once a year is sufficiently frequent for an update on the solo bank's financial position?

4.1.4 Options for the Supplemental Disclosure Statement (SDS)

The SDS for locally-incorporated banks is required to include the following documents:

> if the bank has a material guarantee of its obligations, a copy of the guarantee contract and a copy of the guarantor's financial statements (except for government guarantors);
>
> if a person has entered into any material cross-guaranteeing arrangements with the bank, a copy of the contract (if a single contract is available); and
>
> if the bank calculates its aggregate credit exposure to connected persons on a net basis, a copy of the bilateral netting agreement and, if applicable, a copy of an external opinion confirming the robustness of the agreement.

[13] Banks accredited to use their own IRB (internal ratings based) models for determining their capital requirements for credit risk.

The GDS has to refer to the existence of any such guarantees or netting arrangements, so the thought was that any concerned reader of a GDS should be able to get hold of the background documentation. The idea of having a separate SDS was to keep this material, which will tend to be rather lengthy and static, out of the GDS (they can be over 200 pages). Banks usually publish their SDSs only on their websites, undated.

However, directors are required to sign off the SDS each quarter as part of a bank's overall disclosure, and any person can request a copy of the most recent SDS immediately from the head office, or within 5 working days if at a branch. This does impose some compliance costs on the banks. Our view is that the likely benefit of requiring these documents to be published is so low that it does not justify any compliance burden. The document that is currently most likely to be of interest, namely the contract containing details of the New Zealand government retail guarantee for each bank, is available on the Treasury website in any case.

Some additional material on banks' risk modelling approaches was added to the SDS requirements as part of the Basel II Pillar 3 disclosure in 2008. However banks have generally opted to keep this material (1-2 pages at most) alongside other Pillar 3 disclosure in the GDS. We propose to group that material with other risk management disclosures in the GDS (see discussion in 4.2.2).

Accordingly, we propose to cut the current requirement to publish the SDS.

As an alternative to losing from the public domain altogether some of the documents that are in the SDS, there could be a requirement that a bank must provide a copy of any of these documents, in response to a request made in writing to the bank's [illegible]

Dual-registered branches

In this case, the global banking group's New Zealand operations are currently required to be disclosed at four different levels of consolidation:

	Branch disclosure	NZ subsidiary disclosure
Full and half year	(1) Business of the branch on a stand-alone basis (2) "NZ banking group", that is, the branch, the NZ subsidiary on a consolidated basis, and any other NZ subsidiaries of the overseas banking group	(3) Business of the locally-incorporated subsidiary on a stand-alone basis (4) Consolidated figures for the subsidiary, including all of its subsidiaries.
Off quarters	As for (2) above	As for (4) above

In addition, the SDS for the branch must contain the following:

the most recent publicly available financial statements of the overseas bank and overseas banking group.

if the overseas bank carries on insurance or non-financial business in New Zealand outside the New Zealand banking group, the most recent publicly available financial statements for each of those businesses (as applicable).

The general view we have formed from talking to users of GDSs is that their main interest is either in the New Zealand subsidiary's figures on a consolidated basis, or on the banking group's New Zealand banking activities as a whole. They pay less attention to the accounts of either the branch or the subsidiary on a stand-alone basis. While it is the locally-incorporated entity that stands or falls as a legal entity, its risk cannot be considered without taking its subsidiaries into account. And the activities of a related New Zealand branch also need to be taken in to account to a greater or lesser degree, to form a view on the group's activities in New Zealand as a whole: this depends on how intertwined the branch and subsidiary's businesses are, which varies according to business model.

On the other hand we think it is important that there is at least some disclosure on the branch as a separate entity, since it is a registered bank subject to prudential supervision by the Reserve Bank.

We therefore propose to reduce the scope of branch disclosure in line with that for locally-incorporated banks: that is, financial statements and other disclosure for the stand-alone branch would only be required in the full-year disclosure, and for the other periods only the New Zealand banking group disclosure would be required.

We plan to remove the separate SDS for branches just as for locally-incorporated banks. For the financial statements currently required in the SDS, we propose the following:

the most recent published financial statements of the overseas bank and overseas banking group should be easily accessible in New Zealand (for example, from the local website, or on request from head office). We think the condition of the global bank is the main question for anyone placing money with the branch.

the requirements relating to financial statements of insurance and non-financial business outside the New Zealand banking group should be dropped from our disclosure regime. These will still be publicly available, but we think they are of such specialised interest that anyone

The RBNZ imposes a limit of $200 million on the total amount of retail deposits a branch may take, unless there is both adequate disclosure in the home country, and the home country's insolvency regime does not give preferential treatment to depositors in that country.

Timeliness of information on the branch is much less important than that on the banking group as a whole. In some cases, banking group information is published in the home country on a quarterly basis, and in many cases the group will also be subject to the continuous disclosure requirements of an overseas stock exchange.

We think there are good arguments for removing the off-quarter disclosure requirement for stand-alone branches, either altogether, or subject to certain criteria.

Q18. Do you agree with our assessment of user needs for the various types of branch disclosure?

Q19. What are your views on the proposed changes in branch disclosure?

Q20. If the requirement for off-quarter disclosure by stand-alone branches is made subject to certain criteria, what do you think those criteria should be?

4.1.6 Improved comparability in certain key areas

<u>Retail mortgages.</u> Figures on mortgage lending are of particular interest to external commentators. However, the figures presented in bank's disclosures are on a number of different bases, varying both across banks and within a given bank's GDS. This greatly complicates assessment of matters such as the analysis of growth in individual bank's mortgage lending and their respective market shares, and has resulted on occasion in basic, but completely understandable, errors in published analysis.

Examples of the reasons for the differences and the problems arising are:

> Residential mortgage lending can include just lending for owner-occupied house purchase, or it can include lending secured on residential property for investment purposes, or it can also include small business lending secured on residential property.
>
> Totals can include off-balance sheet lending commitments as well as loans on the balance sheet (although this at least is normally clear from the context).
>
> A number of different terms are used, including "housing lending", "residential mortgages", "exposures secured by residential mortgages", "retail mortgages", "term loans–housing", "real estate lending (mortgage)", "fixed rate mortgages" (along with floating rate). In some cases explanatory text is provided, but this is not really sufficient to understand all the differences. It appears that "retail mortgages" generally excludes business lending but "residential mortgages" goes wider, but the distinction is not adequately clear.
>
> The numbers disclosed are to meet a number of different requirements. These include figures within the breakdowns of maximum exposure to risk, and lending by industry sector (both within the analysis of credit risk management required by NZ IFRS 7), figures for components of the bank's capital adequacy calculation, and amounts which are required to be broken down by loan-to-valuation ratio (LVR).

The basis of the capital adequacy numbers varies between figures under the Basel II IRB approach (where banks are allowed more flexibility in their categorisation of exposures), the Basel II standardised approach, and the Basel I approach which applies to overseas bank branches, and also to New Zealand financial reporting group figures for dual-registered banks.

Sectoral credit risk concentration figures sometimes include a line for some form of housing lending, but sometimes only include a total personal lending figure.

Finally, it is in many cases not possible to reconcile any of the figures in the disclosure statement with the figure for "NZ$ lending to households – housing" that is privately reported to the RBNZ on the Standard Statistical Return (SSR).

This is a complex area, and we have not yet succeeded in developing a fully worked-out proposal. Our thinking on this so far is the following:

The capital adequacy disclosure on mortgage lending should be considered separately from disclosure for other purposes. This includes the LVR analysis, which we think should be tied across more closely to the capital adequacy numbers, as discussed in more detail below. The focus of these numbers is more on the bank's risk profile rather than the housing market.

We could require that the sector lending concentration table always include a row for mortgage lending, but to be useful that would have to be tightly defined. If we generally require the breakdown to be based on ANZSIC[14] codes as proposed, then lending to a small business that is secured by a residential mortgage would normally be included in the industry sector to which that business belongs.

As a complement to this approach, we could require disclosure of the figure for the widest possible definition for residential mortgage lending, br to fig

<u>*Mortgage LVR disclosure.*</u> Banks subject to the IRB approach under Basel II are required to disclose a breakdown of their mortgage lending categorised by LVR. The total this applies to is defined as "total exposures secured by residential mortgages as used to calculate the Registered Bank's pillar one capital requirement for credit risk". Standardised banks are subject to similar requirements, with the only difference being that is that, in place of the 0%-60%, 60%-70%, and 70%-80% buckets for the IRB banks, they disclose a single LVR bucket of 0%-80%.

In addition to the problems noted above of comparability with other mortgage lending figures, there are also inconsistencies across banks in the way the LVR breakdown is produced. These mainly arise with the IRB banks, given the greater flexibility that the IRB approach allows in determining exposure classes. The problems include:

> Lack of clarity about precisely which exposures should be included in the disclosure. In particular the requirement does not specify how to treat off-balance sheet exposures, and whether the disclosures should be limited to exposures classified within the 'retail' asset class for capital adequacy purposes.
>
> Lack of clarity about how to treat exposures for which LVR information is missing.

In addressing these problems, as discussed above, our preference is to aim for consistency between the LVR disclosures and other Pillar 3 capital-related disclosures, rather than with other housing-related disclosures. We therefore propose the following amendments to give readers greater clarity on what the LVR numbers represent, and to allow more meaningful comparisons across banks:

> *Missing values.* Accounts that are missing LVR information should be included in the highest LVR bucket. This would mean that the riskiness of the mortgage book could be overstated but would never be understated. It would give banks an incentive to capture LVR information, and is consistent with the approach we expect banks to take in their capital calculations.
>
> *Off balance sheet exposures.* The LVR disclosure should include off balance sheet exposures that are included in the regulatory capital calculation (adjusted to an on-balance sheet equivalent where this is consistent with the capital calculation). In our view this would best represent the risks, and would of course be consistent with the capital calculation. In some cases LVR information is not available for pre-approved loans, and in this instance the argument for categorising such loans in the highest LVR bucket would not make sense. In these cases we propose that banks assign an average LVR to such exposures (eg the average LVR of loans originated in the asset class in the last 12 months).
>
> *Asset class.* The LVR buckets used for disclosure purposes are consistent with those used to calculate regulatory capital requirements for mortgage retail credit risk. Restricting the LVR disclosures to retail exposures only would therefore increase the transparency of the capital calculation. However this approach would not provide a full picture of housing risk for those banks that classify some housing exposures within their corporate rather than retail exposure class for capital adequacy purposes. One solution would be to require disclosure of LVR information for both retail and corporate housing exposures, with retail exposures identified separately.

Q23. Have we accurately identified the problems with the LVR disclosure requirements?

Q24. Do you think our proposed approaches are the best way of dealing with accounts that have no LVR information and with off balance sheet exposures?

Q25. Do you think LVR information on mortgages classified as corporate (as well as retail) is important?

Q26. Do you think LVR disclosures should be we d th2cKoa2Up

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out additional prudential disclosure from financial statements: that would remove this complexity, but we do not think that that on its own provides enough reason for going down that route.

We have not heard any arguments in favour of changing the depth and frequency of audit review of the disclosures (in either direction), apart from some concern that it is not possible to obtain a more robust assurance opinion on the capital adequacy information. We therefore propose to keep broadly the same audit requirements as at present, based on full scope audit at the full year and review at the half year.

We will however consider putting in place a rolling programme of audits of the capital adequacy information disclosed by banks, with the scope to be discussed with banks and their auditors outside the disclosure regime.

Q28. Do you agree with our assessment of the current audit requirements?

Q29. Do you have any preferred alternative approach for the revised disclosure regime?

4.2 PROPOSED CHANGES IN DISCLOSURE OF SPECIFIC SUBJECT AREAS

4.2.1 Disclosure of accounting policies

Requirements to explain accounting policies used in preparing the financial statements are set out in NZ IAS 1 *Presentation of Financial Statements* paragraphs 117-124 and in NZ IFRS 7 paragraphs 21 and B5. The NZ-specific paragraph E8 of NZ IFRS 7 and on quarter OiC Schedule 4:4[16] require disclosure of accounting policies in relation to a number of specific instruments. In our view, none of these additional requirements is likely to add to what readers of GDSs can learn about a bank's accounting policies. Where a particular class of instrument is material to a bank's business, the general NZ IFRS requirements should result in its accounting treatment being described. For instance, NZ IAS1 paragraph 119 states:

"In deciding whether a particular accounting policy should be disclosed, management considers whether disclosure would assist users in understanding how transactions, other events and conditions are reflected in reported financial performance and financial position. Disclosure of particular accounting policies is especially useful to users when those policies are selected from alternatives allowed in NZ IFRSs."

This might lead to disclosure being dropped in some cases, but that would only be where it is not currently informative. For instance, the descriptions of policies on classifying loans as over 90 days past due tend to be tautologous. Overall this may not reduce much the total volume of disclosure in full-year disclosure statements, but we think there is benefit in removing superfluous compliance requirements that banks need to check.

For disclosure other than at the full year, banks would only need to disclose material updates in accounting policies.

Q30. Do you agree with our assessment that the additional requirements in the OiCs and in NZ IFRS 7 Appendix E are unnecessary to ensure that users of disclosure

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16 Schedule 4 is "Supplementary financial disclosures and asset quality" and section 4 deals with additional accounting policies.

statements have sufficient information on accounting policies to be able to understand the financial statements?

4.2.2 Disclosure of risk management approaches

Schedules 9 and 10[17] of the on quarter OiC specify disclosure of various aspects of a bank's risk management, including, where relevant, its modelling of credit and operational risk under the Basel II capital adequacy framework. A certain amount was added to these requirements in 2008 to implement Basel's Pillar 3 disclosure requirements. Apart from Schedule 9 paragraphs 4 and 5, the required disclosure either follows what is required by Pillar 3, or overlaps with NZ IFRS requirements, or in a number of cases both.

These are designed to be a coherent set of requirements rather than additional fragments. For instance, Schedule 9 paragraph 1 lists all the risks on which we wish to see disclosure, rather than just those that are required for Pillar 3 implementation but are not specified in NZ IFRS 7. Since there is no scope to reduce the amount of what is disclosed here (which we regard as useful in any case), we prefer not to change the way the requirements are expressed. Also, Schedule 10 disclosures can currently be published within the SDS, but with the proposed dropping of the SDS (see section 4.1.4) they would be merged with the Schedule 9 requirements for publication in the GDS.

The only purely OiC add-ons are Schedule 9 paragraph 4, which requires a description of how a bank reviews its risk management systems, and Schedule 9 paragraph 5, which requires information on the bank's internal audit function. We believe this is sufficiently important information that it should continue to be disclosed.

Both the NZ IFRSs and Pillar 3 only require annual disclosure in these areas. We think this is sufficient unless there are significant changes. We therefore propose to require only material updates in the half-year and off- [illegible]

that this exclusion be extended to banks, so that only large exposures to banks rated below A- would be covered.

the breakdown of the reported large credit exposures into those of investment grade, those below investment grade, and those that are unrated can also be simplified. In most cases, a statement of the aggregate end-period balance and a statement that all counterparties are rated investment grade will suffice (rather than a full table showing nil amounts in the other rows as at present).

the option between using end-period equity and the equity amount on the date of the peak exposure should also dropped, as banks do not use the second option (as far as we have been able to tell).

we also think that the most recent position is the key information for assessing risk, and disclosure of previous period amounts can be dropped. Analysts can always put together a run of data from previous disclosure statements.

We do however think that this slimmed-down information should be published every quarter. It should include figures for peak intra-period exposures over the quarter, as well as end-period figures.

Q33. Do you think that the proposed reduced disclosure on credit exposure concentration still presents the essential information?

4.2.4 Disclosure of credit risk impairment information

Loans that are impaired or in other problem categories, and impairment allowances are another area of crucial interest for readers of GDSs, and we do not think that the financial reporting standards (without NZ IFRS 7 Appendix E) would necessarily result in adequate disclosure in this area. However, the current requirements in the full and half-year OiC Schedule 4 and in NZ IFRS 7 Appendix E overlap significantly with one another and also include information that is of limited value. We propose more focused disclosure, taking into account the following considerations:

The categories "restructured asset", "financial asset acquired through the enforcement of security" and "other individually impaired asset" (defined in NZ IFRS 7 Appendix E) are not useful, as discussed further in Appendix 6 below.

An ageing analysis of past due assets is required by NZ IFRS 7 paragraph 37(a). We think it is useful to specify specific time bucket to improve comparability across banks, but we do not think it is necessary to show movements into and out of any given bucket over the period.

Pillar 3 requires the analysis of impaired assets to be broken down by major risk-weighting category (retail mortgages, other retail, corporate), and we have also had feedback from users that this break-down is useful.

References in the OiCs to "allowances for impairment loss created in respect of *non-financial assets*" should be dropped, since this is not a focus of interest for bank disclosure, and this will be appropriately covered by a range of other NZ IFRSs.

"Other assets under administration" and undrawn balances on facilities provided to problem borrowers are useful information, but both can be reported as end-period balances only, and off-balance sheet problem exposures should relate to individually impaired assets only (rate e –

Loans and advances at fair value

For loans and advances designated as at fair value through profit and loss which are credit impaired, we think there should be separate disclosure, analogous to the above:

> changes in the fair value of loans that is attributable to changes in their credit risk, as required by NZ IFRS 7.9, should be broken down as above for individual and collective credit impairment allowances.
>
> loans at fair value on which there have been credit-risk related changes in fair value should be disclosed along the lines of individually impaired assets above (Banks have in practice found informative ways to disclose this information, for instance describing such loans as "deemed to be impaired").

Nil returns would not be required from banks that do not have any credit-impaired fair-valued loans (as at present).

Past Due Assets

We propose that the required ageing analysis of past due assets should have to include (but not be limited to) end-period balances in the following time buckets:

> at least 30 days but less than 60 days past due
> at least 60 days but less than 90 days past due
> at least 90 days past due.

Other categories

We think the following items should still be disclosed, but only the end-period balances:

> Other assets under administration
> Undrawn balances on lending commitments to counterparties for which drawn balances are individually impaired

Six-monthly disclosure

Six-monthly disclosure should be at the same level of detail as full-year disclosure. However, in line with the rest of the disclosure requirements, only consolidated figures would be required. Banks would also disclose the amount of renegotiated loans, as if NZ IFRS 7 paragraph 36(d) applied at the half year.

Off-quarter disclosure

For the off quarters, the only disclosure required would be: the summary figures in the following table; separate, analogous disclosure for loans and advances at fair value; and the end-period balance of 90 day past due assets. (As at the full and half year, the information shown would also be broken down into the major Pillar 3 risk-weighting categories.)

Individual impairment allowance	*Collective impairment allowance*	*Individually impaired assets*
Charge (credit) to income statement for increase (decrease) in individual credit impairment allowance	**Charge (credit) to income statement for increase (decrease) in collective credit impairment allowance**	
Closing balance	**Closing balance**	**Pre-allowance closing balance**

Q34. Do you think that the proposed revised disclosure on credit impairment has a better focus on the essential information?

Q35. Is there a good case for keeping disclosure of any of the items we are proposing to drop?

4.2.5 Disclosure of Basel Pillar 3 information

The Pillar 3 requirements published by the Basel Committee are for disclosure of detailed quantitative capital adequacy information every six months, and of detailed qualitative information annually. "Significant" banks are expected to disclose their Tier 1 and total capital ratios, and their components, quarterly. We propose to reduce the frequency of detailed disclosure to bring it into line with these Basel requirements. The discussion of risk management disclosure above deals with the Pillar 3 qualitative disclosure.

For the quantitative disclosure, we propose only the following minor changes at the full and half year. In the disclosure of market risk:

> previous period comparisons and figures as a percentage of the bank's equity will be dropped, in line with all the other detailed figures on capital requirement
>
> the intra-period peak exposures will cover the most recent six months rather than three months (since this will not be disclosed in the off-quarters)

For banks accredited to use internal ratings-based modelling approaches under Basel II ("IRB banks"), we propose to cut the requirement to disclose capital adequacy ratios on a Basel I basis. They would however need to disclose summary capital ratios for the solo registered bank at the full and half year, using the Basel II calculation. This is subject to reaching agreement on a satisfactory method for carving out the solo capital requirements from the modelled group requirements.

IRB banks are required to multiply all risk-weighted asset (RWA) figures for credit risk within the IRB approach by a scalar set in their conditions of registration. Banks are required to disclose each RWA figure after applying the scalar. This can lead to confusion: for instance, some banks show exposure-weighted risk weights including the scalar, others do not. We suggest that the impact of the scalar should only be shown at the final stage of aggregating capital requirements.

For the off-quarter quantitative disclosure of capital adequacy, we propose to substantially reduce the current full detail required at the full and half year, to the following summary information:

All banks	
Tier 1 capital ratio	
Total capital ratio	
Tier 1 capital before deductions	

Q36. Do you think that the proposed revised disclosure on capital adequacy includes sufficient information at the off quarter?

Q37. Do you see any need for banks to disclose detailed analysis of capital instruments and reserves in the off quarter?

4.2.6

On demand	Next day to 1 month	Over 1 month to 3 months	Over 3 months to 6 months	Over 6 months to 1 year	Over 1 year to 5 years

This starts from the time bands suggested in NZ IFRS 7 paragraphs B11 and E21, and adds an additional split at 6 months. We think this is the minimum needed to address the concerns about the lack of comparability and insufficiently short time bands.

NZ IFRS 7 paragraph B11E states:

"An entity shall disclose a maturity analysis of financial assets it holds for managing liquidity risk (eg financial assets that are readily saleable or expected to generate cash inflows to meet cash outflows on financial liabilities), if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk."

In our view, the conditional in this statement for such information to be necessary will invariably be met by New Zealand registered banks. Broadly, the information we think is of interest is the value of marketable assets that the bank holds for liquidity risk management purposes, broken down by broad asset categories, and including any assumptions about the amount of time needed to realise those assets for cash.

The liquidity policy BS13 prescribes precise definitions of liquid assets. Although there may be some differences between this list and the securities a bank holds for its internal liquidity risk management, it has the advantage of being comparable across banks. We will give further consideration to what sort of disclosure we might require of banks' holdings of liquid assets as defined in BS13.

NZ IFRS 7 paragraph E19(a) requires a maturity analysis of all financial assets (not just marketable assets) on the same basis as for financial liabilities. This is asking for something different than what is required by paragraph B11E. We think disclosing a separate picture of the overall contractual maturity mismatch of the balance sheet is helpful, and if asset maturities are included they clearly need to be in the same time buckets as liability maturities. Assuming that Appendix E is cut, we would need to include this requirement in our disclosure regime.

Although this ties in to NZ IFRS 7 requirements that will only apply at the full year, we propose that this disclosure be required every quarter. At the half year and off quarter, only consolidated figures would be required, and not the previous period comparisons.

Q38. Do you agree with our assessment of the information that is important for assessing a bank's liquidity risk profile?

Q39. Do you think that the proposed revised disclosure on liquidity risk gives a more useful overview of a bank's liquidity position at the reporting date?

4.2.7 Other proposals for revised disclosure in specific subject areas

<u>*Exposure concentrations*</u>. NZ IFRS 7 requires disclosure of concentration of risk exposure in relation to a bank's key risks (typically credit risk, liquidity risk and market risk). NZ IFRS 7 paragraphs E11 and E12 add precision to this, by specifying that this should include concentrations by customer, industry or economic sector, and by geographic sector, and refer as an example to ANZSIC codes. We think that the use of ANZSIC code breakdowns should be mandated, and therefore propose that these requirements from Appendix E, suitably

adapted, should be captured in the disclosure OiCs, consistent with our preference to remove NZ IFRS 7 Appendix E as a whole.

Users have indicated that this information on credit and funding exposure concentrations is important. They have noted that banks use different groupings in their ANZSIC code breakdown of credit exposures, making cross-bank comparison harder. However, we think there is a limit to how far we can go in spelling out the breakdown, as a given sector may represent a material credit exposure concentration for one bank but not another. Nevertheless, we propose that lending to the agricultural sector should be separately identified. We also discuss in Section 4.1.6 ways in which retail mortgage lending could be more helpfully identified.

We propose that data on funding and lending concentrations be required both at the half year and in the off-quarters, but only on a consolidated basis and without previous period comparisons.

Interest rate re-pricing schedule. This is another area in which users have specifically expressed interest, although again with concerns about comparability. We suggest that the requirement currently in NZ IFRS 7 Appendix E (paragraph E22) is replaced by a more specific requirement in the OiCs with the following maturity buckets specified, and that this should be disclosed every quarter (current period and consolidated only, except at the full year). A bank could provide a further breakdown within any of these maturity buckets if it chose to:

Up to 3 months	3 to 6 months	6 to 12 months	1 to 2 years	Over 2 years

Balance sheet specified items. Currently, full and half-year balance sheet items are governed by NZ IFRSs, including the specific additional rows required by NZ IFRS 7 paragraph E3. Off-quarter disclosure is specified in the OiCs, and includes the items listed in E3. Our preference (as noted) is for Appendix E of NZ IFRS 7 to be removed entirely. We expect

prudential limits normally imposed on locally-incorporated banks in their conditions of registration, as prescribed in Handbook document BS8 Connected Exposures Policy. This disclosure is in addition to the quite extensive disclosure required by NZ IAS 24 *Related Party Disclosures* in full-year financial statements, and tends not to be closely related to it (it relies on a definition of exposure specified in BS8, which generally produces larger, ie more conservative gross numbers).

If a bank was to breach its connected exposure limit, it would have to disclose that breach in its next disclosure statement. It seems to us that that provides the main market discipline on the bank, rather than the need to disclose the numbers every quarter demonstrating compliance. We have not heard from any user who finds this information useful, so we propose to drop it. If anyone does find value in it, we could reduce the frequency of its disclosure to half-yearly, with the peak exposure information covering the previous six months rather than three, and cut the requirement for previous period comparisons.

Q40. Do you find the information on connected exposures valuable? If so, is reducing the frequency and comparators an acceptable alternative to dropping it altogether?

<u>Related party transactions.</u> Our proposals mean that the detail required by NZ IAS 24 will only be included in the full-year disclosure. Total amounts due to related parties are currently required by the off-quarter OiCs, but not amounts due from related parties. We suggest that at least some information on related party balances is important for readers on a regular basis. We propose that disclosure other than at the full year should show at least the total amounts due from and to related entities at the balance date, on the same basis as the full-year disclosure under NZ IAS 24. It should also include any material transactions or material changes in arrangements with related parties over the period.

<u>Historical summary of financial statements.</u> A five year summary of key profit and loss and balance sheet items is currently required at the full and half year. While in our view this can provide useful context for the bank's latest figures, readers of disclosure statements have generally told us they have little interest in this. We propose to drop this requirement unless we hear strong support for it in feedback on the consultation.

Q41. Do you agree that the historical summary of financial statements is of little use?

<u>Securitisation, funds management, other fiduciary duties, and marketing and distribution of insurance products.</u> A detailed description of the banking group's involvement in these activities and some quantitative information is required at the full and half year, and only slightly less at the off quarters. This appears excessive to us. An annual summary, with brief updates in between as necessary, should be sufficient for readers to keep track of the risks. We propose the following streamlining:

- the description of the bank's involvement in these activities, and of arrangements to avoid adverse impacts, should be required annually, with disclosure in any other period only if there has been a material change.

- likewise, the statements about transactions being at arm's length will only be required annually, unless any transaction has <u>not</u> been at arm's length in the reporting period.

- the disclosure of amounts represented by the various activities, and of funding provided to entities conducting those activities, will be required half-yearly. Intra-period peak amounts will cover the latest half-year rather than latest quarter. Previous period comparative numbers will no longer be needed.

This will provide more than is required by NZ IFRS 7 paragraph E9, and thus supports the removal of that.

Insurance business. The total amount of insurance business conducted by the banking group (if any), and a 0unkof barate9, is quiredNd g), w i teTo gf

Appendix One: List of overlaps and duplications between on quarter OICs and NZ IFRSs and recommendation

Disclosure Requirements	On quarter OICs	NZ IFRSs	Recommendation for OiC
General disclosure – name, address	Schedule 3: 1	NZ IAS 1: 138 (a), 51(a)	Remove
General disclosure – parents' name, address	Schedule 3:2(a)(b)	NZ IAS 1: 138 (c)	Keep (OiC specifies parent bank)
General disclosure – pending procedure	Schedule 3: 13	NZ IAS 37	Keep (OiC more specific)
Presentation currency/rounding	Part 2,22(3)	NZ IAS 1,51(d)(e), NZIAS21	Keep (OiC specifically requires NZD)
Providing comparatives	In many schedules	NZ IAS 1, 38	Merged into one general requirement, except for Capital Adequacy
Accounting policies for trading securities	Schedule 4: 4(c)	NZ IAS 39,38; NZ IFRS 7,B5(c)	Remove (see discussion of accounting policies disclosure at 4.2.1)
Financial risk management – risk categories	Schedule 9: 1	NZ IFRS 7, 32	Keep (OiC specifies more, eg operational risk)
Risk management policies – objectives, policies, strategies, and process; nature of risks, measurement and monitoring	Schedule 9: 2(1),2(a)	NZ IFRS 7, 33(a)(b)	Keep (hard to disentangle – see discussion at 4.2.2)
Risk management policies – process for identify, measure and monitor exposures, incl. frequency of monitor/report	Schedule 9: 2(2)(c)	NZ IFRS 7, 33(b)	Keep (hard to disentangle – see discussion at 4.2.2)
Provision for credit impairment and reconciliation of impaired assets	Schedule 4:5-11	NZ IFRS 7: 16, 37, E5, E6, E16-E18	Rationalise OiC requirements on the basis that the NZ IFRS 7 App E requirements will be cut (see 4.2.4)
Reserves and retained earnings – description of nature and purpose of each reserve within equity	Schedule 5:A-5B,2(4)	NZ IAS 1, 79(b)	Cut (NZ IAS 1 level of detail is sufficient)
Listing name, nature of business, country of incorporation, percentage ownership of Controlled entities, associates and interests in joint entities/member of banking group	Schedule 3: 16	NZ IAS 24, 12, 14 NZ IAS 27, 43(b)	Remove
Funds under management and other fiduciary activities – nature and amounts, arrangements for ensuring such activities are separated from other activities	Schedule 8: 2(a), 3, 4	NZ IFRS 7, App. E:E9	Keep OiC annual requirements as long as the NZ IFRS 7 requirement is cut (see discussion at 4.2.7)

Appendix Two: List of items in On-quarter OiC (i.e. additional ones to NZ IFRSs) that should be kept or removed – on the basis that On-quarter OiC will apply to full-year GDS only. Recommendations for the half-year GDS are also provided.

Item	Disclosure Requirements	On quarter OiC	Recommendation For annual	Recommendation for half year
1	General disclosure – restriction on parent to support, other material matters	Schedule 3: 2(c), 18	Keep	Keep
2	General disclosure – guarantors, detail of guarantee	Schedule 3: 4, 6A, 6B, 7	Keep	State if present, more detail only if material update
3	Summary of five year accounts	Schedule 3: 15	Keep	Remove (see Q41)
4	Related party: management contracts, agency relationships, taxation grouping arrangements, debts or other amounts forgiven, transactions at nil or nominal value.	Schedule 4: 2(2)(a)-(e)	Cut (add little to already extensive requirement by NZIAS 24)	Cut
5	Accounting policies for the basis of classifying, and for recognising and measuring assets under administration	Schedule 4: 4(a)(ii)	Cut (see discussion of accounting policies disclosure at 4.2.1)	Covered by material update in accounting policies generally
6	Accounting policies for repurchase agreements, financial instruments used for hedging, accounting for leases, foreign exchange contracts, acceptances and endorsements of bills of exchange, loan transfers	Schedule 4: 4(b)(d)(e)(f) (g) (h)	Cut (see 4.2.1)	Covered by material update in accounting policies generally
7	Risk management policies – structure/organisation of risk management functions, systems and procedures for controlling risk	Schedule 9: 2(2)(b), (d)	Keep (Pillar 3)	Material update only
8	Risk management policies – reviews of risk management systems, internal audit function	Schedule 9: 4 & 5	Propose to keep (see 4.2.2 and Q32)	Material update only (if kept for full year)
9	Risk management policies – credit risk mitigation	Schedule 9: 7	Keep (Pillar 3)	Material update only
10	Operational risk, Market risk, liquidity risk – description, explanation of the nature, how the risk is being monitored and controlled etc	Schedule 9: 1(b)-(f), 2	Keep	Material update only
11	Additional information on Basel II modelling approaches for credit risk and operational risk	Schedule 10	Keep (and move to GDS from SDS – Pillar 3)	Material update only
12	Income statement – net gain or loss attributable to derivatives used for hedging purposes that do not qualify as designated and effective hedging	Schedule 4: 3	Remove	Remove

Appendix Three: Full list of information currently required by OiCs that will be removed, streamlined or restructured, for half-year GDSs

Disclosure Requirements	On quarter OiC	Recommendation
Guarantors and details of guarantees		

Appendix Four: Recommendations to shorten the off-quarter GDSs (with reference to current off-quarter OiC)

Disclosure Requirements	Off-quarter OiC	Recommendation
General disclosure – name, address	Schedule 2: 1	Keep
General disclosure – parent and ultimate holding company info	Schedule 2: 2	Remove
General disclosure – interest in 5% or more of voting securities	Schedule 2: 3	Remove
General disclosure – directors (changes only)	Schedule 2: 4	Keep
Guarantees, guarantors, guaranteed obligations	Schedule 2: 5-9	State if present, more detail only if material update
Absence of supplemental disclosure statement	Schedule 2: 10	Remove – no longer applicable
Conditions of registration	Schedule 2: 11	Material update/breaches only
Credit rating information	Schedule 2: 12	Current ratings summary only
Director's statements	Schedule 2: 14	Keep
Auditor's report	Schedule 2: 15	Keep
Extra line items in Income Statement: net trading gains/losses, other gains less losses on financial instruments at fair value, profit/loss attributable to minority interest, and profit/loss attributable to equity holders of the parent	Schedule 3: 4	Sufficient detail to separate out fair value gains and losses and total changes in equity
Extra line items in Balance Sheet	Schedule 3: 4, B/S items 1-18	Broadly, to be consistent with face of balance sheet at full year. A few key items specified.
Extra balance sheet items: assets used to secure obligations, and assets not legally owned but presented in Balance sheet	Schedule 3:4, B/S items 22 & 23	Cut
Asset quality – generally	Schedule 3: 5-10	Streamlined and shortened
Asset quality – real estate assets, other assets acquired through enforcement of security, movement in allowances for impairment loss for non-financial assets	Schedule 3: 5, 7	Remove
Asset quality – credit risk on loans and receivables at fair value	Schedule 3: 9	Keep, within the above
Asset quality – breakdown by major type of credit exposure	Schedule 3: 10	Keep, within the above
Capital adequacy (quantitative)	Schedules 4, 4A-B	Short summary only
Concentration of credit exposures to individual counterparties	Schedule 5	Streamlined
Credit exposures to connected persons	Schedule 6	Cut
Securitisation, fund mgmt, insurance etc	Schedule 7	Cut
Insurance business	Schedule 2: 13	Cut
Risk management policies, only if any material changes	Schedule 8	Keep

Appendix Five: KIS – Assessment of Current contents and possible additions

Current Requirements	**Required Content**	**Recommendation**
Introductory statement for customers	...to provide customers and potential customers with information about financial condition of their bank...	Keep the format but paraphrase
Corporate info	Name, ultimate parent bank, country of domicile	Keep
Credit rating	Rating agency's name, type of rating, current rating and qualifications and any changes in the last 2 years	Keep
Government guarantee	Whether covered, and how to obtain more info	Keep, paraphrase
Profitability	Net profit/loss after tax, and as percentage of the 12 months total assets	Remove, to be replaced with P/L info
Size	Total assets, % change over the 12 months	Keep, but further breakdown into key balance sheet items
Capital adequacy	Tier one capital ratio, total capital ratio	Keep largely, remove Basel I ratios
Asset quality	Total individually impaired assets, % of total assets, total individual credit impairment allowance, impaired assets %; total collective credit impairment allowance, non-financial assets acquired through enforcement of security	Keep, but revised – a summary version of the general disclosure proposed (see 4.2.4)
Peak credit exposure concentrations	# of individual non bank and bank counterparties, in successive 10% of the banking group's equity	Simplified (see 4.2.3)
Credit exposure to connected persons	Peak end-of-day aggregate credit exposure (to connected persons and non-bank connected persons) as an % of tier one capital; any breaches	Either cut or streamlined (see 4.2.7)
Statement on availability of GDS/SDS		Keep (in respect of GDS)
Auditor's report		Keep
Recommended Additions	**Contents**	
Glossary	Explain technical terms such as what is capital, impairment, credit exposure in simple terms	
Director statements/signoff		
Key ratios	e.g return on equity, reinvestment rate. There are arguments for and against providing underlying data	
How to interpret	A page at the end to explain why particular ratios are important and how to interpret capital ratios etc	
Net loans and advances		
Income statement and Balance sheet	Current statements	
Asset quality & provision	Break down into 90 days past due etc, provide ratios as well.	

		Separate disclosure of financial assets acquired through the enforcement of security seems to us unnecessary on top of this, and in practice amounts disclosed by banks have been negligible. “Other individually impaired assets” is intended as the residual item, ie individually impaired assets that are neither impaired nor acquired through enforcement of security. It would no longer be needed if those two are cut.e 0

E14	Individual large credit exposures.	These requirements duplicate what is required by the OiCs, which we suggest is not very helpful in any case. Suggested improved disclosure, to be required by the OiCs, is set out in Section 4.2.3.
E15	Statement by branches on their disclosure of large exposures.	In relation to E14, this requires branches to state that the individual large credit exposures disclosed do not include exposures to those counterparties if they are booked outside New Zealand. Assuming this approach is retained for branches (as we propose), it is reasonable that this must be stated, since only locally-booked credit exposure is being compared to equity of the banking group globally. However, it should go alongside the rest of the large exposure disclosure requirements in the OiCs, and be cut from Appendix E.
E16	90-day past due assets	This can be cut from Appendix E as it is already covered in the OiCs, and we are proposing that it will continue to be disclosed quarterly (see Section 4.2.4).
E19 – E21	Liquidity risk	The requirement for an "on demand" maturity bucket for funding and for an asset maturity ladder are helpful, but the other requirements here have not delivered useful disclosure. We would prefer additional liquidity risk-related disclosure to be addressed within the Reserve Bank's prudential liquidity policy for banks, as discussed further at Section 4.2.6.
E22	Interest rate re-pricing schedule	From our discussions with users, it seems that there is some demand for this information, although to be really useful the maturity buckets need to be standardised.

Appendix 7: Consolidated Questions

Number	Questions	Section	Page
1	Do you think any of the above three options should be considered further? If so, which one and why?	**3.5.1**	**14**
2	Do you agree with our assessment that Options A and B are the main options for consideration?	**3.5.2**	**16**
3	Is there an alternative approach we should consider?		
4	What are your views on the relative merits of Options A and B?		
5	Do you think that replacing off-quarter disclosure with continuous disclosure is a feasible option for consideration?		
6	Can the banks give us hard information on the likely impact of the proposed changes on their compliance costs?	**3.6**	**17**
7	Do you agree that the delivery time at the half year should be shortened? How much do you think publication deadlines could be reduced in the light of the detailed proposals for change?	**3.7**	**17**
8	What are your views on the appropriate publication mechanism for bank disclosure statements?		**18**
9	Do users of disclosure statements agree with our assessment that the items noted above are of little interest at the off quarters?	**4.1.1**	**20**
10	How concerned are you about the additional length of off-quarter disclosure if NZ IAS 34 applies?		
11	Does not requiring NZ IAS 34 compliance for off-quarter disclosure raise any concerns?		
12	Do you agree with our analysis of the overlaps between Appendix E and other disclosure requirements?	**4.1.2**	**21**
13	Do you have a view on whether Appendix E is required or not?		
14	Do you agree that reduced amounts of previous period comparative information will on balance be beneficial for users of disclosure statements?	**4.1.3**	**22**
15	Do you agree that once a year is sufficiently frequent for an update on the solo bank's financial position?		
16	Is there any benefit in the documents currently in the SDS continuing to be made publicly available?	**4.1.4**	**23**
17	If so, does the alternative delivery mechanism proposed achieve that at acceptably low compliance cost?		
18	Do you agree with our assessment of user needs for the various types of branch disclosure?	**4.1.5**	**26**
19	What are your views on the proposed changes in branch disclosure?		
20	If the requirement for off-quarter disclosure by stand-alone branches is made subject to certain criteria, what do you think those criteria should be?		
21	Do you agree with our assessment of the problems with the various types of mortgage lending disclosure?	**4.1.6**	**27**
22	What are your views on the suggested ways of dealing with these problems, and do you have any alternative suggestions?		

23	Have we accurately identified the problems with the LVR disclosure requirements?		**28**
24	Do you think our proposed approaches are the best way of dealing with accounts that have no LVR information and with off balance sheet exposures?		**29**
25	Do you think LVR information on mortgages classified as corporate (as well as retail) is important?		
26	Do you think LVR disclosures should be used to provide greater transparency about the regulatory capital calculation?		
27	Do you think requiring LVR disclosures about both retail and corporate housing exposures would be costly or excessive?		
28	Do you agree with our assessment of the current audit requirements?	**4.1.7**	**30**
29	Do you have any preferred alternative approach for the revised disclosure regime?		
30	Do you agree with our assessment that the additional requirements in the OiCs and in NZ IFRS 7 Appendix E are unnecessary to ensure that users of disclosure statements have sufficient information on accounting policies to be able to understand the financial statements?	**4.2.1**	**30**
31	Do you agree with keeping broadly the current lay-out of the risk management disclosure requirements?	**4.2.2**	**31**
32	Do you agree that the additional disclosure on reviews of risk management systems and on internal audit should be retained?		
33	Do you think that the proposed reduced disclosure on credit exposure concentration still presents the essential information?	**4.2.3**	**3**