



CONTENTS OF THE FINANCIAL STATEMENTS

34	Guide to the Main Functions of the Reserve Bank	67	Risk Management Notes
35	Five Year Financial Summary	67	14. Risk Management
37	2001/2002 Budget Information	68	15. Operational Risk
37	Budget Assumptions	68	16. Market Risk
38	Budgeted Statement of Cost of Services	69	17. Credit Risk
39	Budgeted Statement of Financial Performance	73	18. Interest Rate Risk
40	Management Statement	76	19. Foreign Currency Risk
41	Audit Report	78	20. Liquidity Risk
43	2000/2001 Financial Statements	79	Consolidated Statement of Cost of Services Notes
43	Statement of Accounting Policies	79	21. Currency Operations
48	Consolidated Statement of Financial Position	79	22. Foreign Reserves Management
50	Consolidated Statement of Movements in Equity	80	23. Registry and Depository Services
51	Consolidated Statement of Cost of Services	81	Consolidated Statement of Financial Performance Notes
52	Consolidated Statement of Financial Performance	81	24. Interest Income from Financial Assets
54	Consolidated Statement of Cash Flows	81	25. Interest Expense on Financial Liabilities
56	Notes to be read as part of the Consolidated Financial Statements	81	26. Net Foreign Exchange Revaluation Gain (Loss)
56	1. Nature and Extent of Activities	82	27. Other Income
58	Asset Notes	82	28. Asset Management Expenses
58	2. Foreign Currency Marketable Securities	82	29. Other Operating Expenses
58	3. Derivative Instruments	83	Other Notes
59	4. Other Local Currency Financial Assets	83	30. Reconciliation of Operating Cash Flows with Reported Operating Surplus
59	5. Inventories	84	31. Consolidated Cash Balances
60	6. Fixed Assets	85	32. Statement of Commitments
61	Liability and Equity Notes	85	33. Subsidiary Companies
61	7. Other Deposits	85	34. Free Services
61	8. Miscellaneous Liabilities	86	35. Related Parties
62	9. Provision for Restructuring	86	36. Contingent Liabilities
62	10. Transfers to Retained Earnings and Provision for Transfer of Surplus	87	37. Income Tax
63	11. Equity	88	38. Custodial Activities
64	12. Fair Value of Financial Instruments		
65	13. Concentrations of Funding		

GUIDE TO THE MAIN FUNCTIONS OF THE RESERVE BANK

The Reserve Bank's outputs are classified according to the major functions of the Bank. Definitions of each output are provided below and where necessary further explanations are provided.

Monetary Policy Formulation:

Formulating and publicly presenting monetary policy to enable the Bank to maintain price stability, in the most efficient manner possible.

Market Operations:

Trading, liaising with and monitoring financial markets, to effectively implement monetary policy and maintain the Bank's capacity to intervene in financial markets in support of the orderly and competitive functioning of those markets.

Financial System Oversight:

Registering and supervising banks, promoting the efficiency and soundness of the New Zealand financial system and limiting the significant damage to the financial system that could arise from a bank failure or other financial system distress.

Currency Operations:

Maintaining the supply and integrity of legal tender currency to facilitate cash transactions in the community.

Registered banks pay the Reserve Bank the face value of the currency being issued to them. These funds are invested in New Zealand government securities, which are included in local currency financial assets on the Reserve Bank's balance sheet to back the currency in circulation liability. Currency in circulation is a non-interest bearing liability. However, the New Zealand government securities investment portfolio asset is interest-bearing. The income directly associated with the issue of currency is referred to as seigniorage and provides the Bank with its main source of income.

Foreign Reserves Management:

Maintaining the capability to counter circumstances of severe illiquidity in our foreign exchange market and maintaining the Bank's foreign reserves at a level and in a form suitable for foreign exchange market intervention.

The Crown has advanced foreign currency funds to the Reserve Bank, which the Bank has invested in foreign currency assets that are held as foreign reserves. These assets and liabilities closely match each other by currency, duration, and value. As a result, the Bank has limited exposure to interest and exchange rate movements in these overseas markets.

Banking Services:

Providing banking services to the government, settlement banks and appropriate overseas institutions to meet their banking needs and to facilitate effective implementation of monetary policy.

Overseas Investment Commission Secretariat:

Providing the secretariat of the Overseas Investment Commission. The Commission administers New Zealand's legislative controls on major inward foreign direct investment.

Registry and Depository Services:

Providing high quality depository, registry and settlement services to the securities market.

Other Outputs:

Producing other outputs which cannot be classified under the Bank's main functions. These include sundry economic policy advice and overseas representation and liaison.

FIVE YEAR FINANCIAL SUMMARY¹

Consolidated Statement of Financial Position ² As At	1997 June (\$m)	1998 June (\$m)	1999 June (\$m)	2000 June (\$m)	2001 June (\$m)
Assets:					
Foreign Currency Financial ³	5,677	6,522	6,493	5,898	6,054
Local Currency Financial	4,029	4,413	5,321	4,092	5,225
Other Assets	62	61	60	51	46
Total Assets	9,768	10,996	11,874	10,042	11,325
Liabilities and Equity:					
Foreign Currency Financial ³	5,676	6,519	6,487	5,899	5,908
Local Currency Financial	1,880	2,176	2,926	1,405	2,379
Currency in Circulation	1,665	1,733	1,885	2,160	2,463
Other Liabilities	151	164	171	177	170
Equity	396	404	405	400	405
Total Liabilities and Equity	9,768	10,996	11,874	10,042	11,325

Consolidated Statement of Financial Performance Financial Year Ending	1997 June (\$m)	1998 June (\$m)	1999 June (\$m)	2000 June (\$m)	2001 June (\$m)	2002 June Budget (\$m)
Net Investment Income	170.4	187.4	186.1	192.4	189.7	207.2
Other Income	10.7	10.7	11.7	11.4	9.2	9.1
Total Operating Income	181.1	198.1	197.8	203.8	199.0	216.3
Operating Expenses	37.8	37.0	44.2	44.4	38.7	37.4
Taxation ⁴	0.9	0.8	0.6	0.1	0.7	-
Surplus Available for Appropriation	142.5	160.3	153.0	159.3	159.6	178.9
Transfers to Equity	6.4	8.4	2.2	1.6	5.4	3.6
Payment to Government	136.0	151.9	150.8	157.7	154.1	175.3

1 Figures in this section have been rounded. Totals have not been adjusted for rounding error.

2 Where amounts have been reclassified, comparative figures have been restated.

3 The changes in the levels of Foreign Currency Assets and Liabilities over this period are largely due to changes in exchange rates.

4 There is no budgeted taxation expense as the Bank's subsidiary company (RBNZ Registry Limited) ceased trading on 30 June 2001.

Consolidated Statement of Cost of Services⁵	1997	1998	1999	2000	2001	2002
Financial Year Ending	June	June	June	June	June	June
	(\$m)	(\$m)	(\$m)	(\$m)	(\$m)	Budget (\$m)
Functions:						
Monetary Policy Formulation	6.1	6.7	7.2	7.2	7.4	8.3
Market Operations	2.8	2.8	2.8	2.8	3.2	3.5
Financial System Oversight	2.8	2.8	2.7	3.1	3.6	4.8
Currency Operations ⁶	15.8	14.0	19.6	19.2	12.9	8.8
Foreign Reserves Management	3.7	3.7	4.0	3.7	3.9	4.2
Banking Services	0.8	0.8	1.1	1.3	1.7	2.2
Overseas Investment Commission Secretariat	0.7	0.9	0.7	0.7	0.7	0.8
Registry and Depository Services ⁷	5.5	5.7	5.9	6.1	5.5	4.0
Other Outputs	0.7	0.6	1.3	0.8	0.9	0.8
Total	38.9	38.0	45.3	44.9	39.8	37.4
Less Intercompany Transactions	0.2	0.2	0.4	0.4	0.4	-
Total for Bank	38.7	37.8	44.9	44.5	39.4	37.4
Income Retained under Funding Agreement	11.4	11.2	11.9	11.8	10.8	10.0
Net Expenditure under Funding Agreement	27.3	26.6	33.0	32.7	28.6	27.4

The Consolidated Statement of Cost of Services shows the total cost of providing each function, including internal transfers between functions. It includes fees charged by the Registry and Depository Services function to other functions, which are netted off against Registry income in the Consolidated Statement of Financial Performance.

The Consolidated Statement of Cost of Services has been restated to show net expenditure under the Funding Agreement methodology applicable from 1 July 2000.

⁵ Figures in this section have been rounded. Totals have not been adjusted for rounding error.

⁶ The increase in Currency Operations expenses during the 1999 and 2000 financial years was largely due to the one-off effect of introducing polymer bank notes. These notes are expected to have a much longer life than the previous paper notes and result in lower note issue costs in future years.

⁷ Includes taxation expense.

2001/2002 BUDGET INFORMATION

The Reserve Bank's budget has been prepared for a 12 month period and is consistent with the Bank's accounting policies.

The 2001/2002 budget has been completed using interest and exchange rates prevailing at the time the budget was prepared. No allowance has been made for future changes in interest and exchange rates.

Budget Assumptions

The major assumptions underlying the preparation of the 2001/2002 budget are that:

1. the Bank performs the functions prescribed in the Reserve Bank of New Zealand Act 1989, and existing functions not directly specified in the legislation;
2. the levels of activity in the Foreign Reserves Management and Market Operations functions in 2001/2002 will be similar to the 2000/2001 levels;
3. the SWIFT interface to the Exchange Settlement Account System will become operational in October 2001; and
4. registry services processing operations will be provided by an external contractor from July 2001.

BUDGETED STATEMENT OF COST OF SERVICES

The Bank has budgeted to provide the following functions in 2001/2002.

	Operating Income Budget 2002 \$000	Operating Income Actual 2001 \$000	Operating Expenses Budget 2002 \$000	Operating Expenses Actual 2001 \$000	Operating Surplus (Deficit) Budget 2002 \$000	Operating Surplus (Deficit) Actual 2001 \$000
For the year ended 30 June						
Functions:						
Monetary Policy Formulation	9	10	8,310	7,431	(8,301)	(7,421)
Market Operations	14,160	14,612	3,473	3,194	10,687	11,418
Financial System Oversight	27	16	4,812	3,646	(4,785)	(3,630)
Currency Operations	180,023	176,215	8,755	12,881	171,268	163,334
Foreign Reserves Management	14,381	448	4,230	3,868	10,151	(3,420)
Banking Services	1,930	1,426	2,229	1,669	(299)	(243)
Overseas Investment Commission Secretariat	810	581	808	675	2	(94)
Registry and Depository Services	4,993	6,021	4,001	5,505	992	516
Other Outputs	1	3	799	883	(798)	(880)
Total	216,334	199,332	37,417	39,752	178,917	159,580
Less Intercompany Transactions ⁸	-	379	-	379	-	-
Total for Bank	216,334	198,953	37,417	39,373	178,917	159,580
Income Retained under Funding Agreement			9,966	10,815		
Net Expenditure under Funding Agreement			27,451	28,558		

8 There are no budgeted intercompany transactions as the Bank's subsidiary company (RBNZ Registry Limited) ceased trading on 30 June 2001.

BUDGETED STATEMENT OF FINANCIAL PERFORMANCE

	Budget 2002 \$000	Actual 2001 \$000
For the year ended 30 June		
Operating Income:		
Net Investment Income	207,213	189,736
Other Income	9,121	9,217
Total Operating Income	216,334	198,953
Operating Expenses:		
Personnel	17,077	16,734
Asset Management	5,033	6,078
New Currency Issued	3,707	4,689
Administration	1,473	1,319
Other	10,127	9,022
Total Operating Expenses	37,417	37,842
Loss on Revaluation of Bank Properties	-	817
Total Expenses	37,417	38,659
Operating Surplus	178,917	160,294
Taxation ⁹	-	714
Surplus Available for Appropriation	178,917	159,580


9 There is no budgeted taxation expense as the Bank's subsidiary company (RBNZ Registry Limited) ceased trading on 30 June 2001.

17 August 2001

MANAGEMENT STATEMENT

Pursuant to section 165 of the Reserve Bank of New Zealand Act 1989, we hereby certify that:

1. We have been responsible for the preparation of the annual financial statements and for the judgements used in them.
2. We have been responsible for establishing and maintaining a system of internal controls designed to provide reasonable assurance as to the integrity and reliability of the Bank's financial reporting.
3. In our opinion, the annual financial statements for the year ended 30 June 2001 fairly reflect the financial position and operations of the Bank.



Governor



Deputy Chief Executive



Deputy Governor

Auditors' Report to the Readers of the Financial Statements of the Reserve Bank of New Zealand

We have audited the financial statements on pages 43 to 88. The financial statements provide information about the past financial performance and cash flows of the Reserve Bank of New Zealand and Group for the year ended 30 June 2001 and their financial position as at that date. This information is stated in accordance with the accounting policies set out on pages 43 to 47.

Governors' responsibilities

The Governors are responsible for the preparation and presentation of the financial statements which give a true and fair view of the financial position of the Reserve Bank of New Zealand and Group as at 30 June 2001 and their financial performance and cash flows for the year ended on that date.

Auditors' responsibilities

We are responsible for expressing an independent opinion on the financial statements presented by the Governors and reporting our opinion to you.

Basis of opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. It also includes assessing:

- (a) the significant estimates and judgements made by the Governors in the preparation of the financial statements; and
- (b) whether the accounting policies are appropriate to the circumstances of the Reserve Bank of New Zealand and Group, consistently applied and adequately disclosed.

We conducted our audit in accordance with generally accepted auditing standards in New Zealand. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

We carried out other assurance services for the Reserve Bank of New Zealand. Other than these assignments and in our capacity as auditor, we have no relationship with or interests in the Reserve Bank of New Zealand or any of its subsidiaries.

Unqualified opinion

We have obtained all the information and explanations we have required.

In our opinion:

- (a) proper accounting records have been kept by the Reserve Bank of New Zealand as far as appears from our examination of those records; and
- (b) the financial statements on pages 43 to 88:
 - (i) comply with generally accepted accounting practice in New Zealand; and
 - (ii) give a true and fair view of the financial position of the Reserve Bank of New Zealand and Group as at 30 June 2001 and their financial performance and cash flows for the year ended on that date.

Our audit was completed on 17 August 2001 and our unqualified opinion is expressed as at that date.


Chartered Accountants

Wellington



RESERVE BANK OF NEW ZEALAND 2000/2001 FINANCIAL STATEMENTS

STATEMENT OF ACCOUNTING POLICIES

(a) Reporting Entity and Statutory Base

These are the consolidated financial statements of the Reserve Bank of New Zealand, a body corporate under the Reserve Bank of New Zealand Act 1989. These statements apply to the financial year ended 30 June 2001. They have been prepared in accordance with part VI of the Reserve Bank of New Zealand Act 1989.

In these financial statements, the Reserve Bank of New Zealand is also referred to as the "Reserve Bank" or the "Bank".

The Governor of the Reserve Bank of New Zealand authorised these financial statements for issue on 17 August 2001.

(b) Measurement Base

Unless otherwise stated, the measurement base is historic cost.

(c) Currency of Presentation

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

(d) Basis of Consolidation

The consolidated financial statements are prepared using the purchase method. All material inter-company balances and transactions are eliminated. Parent financial statements are not produced because the difference between the parent and group accounts is not material.

(e) Foreign Currency Conversions

Transactions in foreign currencies have been translated to New Zealand dollars using exchange rates applying on the trade date of transactions. Foreign currency financial assets and financial liabilities have been translated to New Zealand dollars using mid-market exchange rates applying at balance date. The following New Zealand dollar exchange rates for major currencies were used to convert foreign currency assets and liabilities to New Zealand dollars for reporting purposes:

	2001	2000
Euro	0.4791	0.4919
Japanese yen	50.22	49.44
United States dollars	0.4052	0.4685

(f) Financial Assets and Liabilities

The Bank presents financial assets and liabilities, and the associated income and expense streams, by distinguishing between foreign currency and local currency activities. Foreign currency activities mainly arise from the Bank's Foreign Reserves Management function. Local currency activities mainly reflect the assets and liabilities associated with monetary policy implementation, investment of the proceeds of issuing circulating currency and banking activities.

The separate reporting of these activities is considered to provide a better presentation of the Bank's financial position, financial performance and risk profile. The Bank considers that the combined reporting of foreign and local currency activities would weaken the informational value of the financial statements.

All financial assets and liabilities are recognised in the Statement of Financial Position on a trade date basis. This means that purchases and sales of financial assets are recognised from the date at which the purchase or sale is agreed.

Foreign Currency Marketable Securities

Foreign currency marketable securities are valued at quoted market mid-prices. Any premium or discount on purchase is capitalised and amortised over the term of the security on a constant yield to maturity basis. Changes in market value are recognised as an increase or decrease in the value of the Marketable Securities in the Statement of Financial Position.

Gains and losses arising from changes in the market value of foreign currency marketable securities are recognised immediately in the Statement of Financial Performance. Where the security is still owned, the gain or loss is reported as Gain (Loss) from Unrealised Price Revaluations. Where the gain or loss has been realised (through selling the security), this is reported as Gain (Loss) Realised from Price Changes.

Foreign Currency Term Liabilities

Foreign currency term liabilities are reported at market or fair value. The funds from these liabilities are invested in foreign currency marketable securities. This valuation policy ensures consistency with the policy adopted for the corresponding assets. Market or fair value is imputed by deriving the fair value rate from the relevant market yield curve of similar liabilities and discounting the future cash flows of the liabilities at this rate. Changes in the value of these liabilities are recognised as an increase or decrease in the value of the Term Liabilities in the Statement of Financial Position.

Gains and losses arising from changes in market value of foreign currency term liabilities are recognised immediately as expenses in the Statement of Financial Performance. Where the liability is still owed, the gain or loss is reported as (Gain) Loss from Unrealised Price Revaluation. Where the gain or loss has been realised (through repayment of the liability), this is reported as (Gains) Losses Realised from Price Changes.

Repurchase and Reverse-Repurchase Transactions

Securities sold under agreements to repurchase continue to be recorded as Marketable Securities in the Statement of Financial Position. The obligation to repurchase (Securities Sold Under Agreements to Repurchase) is disclosed as a liability. The difference between the sale and repurchase price represents an expense and is amortised over the term of the contract and reported in the Statement of Financial Performance.

Securities held under reverse-repurchase agreements are recorded as an asset in the Statement of Financial Position (Securities Purchased Under Agreements to Re-sell). The difference between the purchase price and sale price represents income and is amortised over the term of the contract and reported in the Statement of Financial Performance.

Both repurchase and reverse-repurchase transactions are reported at the transaction value inclusive of any accrued income or expense.

Securities Lending Programme

Securities lent out under the securities lending programme are accounted for on the same basis as repurchase and reverse-repurchase transactions.

Derivative Instruments

The Bank's involvement in derivative instruments comprises forward foreign exchange swap contracts, interest rate futures and interest rate swaps.

Forward foreign exchange swap contracts are revalued for changes in exchange rates. Premiums or discounts on inception are amortised over the life of the swap and are not revalued for changes in interest rates. Changes in value are reported in the Statement of Financial Performance as Liquidity Management Swap Income. The net value at balance date is reported in the Statement of Financial Position.

Interest rate futures are reported in the Statement of Financial Position at quoted market mid-prices. Changes in market value are recognised immediately in the Statement of Financial Performance as Other Foreign Currency Income (Loss). Margin and cash accounts arising from interest rate futures are recognised in the Statement of Financial Position as Other Cash Balances.

Interest rate swaps are reported at fair value in the Statement of Financial Position. The fair value is derived by discounting the future cash flows based on the relevant market yield curves. Changes in fair value are recognised immediately in the Statement of Financial Performance as Other Foreign Currency Income (Loss). Interest receivable and payable for interest rate swaps with the same counterparty is reported net where a legal right of set-off exists.

All derivative instruments in a gain position are reported within the balance of foreign currency Marketable Securities in the Statement of Financial Position. Derivative instruments in a loss position are reported in the Statement of Financial Position as Derivative Instruments in a Loss Position. Derivative instruments in a loss position are offset against derivative instruments in a gain position where a legal right of set-off exists.

Short Sales of Marketable Securities

A “short sale” is a sale of a security that the Bank does not own. Short sales arise as part of the foreign reserves management function (see note 1) and the net returns on short sales are reported as income generated through departures from neutral risk positions (see note 22). Securities that are sold short are recorded at quoted market prices and reported as Short Sales of Marketable Securities in the Statement of Financial Position. Any gains or losses are recognised immediately in the Statement of Financial Performance on the same basis as foreign currency Marketable Securities.

Unsettled Transactions

Unsettled transactions are security purchases or sales that have been agreed but are yet to be settled. Amounts payable for unsettled purchases of securities are reported as liabilities under the title Payable for Unsettled Purchases of Securities. Amounts due from unsettled sales of securities are reported as assets under the title Receivable from Unsettled Sales of Securities.

Unsettled transactions are reported at the contract amounts.

Investment Portfolio - NZ Government Securities

The Bank's investment portfolio is accounted for on a constant yield to maturity basis. This reflects the intention to hold the portfolio until maturity as these assets represent the investment of the proceeds from issuing currency and the Bank's equity. Any premium or discount on purchase is capitalised and amortised over the term of the security on a constant yield to maturity basis. The portfolio is recorded in the Statement of Financial Position at historic cost adjusted for amortisation of any premium or discount on purchase. Interest is accrued in the Statement of Financial Performance as Local Currency Interest Income.

Market Test Activities

From time to time, the Bank may hold small trading positions in local currency securities as part of market test activities. These are valued at quoted market prices. Changes in market value are recognised as an increase or decrease in the value of Other Local Currency Financial Assets. Gains or losses are recognised immediately in the Statement of Financial Performance as Gain (Loss) from Market Test Activities.

Other Financial Assets and Liabilities

Local and foreign currency cash, deposits and short-term advances are valued at transaction date value.

(g) Currency in Circulation

Currency issued by the Reserve Bank represents a claim on the Bank in favour of the holder. The liability for Currency in Circulation is recorded at face value in the Statement of Financial Position.

(h) Collectors' and Demonetised Currency

The Reserve Bank has a liability for the face value of collectors' currency. However, it is most unlikely that significant amounts of collectors' currency will be returned for redemption. Therefore, the face value of collectors' currency is recognised as a contingent liability.

The Bank has a liability for the face value of demonetised currency still in circulation. This is recognised as a contingent liability except for a portion retained in the Statement of Financial Position to cover expected future redemptions.

(i) Land and Buildings

Land is carried at market value. Property intended for sale is valued at the lower of book value or market value. Buildings are valued at depreciated market value except for the specialised basement and ground floor occupied by the Reserve Bank, which are valued at adjusted replacement cost. Surpluses of book value over historic cost for this class of asset are recorded in the Properties Revaluation Reserve. Where the book value of this class of asset falls below historic cost, previous revaluations are reversed and any remaining balance is charged as an expense in the financial year it occurs. Independent valuations of this class of asset are obtained triennially. Buildings are depreciated on a straight line basis over 40 years.

(j) Other Fixed Assets

Other Fixed Assets are carried at cost less depreciation. The following assets held by the Reserve Bank of New Zealand are depreciated on a straight line basis over the following terms:

Computer Hardware	4 years
Computer Software	5 years
Plant and Equipment	5 years
Building Improvements	8 years
Miscellaneous	expected useful life

Motor vehicles are depreciated on a diminishing value basis at a rate of 26 percent per annum.

(k) Operating Leases

Where the Bank is the lessee, the lease rentals payable on operating leases are recognised in the Statement of Financial Performance over the term of the lease on a basis consistent with the expected benefits derived from the leased assets.

Where the Bank is the lessor, the assets leased out are retained in the balance of Fixed Assets and depreciated on the same basis as Other Fixed Assets.

(l) Currency and Artwork Collections and Archives

Items held in the Reserve Bank's currency and artwork collections and archives that have a material commercial value are independently valued at estimated market values. Surpluses of book value over historic cost for this class of asset are recorded in the Currency and Artwork Collections Revaluation Reserve. Nominal values have been placed on items with no material commercial value. Collections are not depreciated. Additions are held at cost until subsequent revaluations.

(m) Inventories

Inventories are carried at the lower of cost or realisable value. Cost is determined on a weighted average basis. Unissued currency stocks are recorded as inventory at the cost of acquisition and expensed when issued.

(n) Accounts Receivable

Accounts receivable are carried at expected realisable value after making due allowance for doubtful debts.

(o) Provision for Transfer of Surplus

The Bank's notional surplus income, as calculated under section 158 of the Reserve Bank of New Zealand Act 1989, is recorded in the Statement of Financial Performance as Provision for Transfer of Surplus. Under section 162 of the Act, the Treasurer directs whether the notional surplus income is paid to the Crown or credited to the Bank's reserves (after having regard to the Bank's capital requirements and the views of the Board of Directors). As the full notional surplus is required to be paid to the Crown unless otherwise directed by the Treasurer, the full notional surplus is shown as a liability at balance date.

(p) Provision for Restructuring

A provision for restructuring is recognised only when the Bank has a detailed restructuring plan and the plan has either started to be implemented or has been communicated to those affected by it. Only those expenses that are necessarily entailed by the restructuring and are not associated with ongoing activities are included in the provision.

(q) Retirement Gratuity

Retirement gratuity liabilities are recorded at actuarial value. This is calculated using a discounted cash flow model based on the relevant market yield curves. Changes in value are recognised in the Statement of Financial Performance as Personnel Expenses. Retirement gratuity liabilities are reported in the Statement of Financial Position as Accrued Employee Entitlements.

(r) Personnel Expenses

Personnel Expenses include the full cost of all staff benefits, including any applicable Fringe Benefit Tax. Salaries and leave accrued at year-end are reported in the Statement of Financial Position as Accrued Employee Entitlements.

(s) Income Tax

Section CB3 of the Income Tax Act 1994 exempts the Reserve Bank from income tax.

The Bank's subsidiary company, RBNZ Registry Limited, is liable for income tax. Taxation charged against profit includes both current and deferred taxation calculated using the comprehensive basis under the liability method. Deferred taxation arises from items of income and expenditure being included in taxation computations in periods different from those in which they were recorded in the Statement of Financial Performance.

(t) Custodial Activities

Securities held by the Reserve Bank under custodial arrangements are not included in these financial statements (see note 38).

(u) Segmental Reporting

The Bank presents financial assets and financial liabilities, and their associated income and expense streams, by distinguishing between foreign currency and local currency activities. In addition, the Bank provides operating results by function. The Bank considers that these reporting approaches provide appropriate segmental reporting of the Bank's activities.

(v) Income Allocated Between Functions

Each function receives income and incurs expenses relating directly to the assets and liabilities used exclusively by that function. These income and expenses are presented in the Statement of Cost of Services. Notional balance sheets are calculated for each of the Bank's functions as though each function operated autonomously. Income and expense flows are also attached to the notional funding for each function. This structure enables each function to more accurately report the financial outcome of the services provided.

The income earned from the assets funded by the Bank's net equity is allocated equally to the Foreign Reserves Management and Market Operations functions.

(w) Cash Flows

Cash is defined as those items that are convertible to cash within two working days and are used in the day-to-day cash management of the Bank.

Investing activities include the cash movements, including realised gains and losses, in the Reserve Bank's financial asset portfolios. Also included are cash flows arising from movements in fixed assets, and the repayment of loans to staff.

Financing activities include those cash flows arising from the issue of circulating currency, borrowing from the Treasury, and payment of the net operating surplus to the Crown.

Operating activities include income and expenditure cash flows not included in investing or financing activities.

(x) Comparative Amounts

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

(y) Changes in Accounting Policies

There have been two changes in the Reserve Bank's accounting policies for the year ended 30 June 2001.

The Bank commenced depreciating its buildings from 1 July 2000. This has decreased the reported value of buildings by \$27,000 and increased depreciation expense by \$513,000. If the Bank had not depreciated buildings, the Loss on Revaluation of Bank Properties would have been \$1,330,000. This change in accounting policy has not been given retrospective effect as the adjustment is not material.

The Bank now reports its retirement gratuity liabilities on an actuarial basis. Previously, the Bank accrued retirement gratuities when employees became entitled to the gratuity. This change in accounting policy increased the Accrued Employee Entitlements liability by \$1,022,000 and increased Personnel Expenses by the same amount.

Neither of these changes affects the Statement of Cash Flows.

There have been no other material changes to the Bank's accounting policies and uniform accounting policies have been applied throughout the Bank.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 30 June	Note	2001 \$000	2000 \$000
Assets:			
Foreign Currency Financial Assets			
Cash Balances with Other Central Banks		141,936	105,537
Other Cash Balances		5,993	3,037
Marketable Securities	2	4,186,807	4,313,238
Short-Term Advances		148,093	-
Receivable from Unsettled Sales of Securities		4,400	90,524
Securities Purchased Under Agreements to Re-sell		1,512,238	1,314,560
Accrued Interest		54,963	71,380
Total Foreign Currency Financial Assets*		6,054,430	5,898,276
Local Currency Financial Assets			
Cash on Hand		206	58
Securities Purchased Under Agreements to Re-sell		2,516,507	1,600,265
Investment Portfolio - NZ Government Securities		2,661,517	2,445,433
Accrued Interest		46,482	46,584
Other Local Currency Financial Assets	4	41	91
Total Local Currency Financial Assets		5,224,753	4,092,431
Total Financial Assets		11,279,183	9,990,707
Other Assets			
Accounts Receivable		1,539	1,822
Inventories	5	6,692	8,151
Deferred Taxation		-	214
Fixed Assets	6	37,694	41,172
Total Other Assets		45,925	51,359
Total Assets		11,325,108	10,042,066

* Foreign currency assets and liabilities do not match due to \$145.4 million of Short-Term Advances arising from foreign exchange swap contracts for monetary policy implementation. These Short-Term Advances are fully hedged through forward transactions.

As at 30 June	Note	2001 \$000	2000 \$000
Liabilities:			
Foreign Currency Financial Liabilities			
Payable for Unsettled Purchases of Securities		-	123,097
Short Sales of Marketable Securities		178,992	186,536
Derivative Instruments in a Loss Position	3	9,974	86,358
Securities Sold Under Agreements to Repurchase		962,676	911,618
Term Liabilities		4,668,965	4,496,971
Accrued Interest		87,241	94,647
Total Foreign Currency Financial Liabilities*		5,907,848	5,899,227
Local Currency Financial Liabilities			
Government Deposits		2,248,961	1,327,376
Other Deposits	7	129,051	77,693
Accrued Interest		796	245
Total Local Currency Financial Liabilities		2,378,808	1,405,314
Total Financial Liabilities		8,286,656	7,304,541
Other Liabilities			
Currency in Circulation		2,462,737	2,159,965
Provision for Transfer of Surplus	10	154,138	157,681
Miscellaneous Liabilities	8	16,182	19,779
Total Other Liabilities		2,633,057	2,337,425
Total Liabilities		10,919,713	9,641,966
Equity	11	405,395	400,100
Total Liabilities and Equity		11,325,108	10,042,066

The above statement is to be read in conjunction with the notes on pages 56 to 88.

CONSOLIDATED STATEMENT OF MOVEMENTS IN EQUITY

For the year ended 30 June	Note	2001 \$000	2000 \$000
Equity at Start of Year		400,100	404,890
Net Surplus for the Year		159,580	159,265
Movement in Properties Revaluation Reserve	11	(147)	(6,400)
Movement in Currency and Artwork Collections Revaluation Reserve	11	-	26
Total Recognised Revenues and Expenses for the Year		159,433	152,891
Provision for Transfer of Surplus to Government	10	(154,138)	(157,681)
Equity at End of Year		405,395	400,100

The above statement is to be read in conjunction with the notes on pages 56 to 88.

CONSOLIDATED STATEMENT OF COST OF SERVICES

For the year ended 30 June	Note	Operating	Operating	Operating	Operating	Operating
		Income	Expenses	Surplus	Surplus	Surplus
		Actual	Actual	(Deficit)	(Deficit)	(Deficit)
		2001	2001	2001	2001	2000
		\$000	\$000	\$000	\$000	\$000
Functions:						
Monetary Policy Formulation		10	7,431	(7,421)	(9,173)	(7,159)
Market Operations		14,612	3,194	11,418	11,237	11,851
Financial System Oversight		16	3,646	(3,630)	(3,715)	(3,067)
Currency Operations	21	176,215	12,881	163,334	143,029	147,300
Foreign Reserves Management	22	448	3,868	(3,420)	9,546	12,848
Banking Services		1,426	1,669	(243)	(388)	202
Overseas Investment Commission Secretariat		581	675	(94)	(14)	(63)
Registry and Depository Services	23	6,021	5,505	516	345	192
Other Outputs		3	883	(880)	(843)	(839)
Total		199,332	39,752	159,580	150,024	161,265
Less Intercompany Transactions ¹⁰		379	379	-	-	2,000
Total for Bank		198,953	39,373	159,580	150,024	159,265
Income Retained under Funding Agreement ¹¹			10,815			
Net Expenditure under Funding Agreement			28,558			

The Consolidated Statement of Cost of Services shows the total cost of providing each function, including internal transfers between functions.

The above statement is to be read in conjunction with the notes on pages 56 to 88.

10 Intercompany transactions are mainly for the purchase of registry services by other Bank functions. In 1999/2000, they include a \$2,000,000 dividend paid by RBNZ Registry Limited to the Bank.

11 The Funding Agreement commencing 1 July 2000 allows the Bank to retain revenue from specified revenue-generating activities and net this revenue against expenses for the calculation of Net Funding Agreement Levels.

CONSOLIDATED STATEMENT OF FINANCIAL PERFORMANCE

		Actual 2001 \$000	Budget 2001 \$000	Actual 2000 \$000
For the year ended 30 June	Note			
Operating Income:				
Income from Foreign Currency Financial Assets				
Interest Income	24	195,874		165,555
Gain (Loss) from Unrealised Price Revaluations		65,952		(12,464)
Gain (Loss) Realised from Price Changes		27,586		(3,463)
Other Foreign Currency Income (Loss)		(630)		(2,002)
Total Income from Foreign Currency Financial Assets		288,782		147,626
Expenses on Foreign Currency Financial Liabilities				
Interest Expense	25	210,431		176,230
(Gain) Loss from Unrealised Price Revaluations		71,310		(32,922)
(Gain) Loss Realised from Price Changes		21,726		485
Other Foreign Currency Expenses		817		644
Total Expenses on Foreign Currency Financial Liabilities		304,284		144,437
Net Foreign Exchange Revaluation Gain (Loss)	26	1,272		(439)
Foreign Currency Investment Income		(14,230)		2,750
Income from Local Currency Financial Assets				
Interest Income	24	276,847		248,605
Liquidity Management Swap Income		10,457		22,616
Gain from Market Test Activities		148		27
Total Income from Local Currency Financial Assets		287,452		271,248
Total Expenses on Local Currency Financial Liabilities	25	83,486		81,644
Local Currency Investment Income		203,966		189,604
Net Investment Income¹²		189,736	182,054	192,354
Other Income	27	9,217	8,215	11,398
Total Operating Income		198,953	190,269	203,752

12 The Bank does not forecast the main drivers of gross investment income and expenses for budget purposes (exchange rates and interest rates). Hence, the budget for investment income is presented on a net basis.

For the year ended 30 June	Note	Actual 2001 \$000	Budget 2001 \$000	Actual 2000 \$000
Operating Expenses:				
Personnel		16,734	17,342	20,146
Asset Management	28	6,078	5,916	6,289
New Currency Issued	21	4,689	5,511	9,341
Administration		1,319	1,206	1,600
Other	29	9,022	10,101	7,012
Total Operating Expenses		37,842	40,076	44,388
Loss on Revaluation of Bank Properties		817	-	-
Total Expenses		38,659	40,076	44,388
Operating Surplus		160,294	150,193	159,364
Taxation	37	714	169	99
Surplus Available for Appropriation	10	159,580	150,024	159,265

The above statement is to be read in conjunction with the notes on pages 56 to 88.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 30 June	Note	2001 \$000	2000 \$000
Cash Flows From Operating Activities:			
Source:			
Interest Received - Foreign Currency		286,060	238,674
- Local Currency - Investment Portfolio		181,101	171,861
- Other		91,851	78,385
Liquidity Management Swap Income		13,571	22,616
Fees, Commission and Other Income Received		10,590	8,636
		583,173	520,172
Disbursements:			
Interest Paid - Foreign Currency		283,467	181,397
- Local Currency		82,934	81,808
Payments to Suppliers and Employees		38,938	41,559
Net GST Paid (Received)		28	(103)
Income Tax Paid		358	390
		405,725	305,051
Net Cash Flow From Operating Activities	30	177,448	215,121
Cash Flows From Investing Activities:			
Source:			
Net (Increase) Decrease in Other Local Currency Financial Assets		50	1,173
Sale of Fixed Assets		19	203
		69	1,376
Disbursements:			
Net Increase (Decrease) in Foreign Currency Securities Purchased under Agreements to Re-sell		197,678	(545,686)
Net Increase (Decrease) in Foreign Currency Marketable Securities		9,165	324,318
Net Increase (Decrease) in Other Foreign Currency Financial Assets		61,961	49,089
Net (Increase) Decrease in Other Foreign Currency Financial Liabilities		47,888	889,712
Net Purchases of NZ Government Securities for Investment Portfolio		212,086	237,367
Purchase of Fixed Assets		980	1,174
		529,758	955,974
Net Cash Flow From Investing Activities		(529,689)	(954,598)

For the year ended 30 June	Note	2001 \$000	2000 \$000
Cash Flows From Financing Activities:			
Source:			
Issue of Circulating Currency		3,549,562	10,264,622
Withdrawal of Circulating Currency		3,246,790	9,989,473
Net Issue of Circulating Currency		302,772	275,149
Disbursements:			
Payment for Demonetised Currency		69	39
Net Repayment of Foreign Currency Term Liabilities		166,473	447,176
Payment of Surplus to Government		157,681	150,818
		324,223	598,033
Net Cash Flow From Financing Activities		(21,451)	(322,884)
CASH FLOW FROM ALL ACTIVITIES		(373,692)	(1,062,361)
Plus Exchange Rate Effect		108,422	592,441
NET CASH FLOW FROM ALL ACTIVITIES		(265,270)	(469,920)
Opening Cash Balance		3,264,662	3,734,582
CLOSING CASH BALANCE	31	2,999,392	3,264,662

The above statement is to be read in conjunction with the notes on pages 56 to 88.

Cash is defined in the Statement of Cash Flows as those items that are convertible to cash within two working days and are used in the day-to-day cash management of the Bank. This definition includes local currency securities purchased under agreements to re-sell and a substantial portion of the Bank's foreign reserves portfolio (see note 2).

Cash movements in some portfolios have been presented net as this is considered to provide a fairer presentation of the movements in the Bank's cash profile.

For further information on the management of the Bank's liquidity, see Note 20. Liquidity Risk.

NOTES TO BE READ AS PART OF THE CONSOLIDATED FINANCIAL STATEMENTS

1. Nature and Extent of Activities

The Reserve Bank's role as a central bank determines the nature and extent of its activities with respect to financial instruments. This role is defined by the Reserve Bank of New Zealand Act 1989.

(a) Foreign Currency Activities

Foreign currency activities result mainly from the Reserve Bank's holdings of foreign currency assets under its foreign reserves management function. The foreign reserves management portfolio comprises foreign currency assets held for foreign exchange intervention purposes ("foreign reserves"), pursuant to section 24 of the Reserve Bank of New Zealand Act 1989, and other foreign currency assets held for trading purposes. The level of foreign reserve intervention assets is determined by the Treasurer on advice from the Bank. The funding for foreign reserves is provided by foreign currency loans from the Treasury. These loans incur interest at market rates. Generally these loans are held to maturity, though from time-to-time the opportunity to repay early may be taken at the instigation of either the Bank or the Treasury, where this is expected to reduce the cost of funding. The funding for other foreign currency assets held for trading purposes usually arises through repurchase transactions with foreign securities trading firms.

The foreign currency assets are held in various currencies. The majority are denominated in United States dollars, Japanese yen and euros. The financial instruments held within these foreign currency portfolios consist mainly of sovereign securities, securities held under reverse-repurchase transactions or balances held with other central banks, commercial banks and settlement institutions. Liquidity and credit risk are key criteria in determining the type of instruments held.

The entire foreign reserves portfolio is actively managed. Subject to liquidity and credit risk constraints being satisfied, the Bank defines benchmark portfolios that represent a "neutral" asset and liability structure in terms of market risk. The neutral position is established to minimise the Bank's exposure to foreign currency risk and interest rate risk. In general, liquidity and credit risk constraints mean that the neutral structure will return a loss – the returns on assets will be less than the cost of funding those assets.

Departures of the actual asset and liability portfolio from the neutral asset and liability structure are undertaken where there is an expected increase in returns, within defined risk boundaries. Departures from the neutral structure also arise when the Bank trades in the foreign exchange markets on its own account and when marketable securities are short sold, again for expected return enhancement, within defined risk boundaries. Departures from the neutral structure involve discretionary trading and portfolio management decisions, and quantitative trading strategies, undertaken by specialist staff with delegated authority from the Governor.

The Reserve Bank also holds, from time-to-time, foreign currency assets and liabilities that arise from domestic monetary policy implementation. Any foreign currency exposures related to monetary policy implementation are fully hedged through the use of forward foreign exchange swap contracts.

For further information on the risk management policies relating to financial instruments, see notes 14 to 20.

(b) Events during 2000/2001

- (i) A new risk management mandate for foreign reserves management ("the mandate") was agreed by the Governor and implemented from 30 September 2000. While the mandate is substantially a simplification of the previous risk management rules and procedures, there are some significant changes to risk management arising from the mandate.
 - 1) The mandate documents the Governor's strategic objectives with respect to the risks from foreign reserves operations. Wherever possible, these objectives are expressed in terms of tolerance for loss in extreme market stress circumstances ("tail events").
 - 2) Risks from foreign exchange trading and interest rate trading are managed under a single Value at Risk (VaR) limit for all market risks. Previously, foreign exchange and interest rate risk were managed under separate limits (see note 16).
 - 3) The mandate includes risk management policies and procedures with respect to the risks from foreign reserves operations – financial risks such as credit risk, market risk and liquidity risk, and non-financial risks such as operational risk, legal risk and reputational risk. The previous rules and procedures concentrated primarily on financial risks.
- (ii) In April and May 2001, the Bank sold Japanese sovereign long-term debt and bought short-term securities issued by AA rated entities incorporated in North America and Europe to the equivalent of approximately NZ \$800 million. Factors that were considered in the context of this restructuring included:

- 1) Japan's high and rising public sector debt as a proportion of Gross Domestic Product;
- 2) rating agencies' downgrade of Japan's sovereign long-term foreign currency rating from AAA; and
- 3) low credit risk on short-term securities issued by AA rated entities in North America and Europe.

The Bank's exposure to the Japanese government comprised 22 per cent of foreign reserves at 30 June 2001 (2000 40 per cent) and is expected to fall to 7 per cent by 30 June 2002. The Bank had no exposure to Japanese corporates or banks at 30 June 2001 (2000 nil).

As part of this restructuring, the Bank closed out the cross currency interest rate swap transacted in 1997 (by entering into an equal and opposite swap transaction) and entered into a fixed-to-floating interest rate swap.

(c) Derivative Instruments

The Bank's involvement in derivative instruments comprises forward foreign exchange swap contracts, interest rate futures and interest rate swaps. Forward foreign exchange swap contracts are used as a part of hedged foreign exchange transactions for both monetary policy implementation and foreign reserves management. Any unrealised foreign exchange gain (loss) on unsettled forward foreign exchange swap contracts is offset by the foreign exchange revaluation on the associated money market instruments. Interest rate futures and interest rate swaps are used to enhance expected returns on foreign currency assets and, from time to time, to hedge interest rate and foreign exchange risk.

(d) Securities Lending Programme

As part of its foreign reserves operations, the Reserve Bank participates in a securities lending programme managed by The Chase Manhattan Bank. Under the programme, The Chase Manhattan Bank lends out securities owned by the Bank in exchange for cash or alternative securities. The range of financial assets that can be acquired under the programme is constrained by guidelines compatible with those that apply to the Bank's own foreign currency asset portfolios.

The total market value of securities which have been made available to participate in this programme is limited to US \$700 million. As at 30 June 2001, the market value of securities lent out under the programme was US \$259.4 million (2000 US \$406.1 million).

(e) Local Currency Activities

Local currency activities arise as follows:

- (i) Liquidity management operations. Liquidity management largely involves the Reserve Bank offsetting the daily net flows to or from government by advancing funds to or withdrawing funds from the banking system. Most of this business is undertaken through daily open market operations and any residual banking system liquidity is advanced or withdrawn using the Official Cash Rate scheme (OCR). Under the OCR scheme, the Bank advances or withdraws cash at a margin to the OCR. The financial instruments used in these operations include local currency reverse-repurchase transactions and forward foreign exchange swap contracts. In September 2000, the Bank began to use securities from its investment portfolio of NZ government securities in repurchase transactions (to withdraw funds from the banking system) for liquidity management purposes.
- (ii) Holding an investment portfolio comprising New Zealand government bonds to support the liability for currency in circulation and representing the investment of the Reserve Bank's net equity. The Bank's policy is to hold these investments until maturity.

From time to time, the Bank may also hold small trading positions in Crown or registered bank securities as part of market test activities.

(f) Restrictions on Title to Assets

As part of the active management of its foreign currency operations, the Reserve Bank enters into security repurchase transactions. The securities sold by the Bank under repurchase agreements continue to be recorded as Marketable Securities in the Bank's Statement of Financial Position. At balance date, securities with a book value of \$962.7 million (2000 \$911.6 million) had been sold to counterparties under repurchase agreements. These transactions are also recognised as a liability for Securities Sold under Agreements to Repurchase in the Bank's Statement of Financial Position.

The Bank also purchases securities under reverse-repurchase agreements in both its foreign currency and local currency operations. These transactions are recognised as Securities Purchased under Agreements to Re-sell in the Bank's Statement of Financial Position.

ASSET NOTES

2. Foreign Currency Marketable Securities

	Note	2001 \$000	2000 \$000
Marketable Securities			
- Convertible to cash within two days (considered cash equivalent)		2,712,762	2,960,834
- Convertible to cash outside two days (not considered cash equivalent)		1,473,827	1,042,601
Derivative Instruments in a Gain Position	3	218	303
Securities Linked to Derivative Positions		-	309,500
Total Marketable Securities		4,186,807	4,313,238

3. Derivative Instruments

	Book Value 2001 \$000	Notional Principal 2001 \$000	Book Value 2000 \$000	Notional Principal 2000 \$000
Interest Rate Futures:				
Futures in a Gain Position	218	63,582	303	711,016
Net Futures Position	218	63,582	303	711,016
At 30 June 2001, the Bank had 280 open futures contracts (2000 334).				
Interest Rate Swaps:				
Swaps in a Loss Position	(6,860)	282,855	-	-
Net Interest Rate Swap Position	(6,860)	282,855	-	-
Forward Foreign Exchange Swaps:				
Swaps in a Loss Position	(3,114)	151,948	-	-
Net Forward Foreign Exchange Swap Position	(3,114)	151,948	-	-
Cross Currency Swap - Derivative Components	-	-	(86,358)	234,818
Total Derivatives in a Gain Position	218	63,582	303	711,016
Total Derivatives in a Loss Position	(9,974)	434,803	(86,358)	234,818
Total Derivative Instruments	(9,756)	498,385	(86,055)	945,834

4. Other Local Currency Financial Assets

	2001 \$000	2000 \$000
Advances to Staff	38	69
Term Loans	-	19
Other Financial Assets	3	3
Total Other Local Currency Financial Assets	41	91

5. Inventories

	2001 \$000	2000 \$000
Bank Notes for Circulation	4,687	6,487
Coin for Circulation	1,684	1,049
Collectors' Currency	321	615
Total Inventories	6,692	8,151

6. Fixed Assets

	2001 Historic Cost/ Valuation \$000	2001 Accumulated Depreciation \$000	2001 Book Value \$000	2000 Historic Cost/ Valuation \$000	2000 Accumulated Depreciation \$000	2000 Book Value \$000
Freehold Land	11,880	-	11,880	11,980	-	11,980
Buildings	19,185	27	19,158	20,535	-	20,535
Total Land and Buildings			31,038			32,515
Computer Hardware	2,580	1,580	1,000	3,030	1,918	1,112
Plant	314	97	217	5,503	5,202	301
Office Equipment	1,486	1,011	475	4,132	3,321	811
Software	3,237	2,207	1,030	4,521	2,809	1,712
Currency Processing Equipment	2,154	1,985	169	3,601	2,857	744
Motor Vehicles	41	31	10	74	57	17
Building Improvements	3,826	1,826	2,000	4,962	2,492	2,470
Tenancy Inducements	1,527	1,152	375	1,483	1,148	335
Leased Currency Equipment	-	-	-	1,420	1,065	355
Currency Collection	607	-	607	607	-	607
Artwork Collection	154	-	154	171	-	171
Work in Progress	619	-	619	22	-	22
			6,656			8,657
Total Fixed Assets			37,694			41,172

The book values for land and buildings are depreciated market values based on existing use with the exception of the Wellington specialised basement and ground floor occupied by the Bank, which are valued at adjusted replacement cost. The market value of the Bank's land and buildings to a purchaser not requiring the Bank's specialised facilities is assessed at \$29,565,000 (2000 \$30,765,000).

	Valuation Date	Registered Valuer
Auckland Property	June 2001	Jones Lang Lasalle Advisory Limited
Wellington Head Office	June 2001	Jones Lang Lasalle Advisory Limited
Wellington Carparks	June 1999	Darroch Limited

LIABILITY AND EQUITY NOTES

7. Other Deposits

	2001 \$000	2000 \$000
Settlement Bank Deposits	65,785	48,503
Central Bank Deposits	2,115	2,684
International Monetary Fund Deposits	9,506	26,297
Claims Due to Stock Holders	51,451	-
Other Deposits	194	209
Total Other Deposits	129,051	77,693

Claims Due to Stock Holders arose in the Bank's registry operations from the early receipt of funds payable to registered third party stock holders. These funds were paid to the registered stock holders on 2 July 2001.

8. Miscellaneous Liabilities

	Note	2001 \$000	2000 \$000
Accounts Payable		11,976	15,324
Accrued Employee Entitlements		2,638	1,661
Other Current Liabilities		291	336
Provision for Restructuring	9	130	1,245
Demonetised Currency		1,147	1,213
Total Miscellaneous Liabilities		16,182	19,779

Demonetised currency is recognised as a contingent liability (see note 36(c)) except for \$1,147,000 (2000 \$1,213,000), which has been retained to cover future expected redemptions.

Pre-decimal-currency coin was issued by the Treasury and is included in the Bank's contingent liabilities (see note 36(b)).

9. Provision for Restructuring

	2001 \$000	2000 \$000
Currency Operations	-	668
RBNZ Registry	130	577
Total Provision for Restructuring	130	1,245
Currency Operations		
Balance at Start	668	1,466
Less Expenses Incurred	(664)	(894)
Additions to Provision	-	96
Unused Balance Written Back	(4)	-
Balance at End	-	668

During 1998/1999, the Bank made a provision for restructuring of its currency operations. This restructuring included payments to currency staff who were made redundant, as the volume of bank note processing diminished. The restructuring included the closure of the Auckland branch in November 2000 and all restructuring was completed during the 2000/2001 year.

	2001 \$000	2000 \$000
RBNZ Registry		
Balance at Start	577	-
Additions to Provision	31	746
Less Expenses Incurred	(170)	(169)
Balance Reversed	(308)	-
Balance at End	130	577

During 1999/2000, the Bank provided for restructuring RBNZ Registry Limited. This included provision for payments to staff who would be made redundant as a result of the out-sourcing of registry processing activities and the relinquishment of the Austraclear New Zealand System. The relinquishment of the Austraclear New Zealand System did not proceed and the related provision has been reversed. Payments relating to out-sourcing of registry processing activities are expected to be completed early in the 2001/2002 financial year.

10. Transfers to Retained Earnings and Provision for Transfer of Surplus

Under section 162 of the Reserve Bank of New Zealand Act 1989, the Bank's surplus, after any transfers to or from Equity, is paid to the government.

Transfers to or from the Reserve Bank's equity reflect the difference between actual net expenditure and the level of net expenditure specified under the Funding Agreement with government. Under-spending by the Bank in relation to the Funding Agreement results in a transfer to Equity. Over-spending by the Bank results in a transfer from Equity. In the current year, under-expenditure by the Bank of \$5,442,000 has consequently been transferred to the Bank's Equity. In the 1999/2000 year, under-expenditure by the Bank of \$1,584,000 was transferred to the Bank's Equity.

The Treasurer may authorise additional transfers to Equity. In the year under review, no additional transfers were made and the Bank's consolidated surplus, net of the transfers noted above, has been recorded in the Provision for Transfer of Surplus.

	2001 \$000	2000 \$000
Total Expenses	39,373	38,808
Income Retained under Funding Agreement	10,815	-
Net Expenditure under Funding Agreement	28,558	38,808
Funding Level specified in Funding Agreement	34,000	40,200
Funding Agreement Under-Expenditure	5,442	1,392
Surplus Available for Appropriation	159,580	159,265
Less Transfers to Equity:		
Funding Agreement Under-Expenditure	5,442	1,392
RBNZ Registry Limited Surplus	-	192
Total Transfers to Equity	5,442	1,584
Provision for Transfer of Surplus	154,138	157,681

The method for calculating expenditure under the Funding Agreement has changed. Previously, the Reserve Bank retained a given sum of money to pay for its operating expenses. Now the Bank retains a smaller sum of money plus the income from some specified revenue-generating activities (including RBNZ Registry Limited).

11. Equity

	2001 \$000	2000 \$000
Retained Earnings		
Opening Balance	399,247	397,663
Add Transfers to Retained Earnings:		
Reserve Bank of New Zealand	5,442	1,392
RBNZ Registry Limited	-	192
Transfer from Currency and Artwork Collections Revaluation Reserve	10	-
Closing Balance	404,699	399,247
Properties Revaluation Reserve		
Opening Balance	147	6,547
Increase (Decrease) in Value of Bank Properties	(147)	(6,400)
Closing Balance	-	147
Currency and Artwork Collections Revaluation Reserve		
Opening Balance	706	680
Disposal of Artwork	(10)	-
Increase (Decrease) in Value of Currency and Artwork Collections	-	26
Closing Balance	696	706
Total Equity	405,395	400,100

12. Fair Value of Financial Instruments

The fair value of a financial instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arms-length transaction.

When a financial instrument is traded in an organised and liquid market, that is able to absorb a significant transaction without moving the price against the trader, quoted market values represent fair value.

Derivative Instruments

Where quoted market prices for derivative instruments are unavailable, the fair value is calculated using discounted cash flow models based on current interest rates for the type and maturity of the underlying instrument. The fair value of all derivative instruments is presented in Note 3. Derivative Instruments.

Financial Assets and Liabilities

All other financial assets and liabilities are valued at either quoted market prices or prices derived from market yield curves, as described in the Bank's accounting policies, except as detailed below.

Repurchase and Reverse-Repurchase Agreements

The reported value of repurchase and reverse-repurchase agreements is considered to approximate their fair value due to the short term nature of the agreements.

Unsettled Transactions

The reported value of unsettled sales and purchases is considered to approximate their fair value due to the very short term until settlement occurs.

Short-Term Advances

The reported value of Short-Term Advances is considered to approximate their fair value due to the short term until maturity.

Investment Portfolio - NZ Government Securities

The fair value of the Bank's Investment Portfolio - NZ Government Securities is \$2,707,561,000 (2000 \$2,508,276,000). This has been calculated by discounting the current holdings at 30 June 2001 market rates.

Deposits

The carrying values of deposits are considered to approximate their fair value as they are payable on demand.

Currency in Circulation

The fair value of Currency in Circulation is considered to be its face value as reported in the accounts.

Provision for Transfer of Surplus

The carrying value of the provision is considered to approximate its fair value due to the short period between balance date and expected payment date.

13. Concentrations of Funding

The Bank's significant end-of-year concentrations of funding were as follows.

As at 30 June 2001	2001 Total \$000	New Zealand Government \$000	New Zealand Public \$000	Overseas Securities Trading Firms \$000	Other \$000
Foreign Currency Financial Liabilities					
Payable for Unsettled Purchases of Securities	-	-	-	-	-
Short Sales of Marketable Securities	178,992	-	-	-	178,992
Derivative Instruments in a Loss Position	9,974	6,860	-	-	3,114
Securities Sold Under Agreements to Repurchase	962,676	-	-	962,676	-
Term Liabilities	4,668,965	4,668,965	-	-	-
Accrued Interest	87,241	87,241	-	-	-
Total Foreign Currency Financial Liabilities	5,907,848	4,763,066	-	962,676	182,106
Local Currency Financial Liabilities					
Government Deposits	2,248,961	2,248,961	-	-	-
Other Deposits	129,051	-	-	-	129,051
Accrued Interest	796	753	-	-	43
Total Local Currency Financial Liabilities	2,378,808	2,249,714	-	-	129,094
Total Financial Liabilities	8,286,656	7,012,780	-	962,676	311,200
Other Liabilities					
Currency in Circulation	2,462,737	-	2,462,737	-	-
Provision for Transfer of Surplus	154,138	154,138	-	-	-
Miscellaneous Liabilities	16,182	-	1,147	-	15,035
Total Other Liabilities	2,633,057	154,138	2,463,884	-	15,035
Total Liabilities	10,919,713	7,166,918	2,463,884	962,676	326,235

Comparative figures as at 30 June 2000 were as follows.

As at 30 June 2000	2000 Total \$000	New Zealand Government \$000	New Zealand Public \$000	Overseas Securities Trading Firms \$000	Other \$000
Foreign Currency Financial Liabilities					
Payable for Unsettled Purchases of Securities	123,097	-	-	123,097	-
Short Sales of Marketable Securities	186,536	-	-	-	186,536
Derivative Instruments in a Loss Position	86,358	86,358	-	-	-
Securities Sold Under Agreements to Repurchase	911,618	-	-	911,618	-
Term Liabilities	4,496,971	4,496,971	-	-	-
Accrued Interest	94,647	94,647	-	-	-
Total Foreign Currency Financial Liabilities	5,899,227	4,677,976	-	1,034,715	186,536
Local Currency Financial Liabilities					
Government Deposits	1,327,376	1,327,376	-	-	-
Other Deposits	77,693	-	-	-	77,693
Accrued Interest	245	237	-	-	8
Total Local Currency Financial Liabilities	1,405,314	1,327,613	-	-	77,701
Total Financial Liabilities	7,304,541	6,005,589	-	1,034,715	264,237
Other Liabilities					
Currency in Circulation	2,159,965	-	2,159,965	-	-
Provision for Transfer of Surplus	157,681	157,681	-	-	-
Miscellaneous Liabilities	19,779	-	1,213	-	18,566
Total Other Liabilities	2,337,425	157,681	2,161,178	-	18,566
Total Liabilities	9,641,966	6,163,270	2,161,178	1,034,715	282,803

RISK MANAGEMENT NOTES

14. Risk Management

The Bank is involved in policy-orientated activities. Therefore, the Bank's risk management framework differs from the risk management frameworks for most other financial institutions. The main financial risks that the Bank is exposed to include credit risk on foreign currency reserves and interest rate risk on both foreign and local currency assets and liabilities. In the management of foreign reserves, minimising liquidity risk is the prime consideration in order to maintain an effective foreign exchange intervention capability. Policies for managing interest rate, credit, foreign currency and liquidity risk are outlined in notes 16 to 20. Like most other central banks, the nature of the Bank's operations creates exposure to a range of operational risks and reputational risks.

Bank management seeks to ensure that strong and effective risk-analysis, management and control systems are in place for assessing, monitoring and managing risk exposure. A Risk Management Committee, comprising the Governor, Deputy Governors and senior management, is responsible for advising on the monitoring and management of all risks that the Bank faces. A Reserves Oversight Committee comprising Deputy Governors and senior management reviews the foreign reserves business strategy and portfolio structure. This review includes the appropriateness of risk-return trade-offs underlying the business strategy and portfolio structure. Specialist staff conduct the Bank's local currency, foreign currency reserves management and foreign exchange dealing operations in accordance with a clearly defined risk management framework, including limits and delegated authorities, set by the Governor. The risk management framework is subject to regular review by the Risk Management Committee.

The majority of the Bank's financial risks arise from the foreign reserves and monetary policy operations of the Bank's Financial Markets Department. Within this department, a Risk Unit is responsible for maintaining the Bank's financial risk management framework. A separate department of the Bank (Financial Services Group) operates independent risk reporting systems that monitor and report compliance with various risk limits and policies.

The Risk Assessment and Assurance Department (which includes Internal Audit) reports to the Governors and the Audit Committee of the Board of Directors on internal audit and risk management issues. A risk-based framework, which evaluates key business risks and internal controls, is used to determine the extent and frequency of internal audits conducted. All Bank departments are subject to periodic internal audit review.

The Bank is subject to annual external audit, with the auditor being appointed by the Treasurer. Auditing arrangements are overseen by an Audit Committee including three of the Bank's independent directors, which meets regularly to monitor the external reporting and audit functions within the Bank. The Committee also reviews the internal audit function and has direct access to the external auditor.

The overall risk management framework is designed to strongly encourage the sound and prudent management of the Bank's risks. The Bank seeks to ensure the risk management framework is consistent with financial market best practice and it periodically engages external experts to assist in reviewing and modifying risk management practices and processes.

15. Operational Risk

Operational risk is the risk of loss (in both financial and non-financial terms) from the processes and procedures adopted by the Bank in fulfilling its responsibilities detailed in the Reserve Bank of New Zealand Act 1989.

Managing operational risk in the Bank is seen as an integral part of day-to-day operations and management, which includes explicit consideration of both the opportunities and the risks of each business activity. Operational risk management includes Bank-wide corporate policies which describe the standard of conduct required of staff, a number of mandated generic requirements (e.g. a project management template) and specific internal control systems designed around the particular characteristics of various Bank activities.

Compliance with the corporate policies, generic requirements and departmental internal control systems are managed by:

- an induction program for new employees, which makes them aware of the requirements;
- a quarterly management affirmation by each departmental head that the corporate policies and departmental internal control systems have been complied with; and
- an active internal audit function.

In addition, departmental managers are required to report to Deputy Governors any significant or material incident that has occurred that could adversely impact on the Bank. This is known as the Proactive Problem Management process. Its purpose is to notify Governors promptly of important unexpected issues and to provide them with an opportunity to give immediate advice.

The above policies and procedures for managing operational risk are reinforced by the requirements of section 165 of the Reserve Bank of New Zealand Act 1989, which requires the financial statements of the Bank to include a statement signed by the Governor and Deputy Chief Executive accepting responsibility for, among other things, the establishment and maintenance of a system of effective internal control within the Bank.

16. Market Risk

In September 2000, the Bank began to manage interest rate risk and foreign currency risk in an integrated manner under market risk management arrangements. Previously, foreign exchange and interest rate risk were managed under separate limits. Market risk is managed as follows:

- (a) Trading positions adopted by specialist staff are controlled by Value at Risk (VaR) limits. VaR measures the potential daily loss from most movements in market interest rates and foreign currencies. On 99 out of 100 days, actual daily losses are expected to be less than VaR.

VaR	Foreign	Interest	Correlation ¹³	2001
	Currency Risk	Rate Risk		Total
	\$000	\$000	\$000	Market Risk ¹⁴
Limit				2,000
As at 30 June	63	371	(88)	346
Peak over period	750	566	(288)	794
Average over period	92	258	(132)	218

During 2000/2001, actual daily losses were within (predicted) VaR 99% of the time.

- (b) Stop-loss limits are set to control losses that may arise from market risk. A stop-loss limit of \$9 million in any rolling 20-day trading period is applied to the aggregate interest rate and foreign currency losses from trading positions. When aggregate market risk losses exceed the stop-loss limit, positions are required to be closed down. The Governor must approve the re-establishment of positions.

¹³ Correlation is the reduction in overall risk due to risks in one portfolio offsetting risks in another portfolio.

¹⁴ The market risk VaR model was adopted by the Bank in September 2000 and so previous year comparative information is not available.

17. Credit Risk

Credit risk is the risk of loss arising from a counterparty to a financial contract failing to discharge its obligations.

(a) Credit Risk Management

Credit risk in the foreign currency portfolios is monitored and managed daily. End-of-day exposures are controlled through comprehensive individual counterparty and issuer credit limits. Exposure concentrations to an industry or geographical location are controlled by aggregate credit limits. Exposures against these limits are measured in credit-equivalent terms depending on the nature of the exposure. Individual credit limits are set on the basis of the rating of the counterparty or issuer. Aggregate credit limits are set on the basis of country ratings and views on the likelihood of a default of one entity affecting the credit-worthiness of other entities. Limits are updated as necessary when new market information emerges, with all limits formally reviewed on an annual basis.

Credit risk in the local currency portfolios is also monitored and managed daily. Intra-day and inter-day exposures are controlled through comprehensive individual counterparty and issuer limits. Exposures to the New Zealand government are not included in this credit framework. Most exposures arise under intra-day reverse-repurchase agreements entered into with settlement account holders under the real time gross settlement system. Securities that the Bank accepts under intra-day reverse-repurchase agreements include New Zealand government bonds, Treasury bills, and short-term paper issued by registered banks, local authorities and highly rated corporates. The securities are held in the Bank's name for the duration of the exposure and there is no charge for this intra-day liquidity. The exposures to the counterparty from whom securities are purchased under reverse-repurchase agreements are monitored but are not subject to formal limits. The Bank only accepts New Zealand government paper in its inter-day liquidity management operations.

The maximum loss that the Bank would suffer as a result of a security issuer defaulting is the value reported in the accounts. The Bank's maximum credit risk exposure in relation to derivatives is the cost of re-establishing the derivative contracts in the market in the event of the failure of the counterparty to fulfil its obligations. This cost is the fair value of the derivatives as reported in Note 3. Derivative Instruments.

(b) Concentrations of Credit Exposure

The Bank's significant end-of-year concentrations of credit exposure by industry type were as follows.

	2001 \$000	2000 000
New Zealand Government	5,224,712	4,092,281
Other Sovereign Issuers (excluding New Zealand Government)	3,896,854	4,887,780
Supranational Financial Institutions	508,808	112,483
Foreign Banks	1,647,868	898,036
Other	941	127
Total Financial Assets	11,279,183	9,990,707

Credit exposures arising from securities purchased under agreements to re-sell (reverse-repurchase agreements) are classified according to the issuer of the security for credit exposure concentration purposes. This is consistent with the Bank's view of the substance of the credit exposure and internal risk management. An alternative approach would be to classify credit exposures arising from securities purchased under agreements to re-sell according to the counterparty to the transaction. Using this approach would result in credit exposures of \$1.51 billion (2000 \$1.35 billion) being reported against securities trading firms and \$2.5 billion (2000 \$1.6 billion) reported against New Zealand banks instead of against Other Sovereign Issuers and the New Zealand Government respectively.

The Bank's significant end-of-year concentrations of credit exposure by geographical area (based on the entity's country of ownership) were as follows.

	2001 \$000	2000 \$000
New Zealand	5,224,820	4,092,409
USA	1,988,147	2,039,004
Japan	1,036,163	2,062,607
Europe	2,343,652	1,555,940
Supranational Financial Institutions	508,808	112,483
Other	177,593	128,264
Total Financial Assets	11,279,183	9,990,707

(c) Credit Exposure by Credit Rating

The following table presents the Bank's financial assets based on Standard and Poor's credit rating of the issuer. AAA is the highest quality rating possible and indicates the entity has an extremely strong capacity to pay interest and principal. AA is a high grade rating, indicating a very strong capacity, and A is an upper medium grade, indicating a strong capacity. BBB is the lowest investment grade rating, indicating a medium capacity to pay interest and principal. Ratings lower than AAA can be modified by + or - signs to indicate relative standing within the major categories. N/R indicates the entity has not been rated by Standard and Poor's.

	Credit Rating	2001 \$000	% of 2001 Financial Assets	2000 \$000	% of 2000 Financial Assets
Foreign Currency Financial Assets					
Cash Balances with Other Central Banks	AAA	115,009	1.0%	105,537	1.1%
	AA+	26,927	0.2%	-	-
Other Cash Balances	AA+	2,258	0%	-	-
	AA	2,912	0%	2,240	0%
	N/R	823	0%	797	0%
Marketable Securities	AAA	1,836,405	16.4%	3,625,820	36.3%
	AA+	1,192,385	10.6%	292,333	2.9%
	AA	676,688	6.0%	245,663	2.4%
	AA-	481,329	4.3%	149,422	1.5%
Short-Term Advances	AA+	148,093	1.3%	-	-
Receivable from Unsettled Sales of Securities	AAA	-	-	90,524	0.9%
	AA+	2	0%	-	-
	AA	4,398	0%	-	-
Securities Purchased Under Agreements to Re-sell	AAA	1,512,238	13.4%	1,314,560	13.2%
Accrued Interest	Various	54,963	0.5%	71,380	0.7%
		6,054,430	53.7%	5,898,276	59.0%

	Credit Rating	2001 \$000	% of 2001 Financial Assets	2000 \$000	% of 2000 Financial Assets
Local Currency Financial Assets					
Cash on Hand	N/A	206	0%	58	0%
Securities Purchased Under Agreements to Re-sell	AAA	2,516,507	22.3%	1,600,265	16.0%
Investment Portfolio - NZ Government Securities	AAA	2,661,517	23.6%	2,445,433	24.5%
Accrued Interest	AAA	46,482	0.4%	46,584	0.5%
Other Local Currency Financial Assets	N/R	41	0%	91	0%
		5,224,753	46.3%	4,092,431	41.0%
Total Financial Assets		11,279,183	100.0%	9,990,707	100.0%
Summary by Major Credit Category					
Foreign Currency Financial Assets					
	AAA	3,463,652	30.8%	5,136,441	51.5%
	AA+/-	2,534,992	22.4%	689,658	6.8%
	Various	54,963	0.5%	71,380	0.7%
	N/R	823	0%	797	0%
Total Foreign Currency Financial Assets		6,054,430	53.7%	5,898,276	59.0%
Local Currency Financial Assets					
	AAA	5,224,506	46.3%	4,092,282	41.0%
	N/R	41	0%	91	0%
	N/A	206	0%	58	0%
Total Local Currency Financial Assets		5,224,753	46.3%	4,092,431	41.0%
Total Financial Assets		11,279,183	100.0%	9,990,707	100.0%

(d) Credit Exposure by Counterparty

The table below shows the number of issuers where the Bank's credit exposures equalled or exceeded 10% of the Bank's equity¹⁵ for:

- End-of-year actual credit exposure.
- Peak end-of-day credit exposure (on the basis of limits).
- Peak local currency intra-day credit exposures (on the basis of limits). These exposures arise through intra-day reverse-repurchase agreements entered into with settlement account holders under the real time gross settlement system.

% of equity	End-of-year 2001	End-of-year 2000	Peak end-of-day 2001	Peak end-of-day 2000	Peak local currency intra-day 2001	Peak local currency intra-day 2000
10% to 19.9%	3	6	26	29	19	19
20% to 29.9%	1	5	1	1	1	1
30% to 39.9%	5	1	1	16	11	11
40% to 49.9%	2	-	20	2	-	-
50% to 59.9%	1	-	1	-	-	-
60% to 69.9%	-	-	-	20	-	-
80% to 89.9%	-	-	14	2	-	-
90% to 99.9%	-	-	5	14	-	-
100% to 109.9%	-	-	1	3	-	-
110% to 119.9%	-	-	3	3	-	-
120% to 129.9%	1	-	1	-	-	-
130% to 139.9%	-	-	2	2	-	-
190% to 199.9%	-	1	6	9	-	-
210% to 219.9%	1	-	-	-	-	-
240% to 249.9%	1	-	1	1	-	-
470% to 479.9%	1	-	-	-	-	-
490% to 499.9%	-	1	1	1	-	-
520% to 529.9%	-	1	-	-	-	-

Peak end-of-day exposures greater than 100% of the Bank's equity were to foreign banks and supranational financial institutions. The Bank does not constrain credit exposure to certain sovereign issuers (e.g. the United States of America). Exposures to these sovereign issuers are managed through other limits and controls (such as currency composition limits). End-of-year exposures greater than 100% were to highly-rated sovereign and supranational issuers.

15 Excludes exposures to the New Zealand government.

18. Interest Rate Risk

Interest rate risk is the risk of loss arising from changes in interest rates.

Foreign Currency Interest Rate Risk

Because the Bank's foreign currency assets are funded by foreign currency liabilities whose interest rate characteristics cannot be exactly replicated, even "neutral" asset portfolios involve some interest rate risk. The interest rate characteristics of the liabilities are similar to those of highly-rated bank and corporate instruments, but liquidity considerations require that a significant proportion of investments are in United States and German domestic government instruments, which have different interest rate characteristics to the liabilities. The Bank accepts the associated interest rate risk as inevitable, but seeks to closely limit additional (mainly duration-related) interest rate mismatches. The Bank is continually reviewing investment opportunities for ways to reduce the costs and risks associated with holding reserves, while maintaining liquidity of intervention assets. The investment in short-term AA securities in the restructuring of our foreign currency assets (refer to note 1(b)(ii)) is a case in point.

Interest rate risk arising from departures from the neutral position is managed by way of Value at Risk limits and stop-loss limits for the Bank's combined market risk as described in note 16.

Local Currency Interest Rate Risk

Interest rate risk on the Investment Portfolio - New Zealand Government Securities is not actively managed as a matter of policy. This decision recognises that:

- (a) active risk management could require the Bank to carry out transactions that may seem in conflict with the Bank's monetary policy stance; and
- (b) the investment portfolio held by the Bank is exactly matched by liabilities held by the Crown, so from a consolidated Crown position the interest rate risk is eliminated.

The Reserve Bank's exposure to interest rate risk that arises from liquidity management operations is minimal, due to the very short-term nature of the exposures created and because the exposures are offset by other interest-bearing assets and liabilities.

Assets and liabilities will mature or re-price within the following periods.

As at 30 June 2001	Weighted Average Interest Rate	2001 Total \$000	Non- Interest Sensitive \$000	6 Months or Less \$000	6 to 12 Months \$000	1 to 2 Years \$000	2 to 5 Years \$000	Over 5 Years \$000
Foreign Currency Financial Assets								
Cash Balances with Other Central Banks	3.05%	141,936	-	141,936	-	-	-	-
Other Cash Balances	2.34%	5,993	-	5,993	-	-	-	-
Marketable Securities	3.24%	4,186,807	-	1,619,161	403,572	609,731	1,250,437	303,906
Short-Term Advances	3.78%	148,093	-	148,093	-	-	-	-
Receivable from Unsettled Sales of Securities	0%	4,400	-	4,400	-	-	-	-
Securities Purchased Under Agreements to Re-sell	3.99%	1,512,238	-	1,512,238	-	-	-	-
Accrued Interest	0%	54,963	-	54,963	-	-	-	-
Total Foreign Currency Financial Assets	3.40%	6,054,430	-	3,486,784	403,572	609,731	1,250,437	303,906
Foreign Currency Financial Liabilities								
Payable for Unsettled Purchases of Securities	-	-	-	-	-	-	-	-
Short Sales of Marketable Securities	5.04%	178,992	-	-	-	-	116,021	62,971
Derivative Instruments in a Loss Position	3.75%	9,974	-	3,114	-	-	6,860	-
Securities Sold Under Agreements to Repurchase	3.46%	962,676	-	962,676	-	-	-	-
Term Liabilities	3.74%	4,668,965	-	1,969,246	502,753	410,781	1,051,346	734,839
Accrued Interest	0%	87,241	-	87,241	-	-	-	-
Total Foreign Currency Financial Liabilities	3.68%	5,907,848	-	3,022,277	502,753	410,781	1,174,227	797,810
Foreign Currency Interest Rate Sensitivity Gap		146,582	-	464,507	(99,181)	198,950	76,210	(493,904)
Local Currency Financial Assets								
Cash on Hand	0%	206	-	206	-	-	-	-
Securities Purchased Under Agreements to Re-sell	5.71%	2,516,507	-	2,516,507	-	-	-	-
Investment Portfolio - NZ Government Securities	7.06%	2,661,517	-	-	150,919	440,987	735,207	1,334,404
Accrued Interest	0%	46,482	-	46,482	-	-	-	-
Other Local Currency Financial Assets	6.33%	41	-	3	30	8	-	-
Other Assets	0%	45,925	45,925	-	-	-	-	-
Total Local Currency Assets	6.29%	5,270,678	45,925	2,563,198	150,949	440,995	735,207	1,334,404
Local Currency Financial Liabilities								
Government Deposits	5.75%	2,248,961	-	2,248,961	-	-	-	-
Other Deposits	5.01%	129,051	-	129,051	-	-	-	-
Accrued Interest	0%	796	-	796	-	-	-	-
Other Liabilities	0%	2,633,057	2,633,057	-	-	-	-	-
Equity	0%	405,395	405,395	-	-	-	-	-
Total Local Currency Liabilities and Equity	2.51%	5,417,260	3,038,452	2,378,808	-	-	-	-
Local Currency Interest Rate Sensitivity Gap		(146,582)	(2,992,527)	184,390	150,949	440,995	735,207	1,334,404
On-Balance Sheet Interest Rate Sensitivity Gap		-	(2,992,527)	648,897	51,768	639,945	811,417	840,500
Off-Balance Sheet Instruments		-	-	63,582	-	-	(30,265)	(33,317)
Total Interest Rate Sensitivity Gap		-	(2,992,527)	712,479	51,768	639,945	781,152	807,183
All Currencies								
New Zealand		(1,226)	(2,992,527)	329,746	150,949	440,995	735,207	1,334,404
United States		31,529	-	209,251	85,404	197,394	(9,194)	(451,326)
Euro		(21,374)	-	27,643	38,016	48,164	(59,302)	(75,895)
Japan		(4,845)	-	149,923	(222,601)	(46,608)	114,441	-
Other		(4,084)	-	(4,084)	-	-	-	-

Comparative figures as at 30 June 2000 were as follows.

As at 30 June 2000	Weighted Average Interest Rate	2000 Total \$000	Non- Interest Sensitive \$000	6 Months or Less \$000	6 to 12 Months \$000	1 to 2 Years \$000	2 to 5 Years \$000	Over 5 Years \$000
Foreign Currency Financial Assets								
Cash Balances with Other Central Banks	6.43%	105,537	-	105,537	-	-	-	-
Other Cash Balances	2.68%	3,037	-	3,037	-	-	-	-
Marketable Securities	3.91%	4,313,238	-	1,232,252	113,558	578,451	1,225,163	1,163,814
Short-Term Advances	-	-	-	-	-	-	-	-
Receivable from Unsettled Sales of Securities	0%	90,524	-	90,524	-	-	-	-
Securities Purchased Under Agreements to Re-sell	6.14%	1,314,560	-	1,314,560	-	-	-	-
Accrued Interest	0%	71,380	-	71,380	-	-	-	-
Total Foreign Currency Financial Assets	4.35%	5,898,276	-	2,817,290	113,558	578,451	1,225,163	1,163,814
Foreign Currency Financial Liabilities								
Payable for Unsettled Purchases of Securities	0%	123,097	-	123,097	-	-	-	-
Short Sales of Marketable Securities	4.62%	186,536	-	-	-	21,324	42,176	123,036
Derivative Instruments in a Loss Position	0%	86,358	-	86,358	-	-	-	-
Securities Sold Under Agreements to Repurchase	6.20%	911,618	-	911,618	-	-	-	-
Term Liabilities	4.40%	4,496,971	-	1,693,213	161,288	533,941	1,058,648	1,049,881
Accrued Interest	0%	94,647	-	94,647	-	-	-	-
Total Foreign Currency Financial Liabilities	4.52%	5,899,227	-	2,908,933	161,288	555,265	1,100,824	1,172,917
Foreign Currency Interest Rate Sensitivity Gap		(951)	-	(91,643)	(47,730)	23,186	124,339	(9,103)
Local Currency Financial Assets								
Cash on Hand	0%	58	-	58	-	-	-	-
Securities Purchased Under Agreements to Re-sell	6.41%	1,600,265	-	1,600,265	-	-	-	-
Investment Portfolio - NZ Government Securities	7.49%	2,445,433	-	-	501,274	152,186	585,593	1,206,380
Accrued Interest	0%	46,584	-	46,584	-	-	-	-
Other Local Currency Financial Assets	5.73%	91	-	30	38	15	8	-
Other Assets	0%	51,359	51,359	-	-	-	-	-
Total Local Currency Assets	6.90%	4,143,790	51,359	1,646,937	501,312	152,201	585,601	1,206,380
Local Currency Financial Liabilities								
Government Deposits	6.50%	1,327,376	-	1,327,376	-	-	-	-
Other Deposits	3.90%	77,693	-	77,693	-	-	-	-
Accrued Interest	0%	245	-	245	-	-	-	-
Other Liabilities	0%	2,337,425	2,337,425	-	-	-	-	-
Equity	0%	400,100	400,100	-	-	-	-	-
Total Local Currency Liabilities and Equity	2.16%	4,142,839	2,737,525	1,405,314	-	-	-	-
Local Currency Interest Rate Sensitivity Gap		951	(2,686,166)	241,623	501,312	152,201	585,601	1,206,380
On-Balance Sheet Interest Rate Sensitivity Gap		-	(2,686,166)	149,980	453,582	175,387	709,940	1,197,277
Off-Balance Sheet Instruments		-	-	(213,211)	215,582	12,807	19,210	(34,388)
Total Interest Rate Sensitivity Gap		-	(2,686,166)	(63,231)	669,164	188,194	729,150	1,162,889
All Currencies								
New Zealand		951	(2,686,166)	241,623	501,312	152,201	585,601	1,206,380
United States		(1,497)	-	(286,337)	215,549	24,108	282,612	(237,429)
Euro		611	-	(42,746)	(58,425)	111,496	27,111	(36,825)
Japan		(340)	-	23,954	10,728	(99,611)	(166,174)	230,763
Other		275	-	275	-	-	-	-

19. Foreign Currency Risk

Foreign currency risk is the risk of loss arising from changes in exchange rates. The assets held in foreign currency portfolios are largely matched by foreign currency liabilities of approximately equal value. The Bank's exposure to foreign currency risk arises from trading positions undertaken by specialist staff. Foreign currency risk is managed by way of Value at Risk (VaR) limits and stop-loss limits for the Bank's combined market risk as described in note 16.

Foreign currency assets and liabilities arising from domestic monetary policy implementation activity are fully hedged using forward foreign currency swaps.

As at 30 June, the Reserve Bank's net exposure to major currencies, including forward foreign exchange swap contracts and foreign currency swaps, was as follows.

	Currency of Denomination				Total All Currencies \$000
	United States Dollar \$000	Euro \$000	Japanese Yen \$000	Other Currencies \$000	
As at 30 June 2001					
Foreign Currency Financial Assets					
Cash Balances with Other Central Banks	102,216	8,029	26,926	4,765	141,936
Other Cash Balances	1,792	1,793	1,171	1,237	5,993
Marketable Securities	2,540,435	646,544	999,828	-	4,186,807
Short-Term Advances	148,093	-	-	-	148,093
Receivable from Unsettled Sales of Securities	15	5	4,380	-	4,400
Securities Purchased Under Agreements to Re-sell	1,120,743	391,495	-	-	1,512,238
Accrued Interest	30,126	15,958	8,879	-	54,963
Total Foreign Currency Financial Assets	3,943,420	1,063,824	1,041,184	6,002	6,054,430
Foreign Currency Financial Liabilities					
Payable for Unsettled Purchases of Securities	-	-	-	-	-
Short Sales of Marketable Securities	143,158	35,834	-	-	178,992
Derivative Instruments in a Loss Position	6,494	-	-	3,480	9,974
Securities Sold Under Agreements to Repurchase	925,433	37,243	-	-	962,676
Term Liabilities	2,659,855	982,407	1,026,703	-	4,668,965
Accrued Interest	38,201	29,714	19,326	-	87,241
Total Foreign Currency Financial Liabilities	3,773,141	1,085,198	1,046,029	3,480	5,907,848
Off-Balance Sheet Instruments	(138,750)	-	-	(6,606)	(145,356)
Net Currency Exposure	31,529	(21,374)	(4,845)	(4,084)	1,226

All net currency exposures were within approved limits at balance date.

	Currency of Denomination				Total All Currencies \$000
	United States Dollar \$000	Euro \$000	Japanese Yen \$000	Other Currencies \$000	
As at 30 June 2000					
Foreign Currency Financial Assets					
Cash Balances with Other Central Banks	102,965	2,223	74	275	105,537
Other Cash Balances	882	810	1,345	-	3,037
Marketable Securities	1,591,602	727,600	1,994,036	-	4,313,238
Short-Term Advances	-	-	-	-	-
Receivable from Unsettled Sales of Securities	-	49,667	40,857	-	90,524
Securities Purchased Under Agreements to Re-sell	1,118,840	154,828	40,892	-	1,314,560
Accrued Interest	28,902	29,351	13,127	-	71,380
Total Foreign Currency Financial Assets	2,843,191	964,479	2,090,331	275	5,898,276
Foreign Currency Financial Liabilities					
Payable for Unsettled Purchases of Securities	-	41,877	81,220	-	123,097
Short Sales of Marketable Securities	21,324	124,423	40,789	-	186,536
Derivative Instruments in a Loss Position	(223,142)	-	309,500	-	86,358
Securities Sold Under Agreements to Repurchase	866,936	-	44,682	-	911,618
Term Liabilities	2,132,318	772,063	1,592,590	-	4,496,971
Accrued Interest	47,252	25,505	21,890	-	94,647
Total Foreign Currency Financial Liabilities	2,844,688	963,868	2,090,671	-	5,899,227
Off-Balance Sheet Instruments	-	-	-	-	-
Net Currency Exposure	(1,497)	611	(340)	275	(951)

20. Liquidity Risk

Liquidity risk is the risk that an entity will encounter difficulty in raising funds at short notice to meet commitments associated with financial instruments. Liquidity risk is also the risk that an entity will have to sell a financial asset quickly at much less than its fair value.

Foreign Currency Activities

Liquidity is a key criterion in determining the composition of the Bank's foreign currency assets. This reflects the potential requirement to liquefy foreign reserves for intervention purposes should the need arise. Accordingly, there is an array of interacting controls aimed at ensuring quick access to funds. These controls include liquid asset ratios based on the liquidity characteristics of securities held and limits on the minimum and maximum proportion of reserves that may be held in any one currency. These limits are monitored daily.

The Bank has additional liquidity arrangements for foreign currency assets including:

- (a) Repurchase agreements with other central banks that provide for the Bank to sell securities in exchange for foreign currency, while simultaneously agreeing to repurchase those same securities at a specified later date for an agreed amount. In essence, the arrangement allows the Bank to enhance the liquidity of its foreign reserves portfolio with minimum additional risks.
- (b) Maintaining a standby credit facility (US \$100 million) to augment the amount of foreign currency that can be accessed quickly.

Local Currency Activities

The Bank is responsible for managing the daily liquidity of the banking system. This includes advancing funds to and withdrawing funds from the banking system in order to smooth out the daily peaks and troughs. The nature of these activities, which mostly involve offsetting the flow of funds from the Crown to settlement banks, is such that the Bank is not subject to the liquidity constraints that impact on other organisations.

CONSOLIDATED STATEMENT OF COST OF SERVICES NOTES

21. Currency Operations

Seigniorage is the income directly associated with the issue of currency and provides the Bank with its main source of income. Registered banks pay the Reserve Bank the face value of the currency issued to them. These funds are invested in New Zealand government securities, which are included in local currency financial assets, to back the currency in circulation liability. Currency in circulation is a non-interest bearing liability. However, the New Zealand government securities investment portfolio is interest bearing. The resulting interest income is seigniorage.

As part of the Currency Operations function, the Bank issues collectors' currency. The net loss for this activity in 2000/2001 was \$48,000 (2000 \$1,522,000 gain). The loss in 2000/2001 included inventory write-offs of \$309,000.

	2001 \$000	2000 \$000
Seigniorage	173,431	161,941
Other Income	2,784	4,557
Operating Income	176,215	166,498
New Note Issue Expenses	1,814	5,727
New Coin Issue Expenses	2,308	3,079
Collectors' Currency Issue Expenses	567	535
Currency Issue Expenses	4,689	9,341
Other Currency Expenses	8,192	9,857
Operating Expenses	12,881	19,198
Currency Operations Function Operating Surplus	163,334	147,300

22. Foreign Reserves Management

The Reserve Bank holds foreign currency assets to enable intervention in the foreign exchange market, should that ever prove necessary. These foreign reserves are fully funded by foreign currency borrowings through the Treasury. New Zealand pays more to borrow overseas than it can earn investing in high quality assets able to be realised quickly. As a result, holding reserves involves a small net cost, although some reduction in that cost is possible through active management of the holdings.

Subject to liquidity and credit risk constraints being satisfied, the Bank defines benchmark portfolios that represent a "neutral" asset and liability structure in terms of market risk. The neutral position is established to minimise the Bank's exposure to foreign currency risk and interest rate risk. Departures from the neutral position involve discretionary trading and portfolio management decisions, and quantitative trading strategies, undertaken by specialist staff with delegated authority from the Governor. The net income arising from departures from the neutral portfolio represents the active management of reserves.

	2001 \$000	2000 \$000
Gain (Loss) on Departures from Neutral Positions	6,287	(4,100)
Gain (Loss) on Neutral Asset/Liability Structure	(19,616)	7,400
Net Investment Income	(13,329)	3,300
Other	(872)	(597)
Foreign Exchange Difference on Translation	(29)	-
Foreign Reserves Management Gain (Loss)	(14,230)	2,703
Residual Income Allocation ¹⁶	14,678	13,844
Operating Income	448	16,547
Operating Expenses	3,868	3,699
Foreign Reserves Management Function Operating Surplus (Loss)	(3,420)	12,848

For further information on the Foreign Reserves Management Function, see Note 1. Nature and Extent of Activities, parts (a) to (d). Further information on risk management is contained in notes 14 to 20.

23. Registry and Depository Services

The Bank provides registrar and paying agency services to issuers of fixed interest securities. The Bank also operates the Austraclear New Zealand System, which provides the financial markets with clearing and settlement services for debt securities and equities.

In May 2000, the Bank outsourced the processing of registry services to BT Portfolio Services (NZ) Limited, though the Bank remains responsible for the services now carried out on its behalf. BT Portfolio Services (NZ) Limited have been operating on the Bank's computer system while their own system is modified to operate in the New Zealand environment.

	Note	2001 \$000	2000 \$000
Fees for Registry and Depository Services		5,449	5,784
Other Income		572	533
Operating Income		6,021	6,317
Personnel		886	2,554
Other Expenses		3,905	3,472
Operating Expenses		4,791	6,026
Registry and Depository Services Function Operating Surplus before Taxation		1,230	291
Taxation ¹⁷	37	714	99
Registry and Depository Services Function Operating Surplus after Taxation		516	192

¹⁶ Residual Income Allocation represents the income earned from the assets funded by the Bank's net equity, which is allocated equally to the Foreign Reserves Management and Market Operations functions.

¹⁷ Up to 30 June 2001, the Registry and Depository Services function was provided through a wholly-owned subsidiary company, RBNZ Registry Limited, which is liable for income tax as described in the Statement of Accounting Policies.

CONSOLIDATED STATEMENT OF FINANCIAL PERFORMANCE NOTES

24. Interest Income from Financial Assets

	2001 \$000	2000 \$000
Interest Income from Foreign Currency Financial Assets		
Cash Balances with Other Central Banks	6,116	23,060
Other Cash Balances	122	39
Marketable Securities	159,465	130,657
Securities Purchased Under Agreements to Re-sell	29,639	11,215
Securities Lending	532	584
Total Interest Income from Foreign Currency Financial Assets	195,874	165,555
Interest Income from Local Currency Financial Assets		
Securities Purchased Under Agreements to Re-sell	89,947	78,139
Investment Portfolio - NZ Government Securities	184,996	170,220
Government Bank Accounts	1,899	211
Advances to Staff	5	19
Term Loans	-	2
Other Securities	-	14
Total Interest Income from Local Currency Financial Assets	276,847	248,605
Total Interest Income from Financial Assets	472,721	414,160

25. Interest Expense on Financial Liabilities

	2001 \$000	2000 \$000
Interest Expense on Foreign Currency Financial Liabilities		
Securities Sold Under Agreements to Repurchase	10,839	3,560
Term Liabilities	199,592	172,670
Total Interest Expense on Foreign Currency Financial Liabilities	210,431	176,230
Interest Expense on Local Currency Financial Liabilities		
Government Deposits	75,698	76,862
Other Deposits	7,788	4,782
Total Interest Expense on Local Currency Financial Liabilities	83,486	81,644
Total Interest Expense on Financial Liabilities	293,917	257,874

26. Net Foreign Exchange Revaluation Gain (Loss)

	2001 \$000	2000 \$000
Foreign Exchange Revaluations:		
Gain (Loss) on Financial Assets	280,638	700,656
Gain (Loss) on Financial Liabilities	(279,366)	(701,095)
Net Foreign Exchange Revaluation Gain (Loss)	1,272	(439)

27. Other Income

	Actual 2001 \$000	Budget 2001 \$000	Actual 2000 \$000
Fees for Registry and Depository Services	5,070	3,667	5,371
Sales of Collectors' Currency	814	1,151	2,560
Rental Income from Properties	1,858	1,689	1,571
Registered Bank Fees	11	20	3
Currency Distribution Income	90	129	396
Overseas Investment Commission Fees	580	786	627
Miscellaneous	794	773	870
Total Other Income	9,217	8,215	11,398

28. Asset Management Expenses

	Actual 2001 \$000	Budget 2001 \$000	Actual 2000 \$000
Depreciation ¹⁸	3,474	3,225	3,563
(Gain) Loss on Disposal of Fixed Assets	573	306	411
Other Asset Management Expenses	2,031	2,385	2,315
Total Asset Management Expenses	6,078	5,916	6,289

29. Other Operating Expenses

	Actual 2001 \$000	Budget 2001 \$000	Actual 2000 \$000
Other Professional Fees	3,776	5,107	2,051
Computer Expenses	2,296	1,957	1,658
Information	1,136	1,138	1,076
Operational Travel	775	764	708
Rental and Lease Expenses	5	-	255
Printing	198	219	239
Agency and Commissions	317	386	411
Audit Fees	192	193	232
Non-Executive Directors' Remuneration	105	105	105
Donations	-	-	4
Miscellaneous	222	232	273
Total Other Operating Expenses	9,022	10,101	7,012

Other Operating Expenses include \$23,000 (2000 \$44,000) paid to the Bank's auditors for work undertaken outside their capacity as auditors of the Bank.

18 The Bank commenced depreciating its buildings from 1 July 2000, as detailed in the Statement of Accounting Policies.

OTHER NOTES

30. Reconciliation of Operating Cash Flows with Reported Operating Surplus

	2001 \$000	2000 \$000
Reported Operating Surplus	159,580	159,265
Add (Subtract) Non-Cash Items:		
Depreciation	3,474	3,563
Amortisation of Premium/Discount on Purchase of Securities	7,259	71,639
Net Unrealised Price Revaluations	5,358	(20,458)
Loss on Revaluation of Bank Properties	817	-
Write-off of Demonetised Coins	-	7
Net Unrealised Foreign Exchange (Gain) Loss ¹⁹	234,961	569,348
	251,869	624,099
Add (Subtract) Movements in Other Working Capital Items:		
Decrease in Accounts Receivable	283	358
Decrease in Miscellaneous Liabilities	(3,531)	(247)
Decrease in Inventories	1,459	(1,029)
Decrease in Interest Payable	(6,855)	(5,331)
Decrease in Interest Receivable	16,519	3,121
Decrease in Deferred Taxation	214	(154)
	8,089	(3,282)
Add (Subtract) Investing and Financing Activities:		
Net Realised Foreign Exchange (Gain) Loss	(236,233)	(568,909)
Net Realised Price Revaluations	(5,860)	3,948
Return of Demonetised Coin	3	-
	(242,090)	(564,961)
Net Cash Flow from Operating Activities	177,448	215,121

¹⁹ This represents the net unrealised effect of exchange rate movements on the Bank's foreign currency assets and liabilities. The net effect on the Bank's overall results, after allowing for realised exchange rate gains and losses, is a net gain of \$1,272,000 (2000 \$439,000 loss).

31. Consolidated Cash Balances

	2001 \$000	2000 \$000
Foreign Currency Assets:		
Cash Balances with Other Central Banks	141,936	105,537
Other Cash Balances	5,993	3,037
Marketable Securities - Liquifiable Within Two Working Days	2,712,762	2,960,834
Local Currency Assets:		
Cash on Hand	206	58
Securities Purchased Under Agreements to Re-sell	2,516,507	1,600,265
	5,377,404	4,669,731
Demand Liabilities:		
Government Deposits	2,248,961	1,327,376
Settlement Bank Deposits	65,785	48,503
Central Bank Deposits	2,115	2,684
International Monetary Fund Deposit	9,506	26,297
Claims Due to Stock Holders	51,451	-
Other Deposits	194	209
	2,378,012	1,405,069
Closing Cash Balances	2,999,392	3,264,662

32. Statement of Commitments

	2001 \$000	2000 \$000
Operating lease commitments		
Computer equipment		
• Due within one year	373	162
• Due within one to two years	278	162
• Due within two to five years	159	27
Total operating lease commitments	810	351
Capital expenditure commitments		
• Due within one year	821	-
Total capital commitments	821	-

33. Subsidiary Companies

The Bank has two wholly-owned New Zealand-incorporated subsidiaries, RBNZ Registry Limited and New Zealand Central Securities Depository Limited (NZCSD).

Up to 30 June 2001, RBNZ Registry Limited provided the Bank's Registry and Depository Services function under an agency agreement with the Bank. From 1 July 2001 these services are provided directly by the Bank. RBNZ Registry Limited ceased trading on 30 June 2001 and is being wound-up.

NZCSD is a non-trading company, incorporated solely for the purpose of acting as a custodian trustee. It holds assets on behalf of the participants in the Austraclear New Zealand System, as described in note 38.

34. Free Services

The Reserve Bank of New Zealand Act 1989 empowers the Bank to charge directly for some of its functions.

Some services are provided free of charge. These include services such as providing information to Ministers and Parliament, contributing to policy and briefing papers, providing information to the public, storing official documents securely, and providing information and library facilities to parties such as government departments and economic research organisations.

The Reserve Bank receives some free services from other organisations, generally involving the provision of information.

The Bank liaises closely with other central banks and international agencies. Information and staff training are exchanged free of charge with these institutions.

35. Related Parties

In the normal course of its operations, the Bank enters into transactions with related parties. Related parties include the Crown, as ultimate owner of the Reserve Bank, various government departments and Crown entities.

Transactions entered into include:

- (a) banking services;
- (b) agency transactions (at no charge);
- (c) foreign exchange transactions;
- (d) funding from the Treasury as part of the foreign reserves management operations; and
- (e) purchases of New Zealand government securities.

The Bank does not disclose the values of transactions and outstanding balances with Crown-related parties due to the large volume of transactions and the large number of related parties. Unless otherwise stated, all transactions take place with reference to market rates. Therefore, disclosure of the values of transactions and outstanding balances with Crown entities would not provide useful or material additional information.

36. Contingent Liabilities

- (a) In terms of a Trust Deed dated 16 May 1980, the Reserve Bank has a contingent liability to maintain the actuarial soundness of the Reserve Bank of New Zealand Staff Superannuation and Provident Fund, following each triennial review of the Fund.

On 2 February 1995, the Bank ceased making contributions to the defined benefit division of the Fund on the advice of the Fund's Actuary that such contributions were no longer necessary. The position is re-examined as part of each triennial review (last completed for the period ended 31 March 1999).

The Actuary performed a limited scope investigation on the financial position of the Fund based on the Fund's annual accounts as at 31 March 2001. The Actuary reported on 13 July 2001 that:

- (i) the assets of the Fund would have been sufficient at 31 March 2001 to meet the benefit obligations in respect of members, including existing pensioners, in the event of the Fund being wound up at that time;
 - (ii) the assets of the Fund would have been sufficient at 31 March 2001 to provide for benefits to members, including existing pensioners, that are attributable to membership prior to 1 April 2001; and
 - (iii) to his knowledge, there had been no circumstances between 31 March 2001 and 30 June 2001 that would cause him to form a different opinion as at 30 June 2001.
- (b) Coin issued by the Treasury prior to July 1989 is not recorded by the Reserve Bank within the total of currency in circulation. The Bank has accepted liability for all coin in the first instance, whether issued by the Treasury or the Bank. However, should coin returned to the Bank exceed that issued by the Reserve Bank, the liability for the excess would revert to the Treasury. The face value of coin issued by the Treasury is \$87,702,000.
 - (c) The Bank has a contingent liability for currency in circulation that has been demonetised but not returned to the Bank. The face value of demonetised currency is \$37,106,000. This includes coin issued by Treasury with a face value of \$12,950,000.
 - (d) The Bank has a liability for the face value of collectors' currency. However, it is most unlikely that significant amounts of collectors' currency will be returned for redemption at face value. The face value of all collectors' currency issued by the Bank to date is \$8,826,000 (2000 \$8,418,000).

Collectors' coin was issued by the Treasury prior to July 1989. Particular specimens of series issued both before and after 1989 are not generally distinguishable. The Bank has in practice accepted a contingent liability for all collectors' coin, but part of this liability could revert to the Treasury should large quantities of coin be returned.

(e) The Bank has indemnified the statutory managers of DFC New Zealand Limited against liability arising from the statutory management of DFC New Zealand Limited, which essentially ended on 15 October 1997. However, these indemnities continue and were given under sections 5 and 39 of the Reserve Bank of New Zealand Act 1989, on substantially the same terms as those provided by the Crown under Part V of the Reserve Bank of New Zealand Act 1989.

Previous Year's Contingent Liabilities

The above five contingent liabilities were recorded in the Reserve Bank's 2000 Annual Report. The only liabilities to arise during the year were:

- (i) demonetised currency with a face value of \$69,000 returned to the Bank for redemption at face value; and
- (ii) collectors' currency with a face value of \$600 returned to the Bank for redemption at face value.

37. Income Tax

Section CB3 of the Income Tax Act 1994 exempts the Reserve Bank from income tax. The Bank incurs and meets liabilities for goods and services tax, fringe benefit tax and other withholding tax.

The Bank's subsidiary company, RBNZ Registry Limited, is liable for income tax. The table below relates only to RBNZ Registry Limited.

For the year ended 30 June	2001 \$000	2000 \$000
Income Taxation Expense:		
Net Surplus Before Tax	1,230	291
Add Back Permanent Difference	933	9
	2,163	300
Income Tax Expense at 33%	714	99
Taxation Expense	714	99
Current Tax Charge:		
Tax Effect of Timing Differences	-	154
Current Tax Charge	714	253
Deferred Taxation:		
Opening Balance	214	60
Deferred Portion of Current Tax Charge	(123)	154
Non-Deductible Deferred Taxation	(91)	-
Deferred Taxation Asset (Liability)	-	214

RBNZ Registry Limited ceased trading on 30 June 2001 and is being wound up.

38. Custodial Activities

The Reserve Bank of New Zealand operates the Austraclear New Zealand System, which is a securities clearing and settlement system. It holds assets, on behalf of the participants, in the name of New Zealand Central Securities Depository Limited (NZCSD), which it has appointed as custodian trustee in terms of the Trustee Act 1956.

NZCSD is a wholly-owned subsidiary of the Reserve Bank of New Zealand, which, in terms of a Deed of Appointment between the Reserve Bank of New Zealand and NZCSD dated 19 May 1995, is incorporated solely for the purpose of acting as a custodian trustee. With the exception of the local currency securities owned by the Bank and held through NZCSD, the Reserve Bank has no beneficial interest in the securities that NZCSD holds, or any management obligations apart from safe-keeping.

The total of securities held by NZCSD at 30 June 2001 was \$78.8 billion (2000 \$79.2 billion).