RESERVE BANK OF NEW ZEALAND

Reserve Bank of New Zealand consultation on registered bank disclosure requirements

Summary of responses and policy outcomes

This paper summarises the submissions received by the RBNZ in response to its August 2010 Consultation Paper: **Review of Disclosure Requirements for Registered Banks** ("the CP"), and notes the Reserve Bank's policy response. We received 17 submissions in total.

Overall, we believe that these changes in the disclosure requirements will significantly reduce banks' compliance costs, while at the same time resulting in more manageable disclosure documents which are better aligned with the needs of their key readers.

The aim of this paper is to provide both a feedback statement, and to give banks as early an indication as possible of the nature of the new disclosure requirements; we know that banks are keen for them to be introduced as soon as possible, given the material reduction in compliance costs. We will be consulting on the details of the proposed requirement shortly, in the form of draft Orders in Council. The timetable is as follows:

By end-November at the latest	Issue draft new Orders in Council for consultation
Mid-January 2011	Deadline for comments on the consultation
Early February 2011	Final Orders in Council ready for regulation-making process
End-February 2011	New Orders in Council gazetted
30 March 2011 at the latest	New Orders come into force
31 March 2011	Balance date for first disclosure statements under the new Orders

We appreciate that this is a relatively tight timeframe, but it reflects the extensive consultation to date, and the desire to enable March 2011 disclosure by registered banks under the new requirements.

Following an overview section, the rest of this paper discusses the comments received and our proposed action in response. This follows the order of the list of questions we included in the

CP, followed by discussion of a few issues that we raised in the consultation which did not have a specific question associated with them. Section numbers refer to the sections of the CP.

Overview

The Reserve Bank appreciates the level of engagement with the review from the key stakeholders, both leading up to the publication of the consultation paper and in the detailed comments provided on it. It is particularly encouraging that there is broad consensus in favour of one of the two main options consulted on, namely Option B, and the Reserve Bank will now put this option into effect.

The main changes to the current regime will therefore be:

- The quarterly Key Information Summary and Supplemental Disclosure Statement will be dropped.
- There will be a single quarterly disclosure document aimed at more financially experienced readers.
- The financial statements that are included in the half-year disclosure statement will be based on interim rather than full-year accounting standards. This will cut this document by a factor of three or four, while still providing readers with the key updates on bank performance and risk that they need; and
- The required information will be streamlined and rationalised in a number of other ways across all periods.

While these main features are going ahead as proposed, the Reserve Bank has also changed some of the details of the proposals in response to concerns raised in the consultation feedback. These are covered in the rest of this paper.

We note that since the disclosure regime was introduced 15 years ago, changes to it have mainly involved increased information requirements, driven by the expansion of financial reporting standards, the introduction of the Basel Committee's capital adequacy disclosure requirements, and other piecemeal additions. This exercise has been the first major review of the disclosure framework, assessing what it delivers against its intended purpose. We plan to undertake regular and more frequent reviews of the regime in future.

We should however remind banks that, as flagged in the consultation paper, the Reserve Bank as the supervisor of registered banks will be considering whether any additional prudential reporting is required, in the light of the revisions to the disclosure regime. For example, there may be a few areas of data which we have concluded are not needed by the market, but which the prudential supervisors need to carry out their regular monitoring of registered banks.

Question 1: Options Considered but not preferred (section 3.5.1)

In the CP, we outlined three options that were considered but not preferred for various reasons. These three options were:

Option 1) maintaining the status quo;

Option 2) removing the RBNZ disclosure regime;

Option 3) separating publication of financial reporting and prudential disclosures.

Responses received overwhelmingly agreed that these three options should not be considered further.

Action: None.

Questions 2 – 5: Assessment of Option A and Option B (section 3.5.2)

Options A and B were the two options we put forward for consultation. The main difference between the two options is that Option A involves keeping the quarterly Key Information Summary (KIS) which would become the only disclosure in the off quarters, while Option B removes the KIS altogether and retains the off-quarter General Disclosure Statement (GDS).

Overall, submitters agreed that these were the only two realistic options. However, a couple of responses suggested that a third option could be that off-quarter reporting be removed altogether (although they would want to ensure that its removal would not lead to any changes in Securities Act requirements, such as the ending of banks' current exemption from the prospectus requirement). Most also noted that they preferred to keep off-quarter reporting, instead of becoming subject to some form of continuous disclosure requirements.

We note that a major review of the Securities Act is currently under way, and will not be completed in time to be reflected in at least the initial planned changes to our disclosure regime. There can be no certainty at this stage whether the removal of off-quarter disclosure would trigger other requirements under any revised Securities Act. If it turned out that some form of continuous disclosure regime could remove the need for off-quarter disclosure, significant further design work would be needed to establish the mechanisms and content of continuous disclosure, and to decide if continuous disclosure was an effective and efficient alternative means of achieving the Reserve Bank's financial stability objectives. Given the compliance cost savings that should be achievable by March 2011, we intend to leave further consideration of options for removing off-quarter disclosure until the future securities law framework is clearer.

Most respondents favoured Option B over Option A. There was general agreement that the KIS has not served the purpose for which it was intended, and that regular disclosure is only of interest to more expert readers, such as financial commentators who can provide the analysis that

general depositors are more likely to read. One comment noted however that some of the information on parent banks that overseas branches are required to disclose in their KIS is useful and is not in the general disclosure statement. We agree with this point.

A few of the responses noted that Option B entails three different formats for general disclosure statements (full-year, half-year and off-quarter), and it would save compliance costs for banks as well as be easier for users to have only two disclosure formats, full-year and interim. This is a valid point, and we discuss below how far the off-quarter and half-year disclosure can be brought into alignment (see "other separate proposals").

Action: Option B should be adopted (with some amendments to the detail, in the light of consultation on specific areas). Some parent bank information in the current branch KIS to be preserved in branch disclosure statements.

Question 6: Banks to provide more information on how compliance cost is reduced (section 3.6)

We received six responses that gave us some further indication of the reduction in costs. Most of the cost reduction comes from the reduced half-year disclosure, resulting in reduced preparation time, board time and reduced audit fees. Most also noted that if print copies are no longer required (i.e. banks merely print a copy off their website upon receiving a request), then there would be a fair amount of savings in printing costs as well (for instance a $60,000 annual cost saving noted by one of the big banks). Some submissions noted that our proposed additions to disclosure for the off quarters would offset some of the cost savings at the half year. (Other reactions to those proposed additions, and our response, are discussed further under "other separate proposals" below.)

While there was little quantified information, there was wide agreement that compliance costs will be reduced. A fuller assessment of the cost savings will be included in our upcoming Regulatory Impact Assessment (RIA), and in finalising this assessment, we will need additional information. We require much better information in this area and ask that banks turn their mind to how they will produce it.

Action: we will seek more quantitative information from banks on the impact on costs in light of the final proposals described here.

Question 7: Shortening the delivery time at the half year (section 3.7)

We suggested that given the proposal that half-year GDSs be prepared on an interim instead of the full-year basis, the deadline for the half-year production should be reduced accordingly, from three months currently to two months (which would align with the off-quarter deadline).

The majority of submitters agreed with shortening the deadline, noting that they would be able to meet that. One submitter suggested that some flexibility be built into the two month deadline,

such that if there are substantial accounting changes, the deadline be extended by another two weeks. However, the two overseas bank branches that responded said that they needed the full three months unless the audit review requirement is dropped.

Overall, timeliness seems a particularly important feature for disclosure statements, and it is also desirable for the purposes of cross-bank comparison that the deadline is the same for all banks. We also think that there should continue to be at least a review audit of the half-year disclosure statements published by all registered banks, including branches. We think the most workable solution to achieve these aims is to set the half-year deadline at two months as proposed, but with a provision that the Reserve Bank can grant an extension up to three months on reasonable grounds. We think this would have the desirable outcome that the major banks would publish their interim disclosure statements within two months of the balance date most of the time, while banks that cannot always manage this deadline currently would be encouraged to shorten any stages in their production process where there may be scope for doing so.

Action: deadline for half-year disclosure statements be shortened to two months, with banks able to request an extension to up to three months on reasonable grounds.

Question 8: Publication mechanism for GDSs (section 3.8)

We suggested in the CP that disclosure statements should be easily accessible on banks' websites, and that we saw no need for requiring hard copies to be available, as long as any request for a copy could be met in a reasonable time by one being printed off the website. We also recommended that banks should have to keep previous GDSs available on their websites – such a requirement becomes more important given that we also suggest that comparatives will no longer be required in the half-year and off-quarter GDSs (see Question 14).

Nine out of 10 submitters supported our approach. One bank was against there being a very specific requirement on where GDSs should be located on websites. However, we note that despite the current general requirement for the disclosure statement to be "readily accessible", it is often hard for even expert users to track down where they are located on a bank's website, so we do think that something precise is required. One respondent suggested that keeping two years of previous GDSs would be sufficient, another said three, and one said five.

One response noted that it is much easier for users to find what they are looking for in a GDS when there is an index. Banks always number the notes to the accounts, so we think it would not be imposing an unreasonable burden to require banks to include an index, to include at least each note to the accounts separately and also other main sections.

Action: Require GDSs to be easily accessible on banks' websites in a standardised way to be determined – such as having a link with a specified name from the home page. Banks will be required to make at least five years of GDSs available on their websites (or since registration if less than five years ago). Require an index.

Questions 9-11: Compliance with NZ IAS 34 in the off quarters (section 4.1.1)

As part of further reducing compliance costs during the off quarters, we suggested in the CP that banks' financial statements included in their disclosure statements should not have to comply with NZ IAS 34 *Interim Reporting,* since that standard requires some items that we view as inessential for meeting the market discipline objectives of the disclosure regime. However, almost all the feedback we received indicated that complying with NZ IAS 34 should be a minimum, and banks would prefer to do that even though it means they need to disclose some additional information. The rationale is that NZ IAS 34 provides a consistent framework that is internationally recognised.

We recognise the validity of the arguments in favour of NZ IAS 34 compliance, and accept the consensus on this point.

Action: Financial statements included in off-quarter GDSs must comply with NZ IAS 34.

Questions 12-13: Assessment of Appendix E of NZ IFRS 7 (section 4.1.2)

We received full support for Appendix E being removed in relation to banks (including from the Financial Reporting Standards Board (FRSB), who have issued an Exposure Draft proposing to make this change, in direct response to our Consultation Paper[1]). Most also thought that it should be removed altogether, although there was one suggestion that banks should be exempted from it, while non-bank deposit-takers should remain subject to it.

Two responses thought that the disclosure required by Appendix E should be removed entirely, but our view remains that a few requirements in Appendix E provide useful information, and accordingly they should be retained in the disclosure Orders in Council ("the OiCs") if Appendix E is dropped. In the majority of these few cases, the requirements already exist in similar form in the current OiCs, so removing them will cut duplicate requirements but leave the resulting disclosed information more coherent and remove overlaps.

Action: We have passed on to the FRSB the comments we received relating to Appendix E (all of which were non-confidential), for them to take account of alongside responses to their Exposure Draft. We have submitted the Reserve Bank's own response to the FRSB's consultation, supporting the proposed removal of Appendix E.

[1] ED 123 Proposed Amendments to NZ IFRS 7 *Financial Instruments: Disclosures*; Removal of Appendix E *New Zealand-specific additional disclosure requirements applicable to financial institutions*. The Consultation period closed on 11 November 2010.

Questions 14-15: Disclosure of comparative and parent information (section 4.1.3)

There was wide support for removing comparative information from the half-year and off-quarter disclosures (except for that required by NZ IAS 34).

There was also general agreement with only requiring information on the parent bank (ie, the solo registered parent bank as opposed to the consolidated banking group) at the full year.

Action: Comparative and parent disclosure will not be required for half year and off quarter.

Questions 16 – 17: Supplemental Disclosure Statement (SDS) (section 4.1.4)

Our proposal to no longer require publication of a separate SDS as part of a bank's quarterly disclosure was supported by all submitters. Four submitters also thought that the content of the SDS for locally-incorporated banks should be removed altogether, as opposed to our alternative proposal of the documents in question being available on written request within a reasonable time period. On balance we believe that the information on guarantee arrangements that banks are already required to disclose is enough that copies of underlying documents do not need to be made available, and the netting agreements and associated legal opinions are so long and technical that making them available serves no useful purpose.

The supplementary disclosure on risk management that banks can currently choose to relegate to the SDS will be required annually alongside other risk management disclosure (see under questions 30-32 below).

The SDS for overseas bank branches includes a copy of the most recent publicly available financial statements of the overseas bank and the overseas banking group. There was general acceptance that these documents are important documents for those interested in the position of the branch, and should therefore continue to be readily accessible in New Zealand.

Action: Banks will no longer be required to publish a separate SDS. Overseas bank branches will be required to make published parent bank and group financial statements readily accessible on their New Zealand website within a short time of their publication (to be specified in the draft new OiCs).

Questions 18 – 20: Branch disclosure (section 4.1.5)

We suggested that off-quarter disclosures could be discontinued for stand-alone branches (those with no associated locally-incorporated bank), subject to certain criteria. There was support for this from two of those branches, from one locally-incorporated bank, and from the Securities Commission (who felt that annual disclosure would suffice). Two of these responses suggested that the criterion for dropping off-quarter disclosures should be based on suitable parent bank information being readily available via the bank's New Zealand website. This was consistent

with the principle, which was generally agreed with, that for branches it is the performance of the whole overseas banking group that is the over-riding concern.

However, comments from a number of other banks, and other respondents, were that the requirements should be the same across all registered banks, and that there was no clear rationale for distinguishing between stand-alone branches and dual-registered branches (those where there is an associated locally-incorporated bank). On balance we have decided to drop this proposal.

Branch disclosure currently includes a table of risk-weighted assets (RWAs) calculated using the Basel I capital adequacy framework. There was broad agreement with the arguments given in the CP why RWA figures are not relevant for branches, and we see no prudential reason why this should be continue to be disclosed. We confirm also that we are removing the two other references to the superseded Basel I framework from our supervisory approach (namely, solo capital adequacy disclosure on a Basel I basis for IRB banks, and the capital adequacy "floor" of 90% of the Basel I requirement, also for IRB banks). (See under questions 36-37 below.) This strengthens the case for removing this last remaining area of dependence on Basel I.

There was general agreement with other changes we proposed for branches, as follows:

- full-year disclosure will cover both the business of the branch itself and the branch's New Zealand financial reporting group, disclosure at other periods will cover only the New Zealand financial reporting group;
- financial statements of insurance and non-financial business carried on in New Zealand outside the banking group will no longer be required as part of a branch's disclosure statement, but summary information on such business will still be required;
- parent group published accounts currently required in the SDS must be readily available on the branch's website (see under questions 16-17 above);
- certain publicly available summary information on the overseas banking group's profitability, total assets, capital adequacy and asset quality that is currently disclosed in the KIS will be included in the disclosure statement;
- a statement will be required alongside the analysis of large credit exposures, to the effect that the aggregate amount of any large exposure to an individual counterparty does not include any exposures to that counterparty that are booked outside New Zealand (from NZ IRFS 7 Appendix E).

Action: Scope of branch disclosure to remain as now except that figures for the solo branch business will no longer be required at the half year. Cut branch disclosure of Basel I RWAs. Other changes agreed as noted in the bullet points above.

Questions 21 - 22: Disclosure of mortgage lending (section 4.1.6)

There was general agreement with the CP's assessment of the problems in mortgage disclosure, leading to difficulties for users in understanding what various mortgage-related figures mean and how they compare across banks. There were a couple of comments about the desirability of pinning down a single precise definition of residential mortgage lending, and suggestions on the way this could be done. However, there were more comments to the effect that there are a number of different figures disclosed since they are required for different purposes. Adding a precise definition would possibly lead to yet another figure being required, leading to further confusion.

One comment was that further more detailed consultation may be needed to get a solution that is achievable by everyone. We agree with that, and will make further attempts beyond the timescale of this review to achieve more consistent disclosure of mortgage information that is helpful to market users.

In the meantime there was some support for our suggestion that it would be helpful for banks to provide a reconciliation of various mortgage lending related numbers in their disclosure statement. We think this could provide at least some clarity for users. The reconciliation could gather various figures from around the disclosure statement (at the balance date) and give a summary explanation of what each means and the reasons for the differences between them. This would for instance cover items described as residential mortgage lending, housing lending, retail mortgage lending, the difference between capital adequacy, balance sheet and exposure concentration numbers, and which figures include off-balance sheet commitments to lend.

Action: require banks to provide a reconciliation table half-yearly between various housing lending-related figures in their disclosure statement.

Questions 23 – 27: Mortgage LVR disclosure (section 4.1.6)

Again, there was general agreement with our assessment that there needs to be greater consistency across banks in the way they produce their breakdown of mortgage lending by loan-to-valuation ratio (LVR). The majority of comments agreed with our proposals regarding loans with missing LVR values, the inclusion of off-balance sheet exposures, and there were generally consistent views on whether the LVR disclosure should include any corporate lending secured on residential mortgages.

Most disagree, however, that the LVR information could be used to provide more transparency about the regulatory capital calculation for banks using internal modelling approaches, and there was also little support for the suggestion of having separate LVR information for corporate and other mortgage lending.

We believe that the LVR breakdown should continue to be based on banks' capital requirements for mortgage lending. For banks on the Basel II standardised approach, the definitions are clearly set out in BS2A *Capital Adequacy Framework (Standardised Approach)*. To achieve consistency, the following requirements should apply to banks on the Basel II IRB approach:

- mortgage loans with no LVR information should be included in the highest LVR bucket;
- off-balance sheet amounts (such as undrawn balances and pre-approved loans) should be included in the calculation at their credit equivalent amount as used to feed into the capital calculation;
- the valuation should be that at the origination of the loan;
- the loan value is at balance date and includes undrawn commitments;
- banks should include all loans which fall within their modelling approach for residential mortgage lending, which will typically include some lending to small businesses.

We believe that this approach serves the purpose of adding to the picture of a bank's risk exposure to the housing market. The disclosure requirements already make it clear that the disclosure should be based on figures used for the capital calculation, but we will consider whether more detailed requirements are needed.

At present, some but not all banks list the main assumptions on which their LVR disclosure is based. We think this is helpful for readers, and propose to make it a requirement.

Action: require banks to disclose the assumptions underlying the LVR disclosure, and to consider whether further detail on the requirements should be spelt out in the Orders in Council.

Questions 28 – 29: audit review requirements (section 4.1.7)

There was strong support from both banks and audit firms for maintaining the current audit requirements, although auditors all mentioned they would prefer the accounting disclosure to be separated from the other disclosure. While the auditors' preferred approach has some benefits, the concern is that this would result in information on closely-related subjects being disclosed in two different places, for instance because one is required by accounting standards and one is required by Basel II disclosure (one example is the breakdown of impaired loans into Basel II risk-weighting categories). On balance we consider there is more benefit in having similar information grouped together.

Two of the stand-alone bank branches noted that the requirement for a half-year audit review can add as much as a month to the process of publishing the half-year disclosure statement. One of them suggested that the half-year audit requirement should be dropped for stand-alone branches provided the ultimate parent bank publishes consolidated interim accounts complying with IAS 34. But as discussed under question 7 above, we think that it is an important principle that all

bank disclosure statements are subject to external review at least six-monthly, and we have suggested a way of encouraging a shorter production time for half-year disclosures without making the two month deadline a non-negotiable limit.

All three audit firms also expressed interest in the Reserve Bank implementing a rolling programme of audits of the capital adequacy information disclosed by banks. Some banks on the other hand expressed some concern at this.

Action: Audit requirements unchanged. Explore further with banks and auditors, outside the scope of the disclosure review, the suggestion of ad hoc audits of capital adequacy information: the primary focus of these would be on the banks accredited to use internal models.

Questions 30 – 32: Disclosure of accounting policies and risk management (sections 4.2.1-4.2.2)

All responses were in favour of removing the current requirements to disclose information on accounting policies that is additional to that required by IFRSs, both those in the OiCs and those in the New Zealand specific Appendix E to NZ IFRS 7. It was agreed that these largely duplicate what is already required by IFRSs and add very little value.

Out of ten submissions on the current required risk management disclosure, eight support keeping broadly the current layout for how the requirements are expressed, while two suggested that the disclosure be left to NZ IFRSs. In addition, there were three submissions in favour of removing the requirement to describe how the bank reviews its risk management systems, which is not required by Basel Pillar 3.

Action: Remove the requirements for additional disclosure of accounting policies from the OiCs. If Appendix E is cut, do not replace its current requirements on accounting policies in the OiCs. Keep the current OiC requirements for risk management disclosure.

Question 33: disclosure of credit exposure concentration to individual counterparties (section 4.2.3)

All but one response agreed with our suggested way of slimming down the credit exposure concentration disclosure so that it is more focused on the essential information; and none of these responses disagreed that the frequency of this disclosure should remain quarterly as at present. One bank suggested further changes to the layout, and in our view (with a slight adaptation) these represent a further improvement. Under this suggestion, the aggregate dollar amounts would be dropped, as it is the size of exposure in relation to the bank's equity that is key, but the size bands would be narrowed to 5% bands starting at 10% of equity. Two tables along the lines of the following example would be required, one for end-period exposures and one for intra-quarter peak exposures. Bank exposures rated A- or better will be excluded as proposed, along with sovereign exposures rated A- or better.

		Exposure as % of equity			
Asset Class	Credit rating	10-15%	15-20%	20-25%	25-30%
Banks	BBB- to BBB+	1	-	-	-
Corporates	A- to AAA	2	1	-	-
	BBB- to BBB+	-	-	-	-

Additional rows would be required for: (1) lower-rated; and (2) unrated exposures; but only if these are not nil returns.

Action: revise the disclosure for credit exposure concentration into a more slimmed down format, as set out in the CP and adapted above.

Questions 34 – 35: disclosure of credit risk impairment information (section 4.2.4)

The proposals in this area are designed to remove redundant information and provide in one place (as opposed to the OiCs and NZ IFRS 7 Appendix E) requirements for a coherent set of information. This required information adds some detail and also standardisation to the basic requirements in the body of NZ IFRS 7. There is also a breakdown of the information into Basel II credit risk categories, which is needed to comply with Basel II's Pillar 3disclosure requirements. There was general support for the changes, including the proposed six-monthly frequency of the full detail with brief updates in the off quarters.

The proposal to require specific time bands for the disclosure of overdue assets was the main area of additional disclosure, and this was generally supported for the advantages of improving comparability across the sector. However, a couple of responses noted that NZ IFRS 7 leaves the content of the analysis of overdue assets to management discretion. It was also noted that the less than 30 day time bucket is needed to reconcile to the total, and that our proposed time bands were slightly different from the industry standard.

In our view there are significant benefits of standardised disclosure of past due assets, and it should be achievable at moderate cost. The time buckets we proposed were intended as the minimum detail to be included in the breakdown, although as we expect the total of past due assets to be disclosed, the less than 30 day amount will also be included. This is not meant to rule out banks providing further sub-divisions as they see fit, as some currently do. On the precise definition of the boundaries, practice varies, but the majority of banks that currently provide a breakdown use the following, so we intend to stick with this:

Overdue < 30 days	30 days overdue 60 days	60 days overdue 90 days	Overdue 90 days

Some responses pointed out that the proposed disclosure of renegotiated assets at the half year, to match that required by NZ IFRS 7 at the full year, is out of date given the IASB's recent

amendment to IFRS 7 to remove the required disclosure of renegotiated assets. They also referred to the reasons that the IASB gave for this change, namely that it is difficult, especially for a large portfolio of loans, to ascertain which loans were renegotiated to avoid becoming past due or impaired rather than for other commercial reasons. Although we believe that the amount of renegotiated assets is conceptually valuable information about a bank's credit risk, we accept that it is problematic to produce a value that is reliable enough to be signed off by directors or auditors.

Action: drop the proposed disclosure of renegotiated assets.

Questions 36-37: disclosure of Basel Pillar 3 information (section 4.2.5)

Feedback on this area was generally in favour of the changes proposed, especially the reduction in the capital adequacy disclosure in the off quarters from full detail to summary.

All of the banks that are subject to the IRB approach to Basel II capital ratios opposed the proposal to switch from disclosing the capital ratio for the solo registered bank on a Basel I basis to a Basel II basis, advising that this change would require a significant amount of work. Some noted that they would not be able to do this in time for the proposed start date of Q1 2011, and also that this might make it impossible for them to meet the proposed two month deadline for interim reporting in future. They also questioned why the Reserve Bank requires solo capital ratios when the Basel framework does not.

In response, we note that as it is ultimately the separately-incorporated registered bank that can fail, it is important that the bulk of the capital within a banking group remains in the registered bank itself. The Reserve Bank does not (generally) impose a minimum solo capital adequacy requirement in conditions of registration, so disclosure is a key means of monitoring alignment with this objective.

The Basel II capital adequacy framework has now been in place long enough that we think it is time to remove the Basel I framework from our supervisory regime altogether. We have confirmed above the removal of risk-weighted assets (which are on a Basel I basis) from branch disclosure, and as previously noted we will also shortly be removing the "floor" of 90% of the Basel I requirement which currently applies to banks subject to the Basel II IRB approach. These decisions strengthen the case to proceed with disclosure of solo capital adequacy on a Basel II basis by IRB banks.

However, we believe that it will be sufficient for solo capital adequacy ratios to be disclosed as part of the detailed capital adequacy disclosure at the half- and full-year points, not in the off-quarter summaries as well. We also acknowledge banks' concerns about the development work needed to make this change, so we intend to include a six-month transition period, with solo ratios to be disclosed on a Basel II basis starting with disclosure for the period to 30 September 2011.

IRB banks are required to multiply all risk-weighted asset figures for credit risk by a scalar set in their conditions of registration. We noted in the CP that there was some confusion about the way in which banks disclose the impact of this scalar on their calculation of required capital, and proposed that the impact only be shown at the final stage of the calculation. This was not generally supported. However, we think that it is helpful practice to footnote the "risk-weighted exposure" column to the effect that the figures include the scalar (currently 1.06), as some banks currently do. We also note some divergence between the banks on which components of the actual capital calculation the scalar applies to. While this issue relates to our capital adequacy rather than disclosure requirements, we note here that the scalar is intended to apply to all credit-risk related risk-weighted exposures for IRB banks, namely: credit risk subject to the IRB approach; specialised lending subject to the slotting approach; equity exposures; and credit risk exposures subject to the standardised approach.

Action: IRB banks to disclose solo capital ratios on a Basel II IRB basis in full-year and six monthly disclosure statements, after a six month transitional period. OiCs to spell out more clearly how the impact of the scalar on risk-weighted exposures should be shown.

Questions 38 – 39: disclosure of liquidity risk (section 4.2.6)

We said in the CP that we had not yet reached the point where we were ready to propose new detailed disclosure of liquidity risk linking in to the Reserve Bank's liquidity policy (BS13). We did however make suggestions on the disclosure of bank's funding maturity profiles in line with the expected removal of the detailed requirements in this area in NZ IFRS 7 Appendix E. We also noted the need for some improvement in the disclosure of liquid assets that banks hold to help manage their liquidity risk.

There was general support for the objectives we set out for the changes in liquidity disclosure. But several responses noted that the proposal to mandate certain time buckets for the maturity ladder could result in banks having to produce two separate maturity ladders to meet IFRS requirements and to satisfy the disclosure Orders. It was also noted that maturity ladders are burdensome to produce, do not change rapidly over time, and are regarded as not being very informative about liquidity risk, which argues against quarterly disclosure. On the other hand, one user is keen to see standardised information on a quarterly basis to improve comparability across the banks. We also note that not all banks include an "on demand" time band in their funding maturity analysis, which for banks seems to us particularly important.

On liquid assets, our concern is that it is not always clear from disclosure statements which assets banks actually hold to manage liquidity risk, as opposed to the amounts of assets in various balance sheet categories such as "liquid assets" and "trading securities". A number of banks do provide a reconciliation between their own liquidity assets and balance sheet items, but we would expect a bank to disclose this annually in any case because of the requirement in NZ IFRS 7 to disclose an analysis of the "financial assets it holds for managing liquidity risk". More

frequent disclosure of liquidity assets is justified by the possibility of the balances changing more rapidly.

Balancing these points, our proposed way forward is as described below. We regard this as an interim solution, and plan to consult further in due course on additional liquidity disclosures, probably based on amounts defined in BS13.

Action: at the half year, require quantitative liquidity risk disclosure on the same basis as at the full year, in compliance with NZ IFRS 7 (but current period only, and group figures only). Require banks, in complying with this, to add at least an on-demand maturity band to the required maturity analysis, if it is not already included to comply with NZ IFRS 7. At the off quarters, banks should disclose an analysis of the financial assets they hold for managing liquidity risk, consistent with the equivalent disclosure at the half year in line with NZ IFRS 7.

Question 40: disclosure of connected exposures (section 4.2.7)

We proposed either to cut altogether the required disclosure of amounts defined with reference to the Reserve Bank's Connected Exposures Policy (BS8), or to reduce its frequency from quarterly. We noted that any breach of the limits imposed by BS8 would have to be disclosed in any case as a breach of conditions of registration.

There was only one response in favour of keeping the disclosure of this information at quarterly frequency, and several were keen to see it removed altogether. Another response noted that the disclosure was useful in providing more information on the mechanics of how the BS8 condition has been met, as opposed to the simple absence of a breach.

Action: require disclosure of the same information on connected exposures as now, but only annually (to include peak end-of-day exposure over the year), and with no requirement for previous period comparisons.

Question 41: historical summary of financial statements (section 4.2.7)

Most submissions noted that users find such a summary useful, and that is not very burdensome to produce. It was generally agreed that it can be reduced in frequency to annual. One bank noted that they produce both the historical summary to comply with this requirement, and their own five year "in brief" summary of performance which they suggest adds additional valuable information. However, we note that we only intend this requirement to set the minimum contents for the historical summary, as it says that the disclosure "must include the following". We welcome banks adding additional rows to the historical summary if they see them as useful. There also appears to be some uncertainty about what is required for "total impaired asset expense" so we will replace this with "total impairment losses charged to the income statement".

Action: require disclosure of historical summary of financial statements as now, but only annually. Clarify that banks may include additional rows. Clarify the definition of the impaired asset charge to be included.

Other separate proposals (section 4.2.7)

Interest rate re-pricing schedule

There was general concern about the proposal to require quarterly disclosure of this schedule, on the grounds of the burden of producing it, the relatively slow rate of change in the numbers, and questions about the value of the information for readers of disclosure statements. A couple of banks pointed out that the specific requirement to publish an interest rate re-pricing schedule is only in Appendix E of NZ IFRS 7, and that interest rate sensitivity analysis can be presented using a value-at-risk approach. However, one user noted the value of requiring standardised maturity bands and quarterly disclosure for being able to carry out cross-bank comparison.

Action: reduce the frequency of this disclosure to half-yearly, but keep the content as proposed. (This includes the half-year requirement being only for the current period, and only on a consolidated basis.) Clarify that additional columns for totals and for non-interest rate sensitive items are also required.

Prescribed quarterly disclosure of lending and funding concentrations

We proposed to require that banks use current ANZSIC codes when providing the industry sector breakdown of lending and funding concentrations, in order to enhance comparability across banks. However, one bank noted that they do not currently classify their customers using ANZSIC codes, and at least one other still uses the 1996 version rather than the 2006 revision. This means it would not be feasible for this to be mandated as a firm requirement from end-March 2011. However, as part of this we also proposed that one of the ANZSIC sub-categories which should be singled out is agriculture, as not all banks currently do so even when it is material to them. We think this is still worth requiring, even if it will not necessarily completely follow the commonly used high-level ANZSIC categorisation.

We also proposed to increase the frequency of this disclosure to quarterly. As with the previous proposal, there were some comments that this information does not change that rapidly from quarter to quarter, and that it is burdensome to produce, so we are dropping this proposal.

Action: include the disclosure on credit risk and funding concentration required by NZ IFRS 7 (excluding Appendix E) in the half-year disclosure (but not off-quarter). Require that any credit risk sector concentration breakdown provided includes lending for agriculture separately, if material to the bank. (The half-year requirement will only be for current period figures, and only on a consolidated basis.)

Specified balance sheet and income statement items

There was general consensus with our proposals on this, with only one bank disagreeing. The off-quarter OiCs currently include a full list of prescribed items to be included in the income statement and balance sheet. Particularly now that we have confirmed that financial statements included in banks' disclosure statements for every interim period will comply with NZ IAS 34, we prefer to leave the general content of balance sheet and income statement to banks' own approaches complying with NZ IAS 34. As proposed in the CP, we see only limited need for specific items to be required, for instance to ensure that fair value adjustments can be separately identified from "other income", and to provide sufficient information on assets used to manage liquidity risk (see questions 38-39 above). These will be required as an overlay to the financial reporting requirements.

There was some comment that any specified breakdown should only need to be provided in the notes to the accounts, not on the face of the balance sheet or income statement: we have no problem with that, and will ensure that the requirements make that clear.

Action: the comprehensive list of prescribed balance sheet and income statement items currently required for the off quarter will be replaced (at the off quarter and half year) by reliance on NZ IAS 34, with specification of a few key items that must be included.

Related party lending in interim disclosures

Since the full detail required by NZ IAS 24 *Related Party Disclosures*, and also the information on amounts under the Reserve Bank Connected Exposures policy will only be disclosed annually under the new approach, we proposed that in the other periods, there should be disclosure of total amounts due to and from related entities. Only one bank disagrees with this proposal. Another bank was concerned that if this extended to all persons captured by NZ IAS 24 (including directors and other key management personnel), the burden of quarterly disclosure would outweigh the benefits.

We plan to go ahead with this proposal. On the question of scope, we agree that balances and transactions with key management personnel should be excluded (this is also understood to exclude eg close family members of, and entities controlled by, key management personnel).

Action: require quarterly disclosure of aggregate amounts due to and from related entities, and of any material transactions with related entities or material changes in arrangements with related entities, excluding amounts in relation to key management personnel.

Securitisation / funds management / insurance business

This was another area where those that commented supported our approach, except for one bank. However, the approach proposed in the CP implied three different disclosure formats, and in the light of general comments that it would be preferable to align the half-year and off-quarter

disclosure as far as possible (see next section), this is an area where we think there is limited downside in further rationalisation to reduce the half-year disclosure to match the off-quarter's. However, the aggregate amount of insurance business (if any) conducted by the banking group will be required quarterly, since this is an amount calculated in accordance with, and limited by, a bank's conditions of registration.

For branches, the aggregate amount of insurance business within the New Zealand banking group will be required quarterly as at present, but information on securitisation, funds management etc is currently only required six-monthly, and this will be reduced to annually.

Action: aggregate amount of insurance business required quarterly for all banks. For locally-incorporated banks, current full detail on securitisation etc will be required annually, in other periods only material updates on the nature of such business and how it is controlled. For branches, full detail on securitisation etc as currently required at the full and half year will continued to be required at the full year, no disclosure will be required in other periods.

Making half-year and off-quarter disclosure the same

Two respondents suggested that the content of disclosure statements should be the same for the half year as for the off quarters. We agree that this would have benefits both for banks preparing disclosure statements, in terms of compliance burden, and for readers by improving comparability of disclosure statements across different reporting periods.

Financial statements included in disclosure statements will be prepared in accordance with NZ IAS 34 *Interim Reporting* for both the off-quarter and the half-year periods (see under questions 9-11 above), which will go some way towards achieving this aim. We have also identified some further adjustments in the OiC requirements for both the half-year and off-quarter disclosure, to bring the half-year reporting closer to the off-quarter reporting. Many of these changes result in full information being given at the full year, with updates only required in any interim period if there have been material changes.

In a few key areas however, we judge that cutting back the half-year disclosure to match that at the off quarter would mean losing key risk information from the half-year disclosure that needs to be provided more frequently than annually, while the converse would mean imposing an unreasonable quarterly burden on the banks. For instance there are some areas (discussed above) where the consultation paper suggested standard disclosure on a quarterly basis, but where we are now recommending that this be pulled back to six-monthly on the basis of feedback from the banks. Taking this into account leaves the following few areas where off-quarter disclosure will remain briefer than at the half year, or will be nil:

- Pillar 3 capital adequacy information (briefer) (in line with Basel Pillar 3 requirements);
- credit impairment information (briefer);

- interest rate repricing schedule (nil);
- liquidity risk (briefer);
- credit exposure sector concentrations (nil);
- funding concentrations (nil).

Option to delay start date

One bank noted that they might find it hard to make all the necessary changes to their systems and processes to be able to publish disclosure statements on the new basis for periods starting from Q1 2011. Some other banks however are strongly in favour of switching as early as possible. We do not see material problems for users of disclosure statements in having some banks disclosing on the old basis and some on the new basis during an interim period.

Action: include a transition period of six months in the revised Orders, so that banks can choose between end-March, end-June and end-September 2011 as the first balance date for reporting on the new basis.

November 2010