2018 ANNUAL REPORT

Year ended 31 August 2018

CONTENTS

Bank of Queensland Limited
ABN 32 009 656 740
AFSL NO. 244616

ABOUT THIS REPORT

This 2018 Annual Report (**Report**) incorporates the Group's audited financial statements and other statutory disclosures. The Report is lodged with the Australian Securities Exchange (**ASX**). Bank of Queensland (**BOQ**) is publicly listed in Australia. The financial statements have been prepared in accordance with Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board (**AASB**) and the *Corporations Act 2001*.

Unless otherwise stated, the Report encompasses all BOQ activities for the financial year commencing on 1 September 2017 and ending 31 August 2018. All monetary values in this document are presented in Australian dollars, which is the Bank's functional currency.

OUR 2018 REPORTING SUITE

BOQ produces a range of reports designed to meet the evolving expectations of a wide range of stakeholders. Our 2018 reporting suite consists of the following additional documents:

ANNUAL REVIEW

BOQ's 2018 Annual Review (**Review**) provides an overview of BOQ's operations across the Group and outlines our commitment to, and strategies for creating long-term value for shareholders, customers, employees and the community. It can be found on the Annual Reports page of our website.

SUSTAINABILITY REPORT

Our sustainability reporting evolved this year from online content to a standalone 2018 Sustainability Report available on the Annual Reports page of our website. This report is supported by supplementary information available on the Sustainability section of the BOQ website. It outlines information about our performance against BOQ's social, environmental and economic opportunities and challenges.

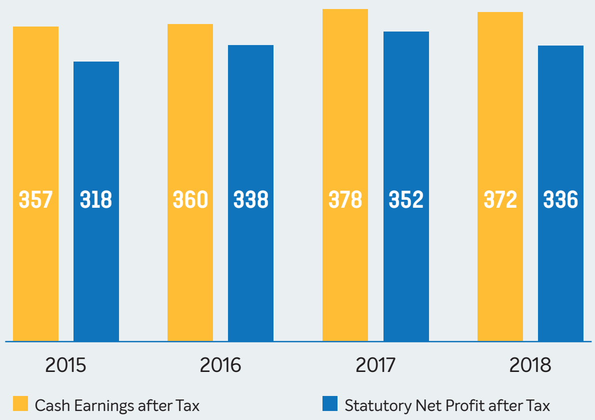
CORPORATE GOVERNANCE STATEMENT

Our 2018 Corporate Governance Statement discloses how we have complied with the ASX Corporate Governance Council's *Corporate Governance Principles & Recommendations* (3rd edition) and is available on the Corporate Governance page of our website.

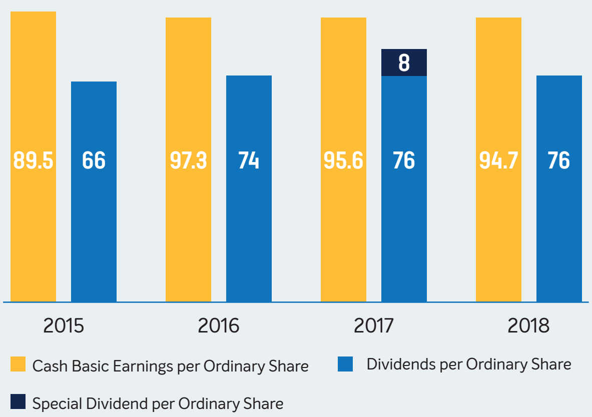
We are always looking for ways to evolve and improve our reporting. Please send your questions, comments or suggestions to our Investor Relations team at **InvestorRelations@boq.com.au**.

OUR 2018 PERFORMANCE

PROFIT RESULTS ($m)



EARNINGS & DIVIDENDS
(¢ per ordinary share)



2018 CASH EARNINGS AFTER TAX

$372m

↓2% from FY17

STATUTORY NET PROFIT AFTER TAX

$336m

↓5% from FY17

CASH BASIC EARNINGS PER ORDINARY SHARE
(¢ per share)

94.7¢

↓3% from FY17

DIVIDENDS PER ORDINARY SHARE
(¢ per share)

76¢

Unchanged from FY17

NET INTEREST MARGIN

1.98%

Up 5bps from FY17

CASH COST TO INCOME RATIO

47.5%

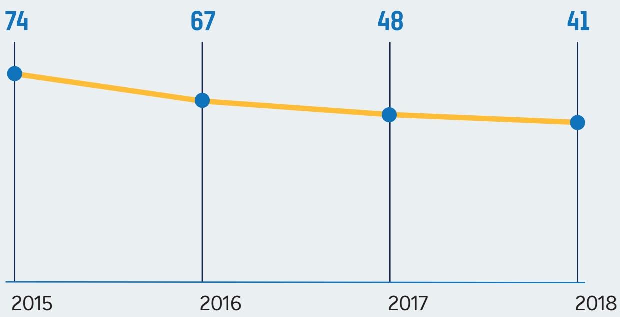
Up 90bps from FY17

CASH RETURN ON EQUITY

9.9%

Down 50bps from FY17

LOAN IMPAIRMENT EXPENSE ($m)



$41m

↓15% from FY17

MESSAGE FROM THE CHAIRMAN AND MANAGING DIRECTOR & CEO

Dear Shareholder

We are pleased to update you on another solid twelve months for Bank of Queensland. While there is no doubt that 2018 has been a year of turmoil for the banking industry, at BOQ we have been focused on implementation of our strategy and ensuring the fundamentals of our business remain strong.

In terms of financial performance, we delivered cash earnings after tax of $372 million. This was a reduction of $6 million or two per cent on 2017. After adjusting for the $16 million one-off profit on the disposal of a vendor finance entity which occurred in 2017, the result was a three per cent increase on an underlying basis. The final ordinary dividend of 38 cents per share was maintained, taking the full year dividend to 76 cents per share.

The Group's balance sheet continued to grow with lending growth of $1.5 billion funded by an improved mix of deposits. The niche commercial lending segments, as well as housing loan growth in Virgin Money Australia and BOQ Specialist contributed strongly to this lending growth. The BOQ Finance business provided a solid contribution with growth of $250 million in its asset finance portfolio. Deposits were driven primarily through the branch network, which focused on encouraging more customers to make BOQ their main financial institution. Despite a number of margin headwinds emerging during the year, this supported an improvement in net interest margin to 1.98 per cent.

Operating expenses were well contained, while important investments in the business were made in line with the Group's strategy. This included a new web experience platform which has delivered an improved digital experience to customers across all of our brands. Further work is underway on the modernisation of our technology architecture. We have also commenced development which will facilitate participation in the New Payments Platform, an industry initiative which will improve the experience for consumers making payments.

Asset quality metrics remain a key strength for BOQ. The ongoing improvements are a direct consequence of deliberate steps taken to clearly articulate risk appetite, lift risk capability and embed more stringent risk practices across the business. Impaired assets reduced by 15 per cent to $164 million, while loan impairment expense reduced 15 per cent to $41 million. Loan arrears remain at benign levels. Regulators have been focusing on responsible lending practices. We are pleased to report that BOQ has been ahead of the curve in this regard.

Our strong capital position has provided flexibility to consider a range of options for capital management. As a result, we have announced plans to increase our capital investment in 2019, with a focus on enhancements to our digital platforms and customer experience.

This investment in the future will provide a much needed boost to our customer offering and allow us to compete more effectively.

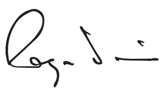
We announced the sale of the St Andrew's Insurance business to Freedom Insurance Group in April 2018. The dynamics of the insurance market have changed significantly since the acquisition of St Andrew's in 2010, and it was determined that a sale was the best outcome for shareholders as well as for the St Andrew's business. This transaction is subject to regulatory approvals.

The banking sector has faced intense scrutiny in 2018. The number of inquiries, reviews and the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry has highlighted how the sector has fallen short of meeting community expectations. Some of the findings that have emerged reflect poorly on the industry and has tested the reputation of all banks. In the case of BOQ, we have been increasing our focus on ensuring that ethical conduct is embedded in everything we do and when mistakes are made, we fix them.

Looking ahead, the operating environment remains challenging with ongoing scrutiny, regulatory change, slowing credit growth, technological change and higher funding costs all adding pressure to earnings growth.

We remain confident that we have the right strategy to navigate this environment and to continue delivering value for our stakeholders into the future.

We would like to thank all of our people and shareholders for your ongoing support and encourage you to review our annual reporting suite for more detail on what has been happening at BOQ in 2018.



Roger Davis
Chairman

Jon Sutton
Managing Director & CEO

2018 DIRECTORS' REPORT

DIRECTORS' REPORT

For the year ended 31 August 2018

The Directors present their report together with the financial report of Bank of Queensland Limited (**the Bank** or **BOQ**) and of the Consolidated Entity (or **Group**), being the Bank and its controlled entities, for the year ended 31 August 2018 and the independent auditor's report thereon.

DIRECTORS' DETAILS

The Directors of the Bank at any time during or since the end of the financial year are:

Name, qualifications and independence status	Experience, special responsibilities and other Directorships
ROGER DAVIS *B.Econ. (Hons), Master of Philosophy* Chairman Non-Executive Independent Director	Mr Davis was appointed Chair of BOQ on 28 May 2013 and has been a Non-Executive Director since August 2008. He has over 33 years' experience in banking and investment banking in Australia, the US and Japan. He was previously a Managing Director at Citigroup where he worked for over 20 years and more recently was a Group Managing Director at ANZ Bank. Mr Davis is currently Chair of AIG Australia Limited and a Non-Executive Director of Argo Investments Limited and Charter Hall Retail Management Limited and was formerly a Non-Executive Director of Aristocrat Leisure Ltd, Ardent Leisure Group, Ardent Leisure Management Ltd and Ardent Leisure Ltd. Mr Davis has a Bachelor of Economics (Hons) degree from the University of Sydney and a Master of Philosophy degree from Oxford. Mr Davis is Chair of the Nomination & Governance Committee, a member of each of the Audit and Risk Committees, and an attendee at all other Board Committees.
JON SUTTON Managing Director & CEO Executive Director	Mr Sutton was appointed Managing Director and Chief Executive Officer in January 2015 following four months as our Acting Chief Executive Officer. Mr Sutton originally joined BOQ in July 2012 as our Chief Operating Officer. Mr Sutton has more than 20 years' experience in banking and prior to BOQ was the Managing Director of Bankwest. Before that, as Executive General Manager of Commonwealth Bank Agribusiness (**CBA**), he was central to the establishment of CBA's agribusiness segment which grew strongly under his guidance and leadership. Prior to this, Mr Sutton was General Manager of Client Risk Solutions at CBA, responsible for marketing derivative products including interest rates, commodities and foreign exchange. He was also Head of Resources and Agribusiness and Head of Corporate Risk Management Commodities, charged with marketing and commodity hedging products to Australian institutions within the base metals, precious metals and energy sectors.
BRUCE CARTER *B Econ, MBA, FAICD, FICA* Non-Executive Independent Director	Mr Carter was appointed a Director of BOQ on 27 February 2014. Mr Carter was a founding Managing Partner of Ferrier Hodgson South Australia, a corporate advisory and restructuring business, and has worked across a number of industries and sectors in the public and private sectors. He has been involved with a number of state government-appointed restructures and reviews including chairing a task force to oversee the government's involvement in major resource and mining infrastructure projects. Mr Carter had a central role in a number of key government economic papers including the Economic Statement on South Australian Prospects for Growth, the Sustainable Budget Commission, and the Prime Minister's 2012 GST Distribution Review. Mr Carter has worked with all the major financial institutions in Australia. Before Ferrier Hodgson, Mr Carter was at Ernst & Young for 14 years including four years as Partner in Adelaide. During his time at Ernst & Young, he worked across the London, Hong Kong, Toronto and New York offices. Mr Carter is the Chair of Australian Submarine Corporation and Aventus Capital Limited, Deputy Chair of SkyCity Entertainment Group Limited and a Non-Executive Director of Eudunda Farmers Ltd and Genesee & Wyoming Inc. Mr Carter is Chair of the Risk Committee and a member of the Audit Committee, Information Technology Committee and the Nomination & Governance Committee.

DIRECTORS' REPORT

For the year ended 31 August 2018

Name, qualifications and independence status	Experience, special responsibilities and other Directorships
RICHARD HAIRE *B.Ec, FAICD* Non-Executive Independent Director	Mr Haire was appointed a Director of BOQ on 18 April 2012. Mr Haire has more than 29 years' experience in the international cotton and agribusiness industry, including 27 years in agricultural commodity trading and banking. He is Chair of the Cotton Research and Development Corporation and Reef Corporate Services Limited and serves as a Non-Executive Director of BEC Stockfeed Solutions Pty Ltd. Mr Haire was formerly a Director of Open Country Dairy (NZ) and New Zealand Farming Systems Uruguay. Mr Haire is Chair of the Audit Committee, and a member of each of the Risk, Human Resources & Remuneration and Information Technology Committees.
JOHN LORIMER *B Com* Non-Executive Independent Director	Mr Lorimer was appointed a Director of BOQ on 29 January 2016. Mr Lorimer has spent more than 30 years in financial services and held executive roles in Australia, Asia and Europe. Mr Lorimer's most recent executive roles were in the United Kingdom where he was Group Head of Finance and then Group Head of Regulatory Risk and Compliance for Standard Chartered Bank. He also held a number of management positions in the retail bank of Citigroup and served as the Chairman of CAF Bank Limited (a subsidiary of Charities Aid Foundation based in the United Kingdom). He is a Non-Executive Director of Bupa Australia Pty Ltd, Bupa Aged Care Holdings Pty Ltd, Bupa Asia Ltd (HK) Ltd, Max Bupa (India) Ltd and Aberdeen New Dawn Investment Trust plc. Mr Lorimer is a member of the Information Technology and Risk Committees.
WARWICK NEGUS *B Bus, M Com, SF Fin* Non-Executive Independent Director	Mr Negus was appointed a Director of BOQ on 22 September 2016. Mr Negus brings more than 30 years of finance industry experience in Asia, Europe and Australia. His most recent executive roles include Chief Executive Officer of 452 Capital, Chief Executive Officer of Colonial First State Global Asset Management and Goldman Sachs Managing Director in Australia, London and Singapore. He was also a Vice President of Bankers Trust Australia and a Director of the University of NSW Foundation and FINSIA. Mr Negus is Chair of Pengana Capital Group and URB Investments Limited and a Non-Executive Director of Washington H Soul Pattinson & Co Ltd, Virgin Australia Holdings Limited and Terrace Tower Group. He is a member of the Council of UNSW and Chair of UNSW Global Limited. Mr Negus is a member of the Audit Committee and Human Resources & Remuneration Committee.
KAREN PENROSE *B Com, CPA, FAICD* Non-Executive Independent Director	Ms Penrose was appointed a Director of BOQ on 26 November 2015. Ms Penrose is an experienced non-executive director and banker. As a banker, Karen has 20 years' experience leading businesses within Commonwealth Bank of Australia and HSBC and over ten years in accounting and finance roles. Ms Penrose has particular expertise in the financial services, property, resources and energy sectors. Ms Penrose is a Non-Executive Director of Vicinity Centres Limited, Spark Infrastructure Group and Future Generation Global Investment Company Limited (pro bono role). Ms Penrose was formerly a Non-Executive Director of AWE Limited and Landcom. She is a member of Chief Executive Women. Ms Penrose is a member of each of the Audit and Human Resources & Remuneration Committees.

DIRECTORS' REPORT

For the year ended 31 August 2018

Name, qualifications and independence status	Experience, special responsibilities and other Directorships
MICHELLE TREDENICK *B Sc, FAICD, F Fin* Non-Executive Independent Director	Ms Tredenick was appointed a Non-Executive Director of BOQ in February 2011. Ms Tredenick is an experienced company director and corporate advisor with over 30 years' experience in leading Australian businesses. Ms Tredenick is currently a Non-Executive Director of Insurance Australia Group Limited, Cricket Australia and Urbis Pty Ltd. She is a member of the Senate of the University of Queensland as well as sitting on the board of the Ethics Centre. Ms Tredenick has previously held executive roles and been a member of the Executive Committee at National Australia Bank, MLC and Suncorp. Her experience includes holding the position of Chief Information Officer with each of these companies as well as Head of Strategy and Marketing and divisional profit and loss roles in Corporate Superannuation, Insurance and Funds Management. Ms Tredenick is also formerly a Non-Executive Director of Vocation Limited (in Liquidation). Ms Tredenick is Chair of the Information Technology Committee, and is a member of each of the Human Resources & Remuneration, Risk and Nomination & Governance Committees.
DAVID WILLIS *B Com, ACA, ICA* Non-Executive Independent Director	Mr Willis was appointed a Director of BOQ in February 2010. Mr Willis has over 35 years' experience in financial services in the Asia Pacific, the UK and the USA. He is a qualified Accountant in Australia and New Zealand and has had 26 years' experience working with Australian and foreign banks. Mr Willis is a Non-Executive Director of CBH Grain Cooperative and Interflour Holdings Pte Ltd, a Singapore-based flour milling company. Mr Willis is the founder of Sydney-based Charity "The Horizons Program". Mr Willis is Chair of the Human Resources & Remuneration Committee, and is a member of each of the Risk and the Nomination & Governance Committees. He is also a Non-Executive Director of BOQ's insurance subsidiaries, St Andrew's Australia Services Pty Ltd, St Andrew's Life Insurance Pty Ltd and St Andrew's Insurance Pty Ltd.
MARGARET (MARGIE) SEALE *BA, FAICD* Non-Executive Independent Director (resigned effective 28 June 2018)	Ms Seale was appointed a Director of BOQ on 21 January 2014. Ms Seale has more than 25 years' experience in senior executive roles in Australia and overseas in the global publishing, health and consumer goods industries, and in the transition of traditional business models to adapt and thrive in a digital environment. Most recently she was Managing Director of Random House Australia (with managerial responsibility for Random House New Zealand) and President, Asia Development for Random House Inc., the global company. Ms Seale remained on the Board of Penguin Random House as a Non-Executive Director and then as Chair until September 2016. Amongst other roles prior to those at Random House, she has held national sales and national marketing roles with Oroton and Pan Macmillan respectively. Ms Seale is a Non-Executive Director of Telstra Corporation Limited, Ramsay Health Care Limited, Scentre Group Limited, Carindale Property Trust and APH Holdings Pty Ltd. She has also served on the boards of the Australian Publishers' Association, The Powerhouse Museum and Chief Executive Women. Prior to her resignation as a Director of BOQ on 28 June 2018, Ms Seale was a member of the Information Technology Committee and Human Resources & Remuneration Committee.

DIRECTORS' REPORT

For the year ended 31 August 2018

COMPANY SECRETARIES

MICHELLE THOMSEN

LLB/B Comm

On 18 January 2018, Ms Michelle Thomsen stepped down from her role as Company Secretary, but remained as General Counsel until 29 June 2018.

VICKI CLARKSON

BA/LLB (Hons), FGIA, FCIS, GAICD

Ms Clarkson joined BOQ as Company Secretary on 3 April 2017. Ms Clarkson commenced her career as a corporate lawyer at Blake Dawson Waldron (now Ashurst) before joining Clayton Utz. Prior to working for BOQ, Ms Clarkson held senior legal and governance roles in ASX listed entities including Aurizon Holdings Limited, Flight Centre Limited and Shine Corporate Ltd. Ms Clarkson is an active member and Deputy Chair of the Queensland State Council of the Governance Institute of Australia.

DIRECTORS' MEETINGS

The number of meetings of the Bank's Directors (including meetings of Committees of Directors) and the number of meetings attended by each Director during the financial year were:

	Board of Directors		Board of Directors – St Andrews		Risk Committee		Audit Committee		Nomination & Governance Committee		Human Resources & Remuneration Committee –BOQ & St Andrews		Information Technology Committee		Investment Committee	
	A	B	A	B	A	B	A	B	A	B	A	B	A	B	A	B
Roger Davis [(1)]	12	12	–	–	7	7	5	5	2	2	–	–	–	–	7	8
Jon Sutton [(2)]	11	12	5	6	–	–	–	–	–	–	–	–	–	–	8	8
Warwick Negus	12	12	–	–	–	–	1	1	–	–	2	2	–	–	6	8
Bruce Carter	12	12	–	–	7	7	5	5	2	2	–	–	2	2	8	8
Richard Haire	12	12	–	–	7	7	5	5	–	–	2	2	8	8	8	8
John Lorimer	12	12	–	–	7	7	–	–	–	–	–	–	6	8	–	–
Karen Penrose	12	12	–	–	–	–	5	5	–	–	7	7	–	–	6	6
Margaret Seale	9	9	–	–	–	–	–	–	–	–	5	5	6	6	–	–
Michelle Tredenick	12	12	–	–	7	7	–	–	2	2	7	7	8	8	–	–
David Willis [(3)]	11	12	6	6	6	7	–	–	2	2	7	7	–	–	2	2
Total number of meetings held	12		6		7		5		2		7		8		8	

A – Number of meetings attended

B – Number of meetings held during the time the Director was a member of the Board / Committee during the year. Mr Sutton's attendances as invitee are also listed.

(1) Roger Davis is Chair of the Nomination & Governance Committee, a member of each of the Audit and Risk Committees, and an attendee at all other Board Committees.

(2) Jon Sutton is also a member of the St Andrew's Audit Committee and Risk Committee. Additionally, Mr Sutton is invited by the Board to attend all of the Bank's Board Committee meetings (or part thereof).

(3) David Willis is also a member of the St Andrew's Audit Committee and Risk Committee.

2018 Corporate Governance Statement is online

BOQ complies with its constitution, the *Corporations Act 2001* (Cth), the ASX Listing Rules, and the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* (3rd Edition) (**ASX Principles**), which is reflected in our Corporate Governance Statement. As an entity regulated by the Australian Prudential Regulation Authority (**APRA**), BOQ also complies with the governance requirements prescribed by APRA under Prudential Standard CPS 510 *Governance*.

Information about BOQ's Board and management, corporate governance policies and practices and Enterprise Risk Management Framework can be found in the 2018 Corporate Governance Statement available at: *http://www.boq.com.au/aboutus_corporate_governance.htm*

DIRECTORS' REPORT

For the year ended 31 August 2018

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DIRECTORS' REPORT

For the year ended 31 August 2018

OPERATING AND FINANCIAL REVIEW

1. HIGHLIGHTS AND STRATEGY

1.1 DISCLOSURE CONSIDERATIONS

Future performance

This document contains certain 'forward-looking statements' about BOQ's business and operations, market conditions, results of operations, and financial condition, capital adequacy and risk management practices which reflect BOQ's views held and current expectations as at the date of this document.

Forward-looking statements can generally be identified by the use of forward-looking words such as 'anticipate', 'believe', 'expect', 'project', 'forecast', 'estimate', 'likely', 'intend', 'should', 'will', 'could', 'may', 'target', 'plan' and other similar expressions.

Forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors, many of which are beyond the control of BOQ and which may cause actual results to differ materially from those expressed or implied in such statements. Readers are cautioned not to place undue reliance on any forward-looking statements. Actual results or performance may vary from those expressed in, or implied by, any forward-looking statements.

BOQ does not undertake to update any forward-looking statements contained in this document, subject to disclosure requirements applicable to it.

Rounding

In accordance with applicable financial reporting regulations and current industry practices, amounts in this report have been rounded off to the nearest one million dollars, unless otherwise stated. Any discrepancies between total and sums of components in tables contained in this report are due to rounding.

Note on Statutory Profit and Cash Earnings

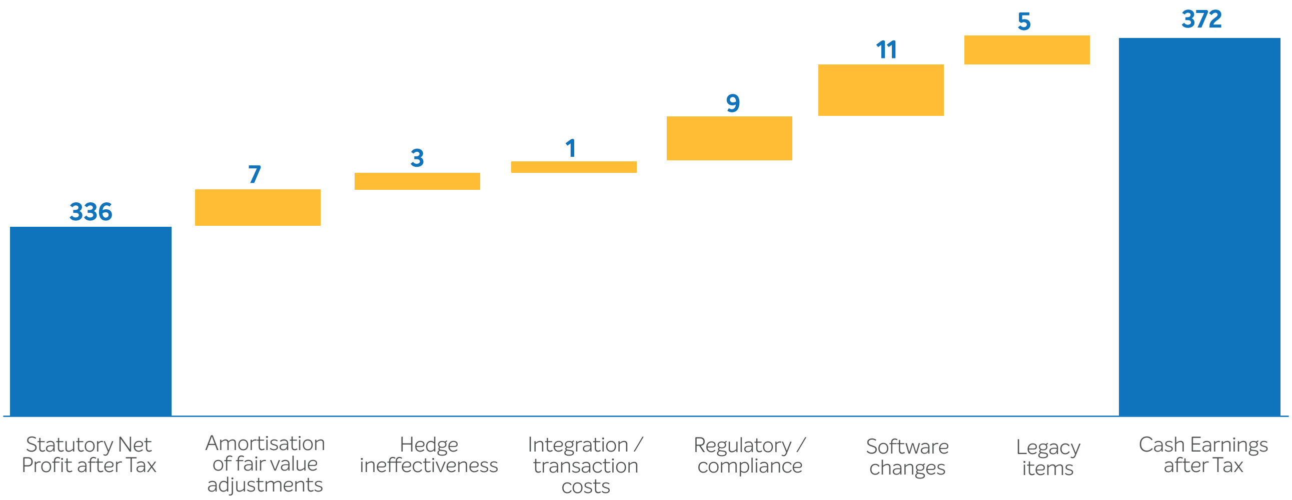
Statutory Profit is prepared in accordance with the *Corporations Act 2001* and the Australian Accounting Standards, which comply with International Financial Reporting Standards (**IFRS**). Cash Earnings is a non-Accounting Standards measure commonly used in the banking industry to assist in presenting a clear view of the Bank's underlying earnings. Refer to Section 5.1 of the Operating and Financial Review Appendices for the reconciliation of Statutory Profit to Cash Earnings.

The main exclusions relate to: Regulatory / compliance costs ($9 million after tax) which include external costs and other related costs associated with the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**), The Banking Executive Accountability Regime (**BEAR**), Code of Banking Practice and other regulatory matters; Legacy Items ($5 million after tax) which includes external legal and net settlement costs associated with the Petersen class action; and Software changes ($11 million after tax) which include a non-recurring adjustment due to a re-assessment of useful lives of existing assets aligned with the Group's Investment Roadmap and a change to the capitalisation policy. Hedge ineffectiveness represents earnings volatility from hedges that are not fully effective under the application of AASB 139 *Financial Instruments: Recognition and Measurement* and create a timing difference in reported profit. These hedges remain economically effective (Refer to the Reconciliation of Statutory Profit to Cash Earnings chart below).

Figures disclosed in this report are on a Cash Earnings basis unless stated as being on a Statutory Profit basis. Unless otherwise stated, all financial comparisons in this document refer to the prior half (**1H18**), current half (**2H18**) and the prior year (**FY17**).

These non-statutory measures have not been subject to review or audit.

Reconciliation of Statutory Profit to Cash Earnings ($m)

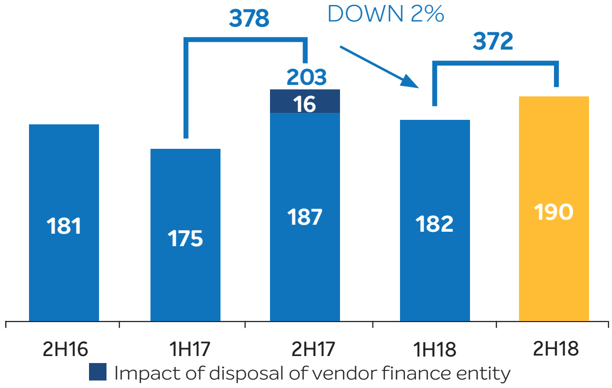


DIRECTORS' REPORT

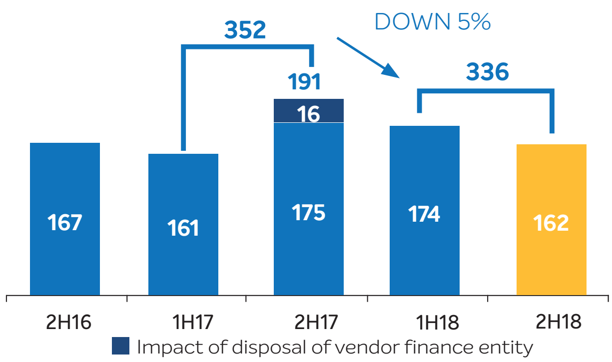
For the year ended 31 August 2018

1.2 GROUP HIGHLIGHTS

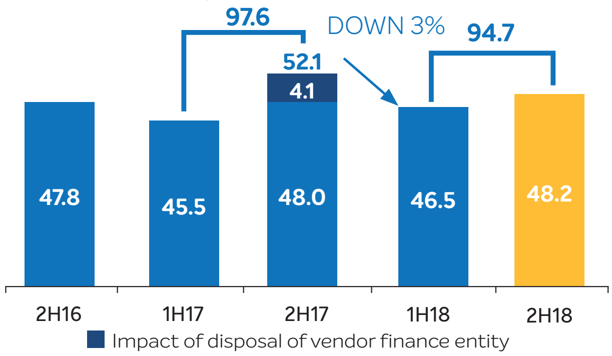
Cash Earnings after Tax ($m)



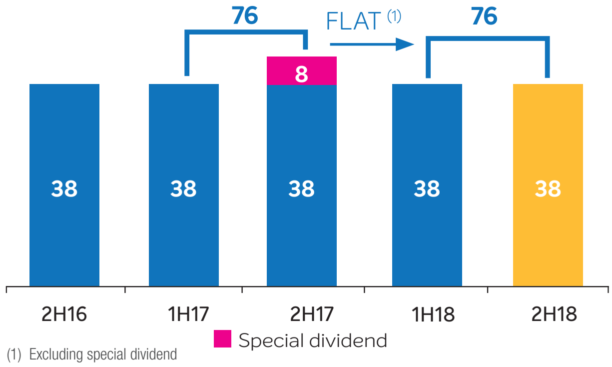
Statutory Profit after Tax ($m)



Cash Basic Earnings per Share (**EPS**) (cents)

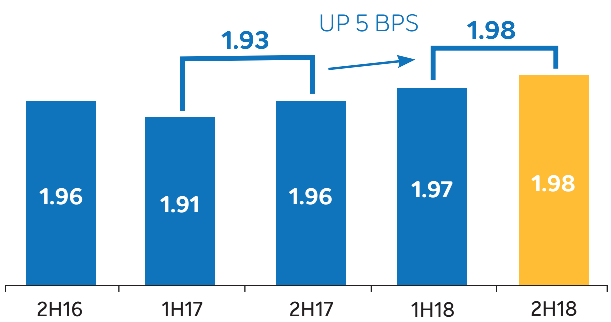


Dividends per ordinary share (cents)



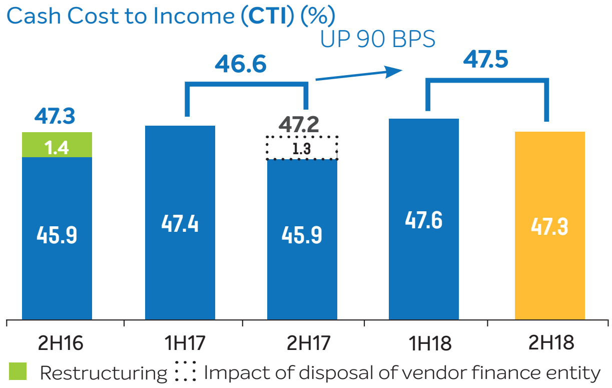
(1) Excluding special dividend

Cash Net Interest Margin (**NIM**) (%) (1)

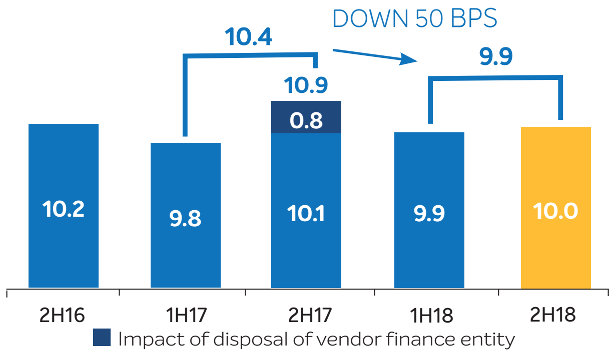


(1) NIM disclosed includes the impact of netting offset accounts against loan balances. Historical data has been previously disclosed excluding this netting.

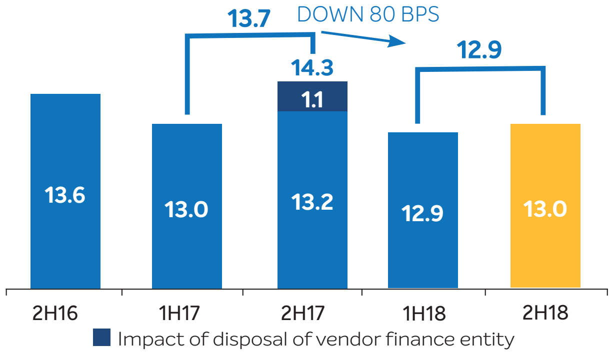
Cash Cost to Income (**CTI**) (%)



Cash Return on Average Equity (**ROE**) (%)



Cash Return on Average Tangible Equity (**ROTE**) (%)



DIRECTORS' REPORT

For the year ended 31 August 2018

1.2 GROUP HIGHLIGHTS (CONTINUED)

CASH EARNINGS AFTER TAX

$372m

Decreased by two per cent on FY17. Excluding the impact of the disposal of a vendor finance entity, increased by three per cent on FY17

CASH NET INTEREST MARGIN

1.98%

Up 5 basis points over FY17 driven by improvements in asset and funding mix (1)

OPERATING EXPENSES

$527m

Three per cent increase on FY17 while investing in technology initiatives and expanding new business lines

LOAN IMPAIRMENT EXPENSE

$41m

Down 2 basis points to 9 basis points of lending and a 15 per cent reduction over FY17

COMMON EQUITY TIER 1

9.31%

Decrease of 8 basis points for the year as a result of capital initiatives offset by positive underlying capital generation

DIVIDENDS

FINAL & INTERIM

$0.76

Flat on FY17

(1) Includes a movement in the weighted average life of mortgages. Refer to Section 2.2 Net interest income.

BOQ has generated cash earnings of $372 million in FY18, representing a two per cent decrease on FY17. Statutory net profit after tax decreased of five per cent on FY17 to $336 million. Excluding the one-off $16 million profit on disposal of a vendor finance entity which occurred in FY17, cash earnings increased three per cent on FY17. Statutory profit after tax was reduced by a number of one-off items including accelerated amortisation expense to create capacity for additional capital initiatives in FY19-20 aligned with the Group's Investment Roadmap.

Total income grew by one per cent from FY17, or two per cent on an underlying basis (excluding the $16 million profit on sale in FY17). This was driven by net interest income growth of four per cent, while non-interest income contracted 17 per cent (nine per cent on an underlying basis).

The improvement in net interest income was driven by a combination of growth in total lending of $1.5 billion or three per cent and an increase in NIM of five basis points to 1.98 per cent. Lending growth was achieved across all major portfolios, with housing loan growth of $653 million or two per cent, commercial loan growth of $569 million or six per cent and BOQ Finance growth of $250 million or six per cent. Housing loan growth was driven by Virgin Money (Australia) (**VMA**) and BOQ Specialist. Commercial lending growth was delivered primarily through targeted niche segments.

The five basis point increase in NIM was achieved through improvements in funding mix, repricing of assets and an extension of the behavioural weighted average life of the home loan portfolio. These benefits were offset by ongoing price competition for new business and a higher bank bill swap rate relative to the cash rate, which increased basis risk and the cost of hedging interest rate risk during the year. Non-interest income was lower as fees, trading and insurance income all reduced from FY17 levels.

Operating expense growth was contained to three per cent despite the rising cost of regulatory compliance, technological change and a need to continue investing in the business to maintain competitiveness.

Asset quality metrics remained sound across the portfolio with impaired assets reducing 15 per cent to $164m and loan impairment expense reducing 15 per cent to $41m. Loan arrears also remained at low and steady levels throughout the year. This is a direct result of a prudent approach to risk management, assisted by benign economic conditions.

BOQ's capital position remains strong with a Common Equity Tier 1 ratio (**CET1**) of 9.31 per cent. On 17 April 2018, the Bank announced it had entered into an agreement to sell the Group's controlled entities, St Andrew's Australia Services Pty Ltd, St Andrew's Insurance (Australia) Pty Ltd and St Andrew's Life Insurance Pty Ltd (**St Andrew's Group**), to Freedom Insurance Group Limited for total consideration of $65 million. The transaction remains subject to certain conditions including receipt of regulatory approvals. The capital released on the settlement of the transaction will be incremental to BOQ's CET1 ratio. Given BOQ's strong capital position, an increase in capital investment has been announced for FY19-20 to further enhance BOQ's digital platforms and customer experience.

The Board has determined to pay a final ordinary dividend of 38 cents per share. The total ordinary dividend for the year is 76 cents per share, unchanged from FY17.

DIRECTORS' REPORT

For the year ended 31 August 2018

1.3 STRATEGY

BOQ is a financial institution whose primary function is gathering deposits and lending. It is listed on the Australian Securities Exchange (**ASX**) and regulated by the Australian Prudential Regulation Authority (**APRA**) as an authorised deposit-taking institution (**ADI**). It is one of the top 100 companies by market capitalisation on the ASX.

BOQ was established in 1874 as the first Permanent Building Society in Queensland. It has evolved into a national bank with a network of retail branches, brokers and brands spanning every state and territory in Australia. The group is now comprised of a number of brands including BOQ, BOQ Specialist, BOQ Finance, VMA and St Andrew's Insurance.

BOQ aims to build a differentiated position in the Australian financial services sector by demonstrating to customers that "It's Possible to Love a Bank". BOQ's corporate strategy is to focus on niche customer segments that value a more intimate banking relationship. BOQ is one of Australia's leading regional banks, and one of the few not owned by one of the major banks. Most of BOQ's retail branches are run by local owner managers, meaning the person running the branch owns the branch. As small business owners, owner managers know what it means to deliver personal service. Through specialisation and deep industry knowledge in niche commercial segments, including medical & dental, corporate healthcare & retirement living, hospitality & tourism and agribusiness, BOQ provides a level of support to business banking customers unique to that offered by other banks.

BOQ is committed to engaging positively with all stakeholders in a fair and transparent way to create value for customers, employees, investors and the communities in which it operates. More information on BOQ's approach to sustainability is available in the 2018 Sustainability Report and in the sustainability section of the BOQ website (*https://www.boq.com.au/Shareholder-centre/sustainability*).

Information on BOQ's corporate governance practices can be located in BOQ's Corporate Governance Statement available on the corporate governance page of the BOQ website (*https://www.boq.com.au/About-us/corporate-governance*).

BOQ's corporate strategy is delivered through four strategic pillars: Customer in Charge; Grow the Right Way; There's Always a Better Way; and Loved Like No Other.

Customer in Charge is about improving customers' experience and expanding BOQ's avenues for growth by putting customers in charge of when, where and how they choose to engage with BOQ. This is regardless of whether they come into a branch, use online services, call on the phone or buy products through a third party intermediary.

BOQ's home loan products, including VMA home loans, are distributed by more than 6,000 accredited brokers, making the Bank more accessible to customers who prefer to use brokers. The Bank continued to expand its distribution into the mortgage broker market in FY18, with 30 per cent of new home loans originated through mortgage brokers. In FY18 BOQ also launched a new website to improve customers' digital experience. This followed similar upgrades for the VMA and BOQ Specialist websites during 2017. BOQ also continued the roll out of its new 'ICON' branch format, with 21 branches now converted to the new format. A new Customer Connect team has also been established, bringing together customer service capability across the enterprise into one group.

Grow the Right Way is about building a strong and profitable business by making the right decisions about where and how to grow. This includes focusing on niche customer segments that value an intimate banking relationship. The niche segments in the BOQ commercial portfolio contributed $623 million in new lending growth in FY18. Together with BOQ Specialist, BOQ Finance and VMA businesses, BOQ's niche strategy is delivering.

BOQ continued its conservative approach to lending, maintaining a high quality lending portfolio. In the branch network, as existing franchise agreements expire, BOQ is moving owner managers onto a new balanced scorecard agreement that includes a wider range of metrics, such as customer and compliance measures. 81 per cent of owner managed branches are now on the new franchise agreement. The Bank continues to transition Franchisees to the new agreement and has taken steps to align the balanced scorecard and commission arrangements with the Sedgwick recommendations for banking industry remuneration and incentives.

There's Always a Better Way is about BOQ's commitment to making systems and processes simpler, faster and smarter. The aim is to improve efficiency, reduce costs, deliver better customer service and establish a nimble organisation positioned to take advantage of a rapidly changing landscape. BOQ is digitising its lending platforms by making improvements to retail, commercial and lease management lending systems. Ongoing focus on efficiency across the Group has enabled it to contain expense growth to three per cent, whilst investing in new technology aligned to a simplified and business enabled target architecture which will enable it to respond more quickly to emerging opportunities than has been possible in the past.

Loved Like No Other is about how BOQ maintains positive stakeholder relationships by living its values, creating a place where people love to work and contributing to the communities in which it operates. These are just some of the things BOQ does to prove "It's Possible to Love a Bank".

In recent years BOQ has reinforced its commitment to ethical conduct through a commitment to the Banking and Finance Oath. The Bank has also built on its internal ethics training and conduct reporting, and introduced a range of team based initiatives to embed company values and drive a customer centric culture. It continues to demonstrate its commitment to a diverse and inclusive workforce by making significant progress on its reconciliation journey. Investment in the 'Customer Heartbeat' program in 2018 also signifies BOQ's commitment to supporting its people to enhance customer experience.

By focusing on the four strategic pillars, BOQ aims to deliver robust and sustainable financial performance, consistent growth in returns to shareholders and superior service to customers and the wider community.

DIRECTORS' REPORT

For the year ended 31 August 2018

1.4 RISK AND REGULATORY DEVELOPMENTS

The financial services industry continues to face heavy scrutiny from the Federal Government, regulators, investors and consumers. Over the past 12 months there has been a significant increase in regulatory consultations, inquiries and industry reviews which has led, or is leading to, a number of changes that could impact BOQ. The key areas of reform and areas of increased risk focus are outlined below.

REGULATORY DEVELOPMENTS

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

On 30 November 2017, the Federal Government announced the establishment of a Royal Commission into the Banking, Superannuation and Financial Services Industry to "ensure the Australian financial system is resilient, efficient and fair". The Hon. Kenneth Hayne AC QC has been appointed as Commissioner.

The Letters Patent was signed on 14 December 2017 and contains the terms of reference for the Commission. Under the terms of reference, the Commissioner is required to inquire into a range of matters, including:

- whether any conduct by financial service entities (including by directors, officers or employees or anyone acting on behalf of those entities) might have amounted to misconduct and, if so, whether the question of criminal or other legal proceedings should be referred to the relevant Commonwealth, State or Territory agency;
- whether any conduct, practices, behaviour or business activity by a financial services entity falls short of community standards and expectations;
- whether any misconduct or behaviour falling below community standards or expectations are attributable to the particular culture, governance and other practices of a financial services entity, the relevant industry or a subsector of the relevant industry;
- the effectiveness of mechanisms for redress for consumers of financial services who suffer detriment as a result of misconduct by financial services entities; and
- the adequacy of existing legislation, regulation, industry self-regulatory systems, and internal systems of financial entities in identifying and addressing misconduct, meeting community standards and expectations, and providing appropriate redress to consumers.

The Commission held its first public hearing on 12 February 2018. The Commission is required to submit a final report containing findings and recommendations to the Government by February 2019.

Productivity Commission inquiry into competition in the Australian financial system

The Productivity Commission (**Commission**) has undertaken an inquiry into competition in the Australian financial system. The Commission reviewed competition with a view to improving consumer outcomes, the productivity and international competitiveness of the financial system and economy more broadly, and supporting ongoing financial system innovation, while balancing financial stability objectives. The Commission's final report was published in August 2018. Key points from the Final Report include:

1) There have been periods of strong price competition in the past, for example the introduction of mortgage brokers, but the larger financial institutions still have the ability to exercise market power over their competitors and consumers.
2) This market power has been achieved with persistently opaque pricing, conflicted advice and remuneration arrangements, layers of public policy and regulatory requirements that support larger incumbents, and a lack of easily accessible information – meaning unaware customers maintain loyalty to unsuitable products.
3) Poor advice and complex information means customers remain attached to high margin products that boost profits but have product features that may have no benefit to the customer. For this situation to persist for so long, current channels for information and advice must be failing.
4) Mortgage brokers have become 'part of the establishment', with fees and trail commissions having no evident link to customer best interests.
5) Trail commissions should be banned and clawback of broker commissions restricted. All brokers, advisors and lender employees delivering home loans to customers should have clear, legally-backed best interest obligations to their clients.
6) Recognising reward structures may still at times conflict with customer best interests. All banks should appoint a Principal Integrity Officer obliged by law to report directly to the Board on the alignment of any incentives/reward with the new customer best interest duty.
7) Merchants should be given the option of selecting the default route that is to be used for payments by dual network cards.
8) More nuance in the design of APRA's prudential measures – both in risk weightings and directions to authorised deposit-taking institutions (**ADIs**) – is essential to lessen market power and address an imbalance that has emerged in lending between business and housing.

The Government will look carefully at all the recommendations in the Productivity Commission's report, consult and consider its response together with any further matters that arise including from the Royal Commission. The Government's final response to the report will not be delivered until after the Royal Commission hands its final report to the Government, due February 2019.

DIRECTORS' REPORT

For the year ended 31 August 2018

1.4 RISK AND REGULATORY DEVELOPMENTS (CONTINUED)

Banking Executive Accountability Regime

As part of the 2017-18 Budget, the Federal Government announced that it will legislate to introduce a new BEAR. The intention of BEAR is to enhance the responsibility and accountability of banks and their directors and senior executives.

The *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017* (Cth) passed through Federal Parliament on 7 February 2018 and received its Royal Assent on 20 February 2018.

Large financial institutions need to comply with the regime from 1 July 2018, with a deferral period for commencement of the variable remuneration requirements to 1 January 2019. Small and medium sized ADIs (which includes BOQ) have an extra 12 months to comply with BEAR (1 July 2019).

Parliamentary Joint Committee on Corporations and Financial Services – Operation and effectiveness of the Franchising Code of Conduct

On 22 March 2018, the Senate referred an inquiry into the operation and effectiveness of the Franchising Code of Conduct to the Parliamentary Joint Committee for report by 30 September 2018. On 19 June 2018, the Senate extended the reporting date from 30 September 2018 to 6 December 2018.

The Committee has invited individual stories that may identify widespread issues and recommendations for reform. The Committee has powers to report to Parliament with recommendations for changes to legislation and government policy but cannot investigate or resolve individual disputes.

Australian Financial Complaints Authority (AFCA)

On 1 May 2018, the Government announced the authorisation of Australian Financial Complaints Limited to operate AFCA, and members of the inaugural AFCA Board. AFCA will be the one-stop shop external dispute resolution (**EDR**) body for disputes arising in the financial sector. The objective of AFCA is to provide free, fast and binding dispute resolution for consumers and small businesses and to increase transparency of dispute resolution practices by enabling ASIC to publish banks' internal dispute resolution data.

AFCA will commence accepting complaints from 1 November 2018. This commencement date will allow AFCA sufficient time to put in place the necessary infrastructure and staff to be ready to receive complaints. Any existing Financial Ombudsman Services (**FOS**) disputes will continue to be dealt with under the current FOS terms of reference until resolved.

Australian Bankers' Association 'Better Banking' Program

In April 2016, the Australian Bankers' Association (**ABA**) announced a six point plan to increase transparency and accountability, improve customer outcomes and build trust and confidence in banks.

This plan has expanded into the 'Better Banking' program (**Program**) with the delivery of industry-led initiatives to provide better products, better service and better culture for bank customers

The Program is well progressed and BOQ has implemented, or will be implementing, the following initiatives:

1) the recommendations from Mr Stephen Sedgwick AO's review into product based payments and commissions;
2) the revised Code of Banking Practice, incorporating the recommendations arising from the Australian Small Business and Family Enterprise Ombudsman's Small Business Loan Inquiry;
3) a Customer Advocate to support customers when things go wrong;
4) an updated Whistle-blower Policy to reflect the ABA's Guiding Principles on Improving Protections for Whistle-blowers; and
5) the ABA's Conduct Background Check Protocol to help stop poor conduct moving around the industry.

New Banking Code of Practice

On 31 July 2018, ASIC confirmed its approval to the new Banking Code of Practice. In providing this approval, ASIC has endorsed the industry's new definition of "small business" as one with:

1) An annual turnover of $10 million or less in the prior financial year;
2) Fewer than 100 full time equivalent (**FTE**); and
3) Less than $3 million total debt to all credit providers, including any undrawn amounts under existing loans, any loans being applied for, and the debt of all its related entities that are businesses.

The Banking Code will be enforceable as part of a customer's contract with their bank. This is a strong commitment to ethical and transparent behaviour, responsible lending and greater financial protections for customers.

New additions to the Banking Code include:

- More information about changes to customers' accounts and greater assistance to vulnerable customers;
- Simplified small business loan contracts with fewer conditions for more than 92 per cent of businesses;
- New cooling off periods for guarantors; and
- An independent compliance committee with specific small business and agribusiness expertise to investigate breaches of the Banking Code.

Banks will be required to fully implement the new Banking Code by 1 July 2019.

DIRECTORS' REPORT

For the year ended 31 August 2018

1.4 RISK AND REGULATORY DEVELOPMENTS (CONTINUED)

Consumer Data Right Bill and Open Banking

The Government is consulting on exposure draft legislation to implement the Consumer Data Right (**CDR**). The CDR will provide individuals and businesses with a right to efficiently and conveniently access specified data in relation to them held by businesses; and authorise secure access to this data by trusted and accredited third parties. The CDR will also require businesses (like BOQ) to provide public access to information on specified products they have on offer.

CDR is designed to give customers more control over their information, leading to more choice in where they take their business, or more convenience in managing their money. The Government has committed to applying the CDR in the banking, energy and telecommunications sector. For the banking sector, this is referred to as "Open Banking" and will be the first sector to apply the CDR.

The CDR is intended to reduce the barriers that currently prevent customers from switching between banks. Banks will be required to provide open access to data on product terms and conditions, transaction use, and will have the ability to direct that the data be shared with other service providers (banks and non-banks).

Introduction of the Modern Slavery Bill 2018

On 28 June 2018, the Government introduced the *Modern Slavery Bill 2018*. This Bill requires certain organisations based in, or operating in Australia, which have an annual consolidated revenue of more than $100 million (defined as 'reporting entities'), to annually report on the risks of modern slavery in their operations and supply chains, and to address those risks. Organisations that do not meet the definition of 'reporting entities' may voluntarily comply with the regime by giving written notice to the Minister.

The annual statements will need to address mandatory criteria set out in the Bill, including the entity's key modern slavery risks and describing their actions to address those risks. These criteria will provide certainty for businesses about how to report and ensure statements can be easily compared.

Net Stable Funding Ratio (NSFR)

On 20 December 2016, APRA released the final revised Prudential Standard APS 210 *Liquidity* (**APS 210**) and Prudential Practice Guide APG 210 *Liquidity* (**APG 210**) which incorporates, among other things, the NSFR requirements for some ADIs.

APRA's objective in implementing the NSFR in Australia for ADIs that are subject to the Liquidity Coverage Ratio (**LCR**), implemented in 2015, is to strengthen the funding and liquidity resilience of these ADIs.

The NSFR encourages ADIs to fund their activities with more stable sources of funding on an ongoing basis, and thereby promotes greater balance sheet resilience. In particular, the NSFR should lead to reduced reliance on less-stable sources of funding, such as short-term wholesale funding, that proved problematic during the global financial crisis. The new APS 210 commenced on 1 January 2018.

Basel Committee on Banking Supervision - Basel III reforms

On 7 December 2017, the Basel Committee on Banking Supervision (**Basel Committee**) published the finalisation of its Basel III framework. A key objective of the revisions is to reduce excessive variability of risk-weighted assets (**RWAs**) across institutions. At the peak of the global financial crises, a wide range of stakeholders – including academics, analysts and market participants – lost faith in banks' reported risk-weighted capital ratios. The Committee's own empirical analyses highlighted a worrying degree of variability in the calculation of RWAs by banks. The finalised Basel III reforms include revisions to the standardised approach to credit risk, as well as revisions to the internal ratings-based (**IRB**) approach to credit risk. The reforms have an implementation date of 1 January 2022 and include transitional arrangements to implement the new standards to ensure an orderly and timely implementation by jurisdictions and adjustment by banks.

APRA's proposed revisions to the capital framework for ADIs

On 14 February 2018, APRA released two discussion papers for consultation with ADIs on proposed revisions to the capital framework. The papers include proposed revisions to the capital framework resulting from the Basel Committee finalising the Basel III reforms in December 2017, as well as other changes to better align the framework to risks, including in relation to housing lending. APRA also released a discussion paper on implementation of a leverage ratio requirement. APRA stated that it is not seeking to increase capital requirements beyond what was already announced in July 2017 as part of the 'unquestionably strong' benchmarks. The key proposed changes to the capital framework include:

- lower risk weights for low Loan to Value Ratio (**LVR**) mortgage loans, and higher risk weights for interest-only loans and loans for investment purposes, than apply under APRA's current framework;
- amendments to the treatment of exposures to small- to medium-sized enterprises (**SME**), including those secured by residential property under the standardised and IRB approaches;
- constraints on IRB ADIs' use of their own parameter estimates for particular exposures, and an overall floor on risk weighted assets relative to the standardised approach; and
- a single replacement methodology for the current advanced and standardised approaches to operational risk.

The paper also outlines a proposal to simplify the capital framework for small ADIs, which is intended to reduce regulatory burden without compromising prudential soundness. Given APRA's expectation that ADIs will meet its unquestionably strong capital benchmarks by 1 January 2020, APRA continues to propose an implementation date of 1 January 2021 for all revised measures.

DIRECTORS' REPORT

For the year ended 31 August 2018

1.4 RISK AND REGULATORY DEVELOPMENTS (CONTINUED)

APRA's plans to remove investor lending benchmark and embed better practices

On 26 April 2018, APRA announced plans to remove the investor loan growth benchmark and replace it with more permanent measures to strengthen lending standards. The 10 per cent benchmark on investor loan growth was a temporary measure, introduced in 2014 as part of a range of actions to reduce higher risk lending and improve practices. APRA noted that in recent years, ADIs have taken steps to improve the quality of lending, raise standards and increase capital resilience. APRA wrote to ADIs to advise that it was prepared to remove the investor growth benchmark, where the board of an ADI is able to provide assurance on the strength of their lending standards. In summary, for the 10 per cent benchmark to no longer apply, Boards will be expected to confirm that:

- lending has been below the investor loan growth benchmark for at least the past six months;
- lending policies meet APRA's guidance on serviceability; and
- lending practices will be strengthened where necessary.

For ADIs that do not provide the required commitments to APRA, the investor loan growth benchmark will continue to apply.

As part of these measures, APRA stated that it also expects ADIs to develop internal portfolio limits on the proportion of new lending at very high debt-to-income levels, and policy limits on maximum debt-to-income levels for individual borrowers.

APRA's proposed changes to make the capital framework for ADIs more transparent, comparable and flexible

On 14 August 2018, APRA released a discussion paper which outlines two general approaches designed to aid ADIs in representing and communicating their capital strength:

- Under one approach, ADIs would continue using existing definitions of capital and risk-weighted assets, but APRA would develop a methodology allowing them to improve the credibility and robustness of internationally comparable capital ratio disclosures; or
- Under a second approach, APRA would change the way ADIs calculate capital ratios to instead use more internationally harmonised definitions of capital and risk-weighted assets. To maintain the strength and risk-sensitivity of the capital framework, there would need to be corresponding increases in minimum ratio and/or capital buffer requirements.

APRA stated that it is open to considering these approaches independently or in combination, or retaining its current methodology, and is seeking industry feedback on whether the benefits of the suggested approaches outweigh the regulatory burden and associated increase in complexity.

Separately, the discussion paper proposes measures to make the capital framework more flexible in times of stress, including by increasing the size of regulatory capital buffers relative to minimum regulatory capital requirements. APRA reiterated that the proposals in this paper are not intended to change the quantum or allocation of capital.

APRA intends to consult on draft revised prudential standards incorporating the outcome of this consultation in 2019. Further, APRA stated that it intends to progress any aspects set out in this Discussion Paper that it proposes to adopt in parallel with the revisions to the ADI capital framework outlined in the February 2018 Discussion Paper.

AREAS OF INCREASED RISK FOCUS

Ethics & business conduct

The conduct of the financial services industry has been under increasing scrutiny with a range of regulatory investigations impacting not just the brand and reputation of the companies involved, but also heightening attention across the broader industry. Regardless of the outcome, these investigations incur a cost and a loss of value, so it's understandable that stakeholders want greater clarity on how ethics and business conduct are managed.

While it is not possible to control the actions of every individual within a company, strong management controls and a culture that values integrity go a long way in minimising the risk of adverse employee behaviour.

BOQ's values, together with its range of policies and frameworks are the foundational elements for how its people behave and are accountable for the decisions they make. BOQ is committed to ensuring an ethical and accountable behaviour across all staff within the Group and its strategic partners, which is supported through:

- Ongoing education of all staff in ethics and values that is being constantly reviewed and refreshed to ensure currency and focus;
- Dedicated Ethics & Security Committee made up of senior executive and management who both review and make decisions on actual or alleged misconduct issues in addition to analysing potential trends for future risks to the group;
- Appointment of a customer advocate who champions the voice of the customer and acts as the key internal arbitrator with a continual focus on the best interests of the customer and minimising the likelihood of future complaints or incidents;

DIRECTORS' REPORT

For the year ended 31 August 2018

1.4 RISK AND REGULATORY DEVELOPMENTS (CONTINUED)

Ethics & business conduct (continued)

- Active participation in an independent Industry Risk Culture Survey that benchmarks BOQ against peers around attitudes to risk and governance. The outcomes from the survey are then used to assist the ongoing development of a risk and culture program across the group; and
- The reporting and monitoring of risk culture has continued to mature, with the ongoing enhancement of risk culture dashboards and the rollout of divisional operational risk committees that support good governance of both risk and culture.

Cyber & business resilience

Risk events that result from the external environment continue to be a major focus for all financial institutions and third parties that support us. The increase in cyber-related attacks, environmental and weather events, pandemics or systems failures can significantly disrupt the systems and processes that enable us to protect our staff, customers and shareholders.

Across BOQ both cyber and business continuity are regarded as material business risks that are activity managed and monitored across the Group. Critical to BOQ's investment in cyber and business resilience is its:

- Specialised and highly-experienced staff;
- Ongoing simplification of systems to reduce the point of potential compromise;
- Development of policies, processes and controls that adopt international and industry standards and best practices;
- Strategic partners, through education and the assessment of their systems and processes that ensure they continue to maintain the same level of resilience and security as BOQ; and
- Ongoing development of business continuity plans and responses through scenario based testing of systems and processes.

Climate change

The risks and opportunities of climate change are becoming increasingly relevant to most businesses in the Australian economy. Through the Paris Agreement of 2015, governments around the world agreed to take action to limit global warming to less than two degrees celsius above pre-industrial levels and as close to 1.5 degree celsius as possible and to transition to net zero emissions by 2050. As a result, the Australian Government has set a target to reduce emissions by 26-28 per cent below 2005 levels by 2030. The transition to a low carbon economy and the ongoing effects of climate change will impact the long-term prosperity of Australia's economy, environment and society. Therefore, businesses are increasing the level of disclosure around how the risks and opportunities of climate change are relevant to their particular business.

In 2017, the Financial Stability Board's Taskforce on Climate-related Financial Disclosures (**TCFD**) published its final report which set out its recommendations for helping businesses disclose climate-related financial information. The TCFD report establishes recommendations for disclosing clear, comparable and consistent information about the risks and opportunities presented by climate change, and provides decision-useful information to lenders, insurers, and investors. The recommendations are structured around four thematic areas that represent core elements of how organizations operate: governance, strategy, risk management, and metrics and targets. BOQ plans to enhance its approach to and disclosures of climate-related risks and opportunities in the year ahead in line with the TCFD recommendations. An overview of the current approach is provided below.

Governance

Management of risk, including climate-related risk, is ultimately overseen by the BOQ Board and Risk Committee. BOQ has an integrated Risk Management Framework in place to identify, assess, manage and report risks on a consistent and reliable basis. This framework has been developed to accord with the tolerance levels set out in the BOQ Risk Appetite Statement. A number of risks have been identified as material business risks for BOQ under this Risk Management Framework, including credit risk and reputation risk. Climate risk forms part of these broader risk categories and is therefore currently assessed indirectly within these broader risks.

The Board delegates day to day management of the business to the management team. This includes identification of opportunities for the business (including climate-related opportunities) as well as management of risk within the risk appetite that has been approved by the Board. The management team utilises the Executive Committee, Business Performance Committee and Executive Credit Committee and various credit policies to assess potential implications to credit risk from climate-related factors.

DIRECTORS' REPORT

For the year ended 31 August 2018

1.4 RISK AND REGULATORY DEVELOPMENTS (CONTINUED)

Strategy

Risks

Although not currently identified as material risks in the context of BOQ's overall Risk Management Framework, the following are the potential climate-related risks which are currently considered to be most relevant to BOQ:

- Transition risks including reduced income for businesses or individuals currently reliant on income from potentially unsustainable sources, changing customer behaviour, enhanced reporting obligations and increased stakeholder concern.
- Physical risks including decline in value of assets due to climate-related weather events or rising sea levels.

These risks would primarily impact BOQ through reduced ability of customers to repay their loans and/or reduced asset values, which could ultimately lead to write-off in asset values and decline in earnings for BOQ.

Opportunities

The following are the key climate-related opportunities which are most relevant to BOQ:

- Funding investment in renewable energy.
- Developing finance solutions to meet the needs of businesses and consumers in a lower-carbon economy.

These opportunities would primarily impact BOQ through increased revenues. There may also be some opportunities to achieve lower costs through pursuit of more energy efficient operations.

Risk management

BOQ's process for identifying, assessing and managing risks is integrated into its overall Risk Management Framework. Climate risk is incorporated into assessment of credit risk and reputation risk, which have been identified as material risks under BOQ's Risk Management Framework. The management team utilises the Executive Credit Committee and credit policies such as the Ecological Care and Sustainability Lending Policy to assess potential implications to credit risk from climate-related factors. Credit risk is assessed at a portfolio level as well as at an individual credit exposure level on a case-by-case basis. On an individual credit level this would include consideration of future cash flows available to service debt as well as valuations of assets taken as security. Property valuations take into account factors such as flooding and environmental risk in estimating the value of properties, which BOQ uses as a basis for determining an appropriate level of lending to be extended relative to that property value. In addition, BOQ's loan agreements require customers to maintain comprehensive insurance for any property provided as security for a loan. Where flood is identified as a potential risk in the valuation, flood cover is required to be included in the insurance policy. This provides a level of protection to the value of security in the event that there is damage or destruction caused by extreme weather events.

Reputation risk is managed in line with BOQ's Reputation Risk Management Policy, through monitoring of both the internal and external environment and regular stakeholder engagement with customers, investors, suppliers, employees, government, media, regulators and community partners. This includes a combination of structured engagement through surveys, regular reporting and industry forums as well as direct feedback from customers and staff or indirect information gathering and monitoring of issues that may be or may become relevant to BOQ.

Metrics and targets

BOQ is in the process of developing metrics that would be most relevant to monitor specific climate-related risks for the business. A key metric that is currently reported is the dollar value and proportion of the loan portfolio that has been extended to businesses who are directly involved in fossil fuel mining ($32 million or <0.1 per cent of BOQ's total loan portfolio as at 31 August 2018). This is a metric that will reduce to zero by the end of 2023 as BOQ has committed to no further financing of equipment directly involved in the extraction of fossil fuels. BOQ has no exposure to coal-fired power generators and has no appetite for lending to this sector. For BOQ's housing loan portfolio, lending identified in mining-dependent regions is subject to a separate policy and risk appetite. Monthly internal reporting on exposures and arrears levels is used to monitor risk in these locations.

As part of the annual portfolio stress testing simulation, in 2018 BOQ has included a weather-related event as a scenario to be tested. The results of this stress test will further assist in understanding risk in the portfolio.

Looking ahead

In FY19, BOQ plans to enhance disclosures aligned to the TCFD framework, which provide additional information on the risk and opportunities of climate change for BOQ. As part of this, consideration will be given to scenario analysis that would be most appropriate for BOQ. There are also a number of renewable energy financing initiatives being explored within the business for which progress is expected to be reported on in FY19.

DIRECTORS' REPORT

For the year ended 31 August 2018

2. GROUP PERFORMANCE ANALYSIS

2.1 INCOME STATEMENT AND KEY METRICS

	Year End Performance			Half Year Performance		
$ million	**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
Net Interest Income	965	926	4%	490	475	3%
Non-Interest Income	145	175	(17%)	70	75	(7%)
Total Income	1,110	1,101	1%	560	550	2%
Operating Expenses	(527)	(513)	3%	(265)	(262)	1%
Underlying Profit	583	588	(1%)	295	288	2%
Loan Impairment Expense	(41)	(48)	(15%)	(19)	(22)	(14%)
Profit before Tax	542	540	–	276	266	4%
Income Tax Expense	(170)	(162)	5%	(86)	(84)	2%
Cash Earnings after Tax	372	378	(2%)	190	182	4%
Statutory Net Profit after Tax [1]	336	352	(5%)	162	174	(7%)

[1] Refer to Section 5.1 of the Operating and Financial Review Appendices for the reconciliation of Statutory Profit to Cash Earnings.

		Year End Performance			Half Year Performance		
Key Metrics		**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
SHAREHOLDER RETURNS							
Share Price	($)	11.49	12.59	(9%)	11.49	12.63	(9%)
Market Capitalisation	($ million)	4,565	4,932	(7%)	4,565	4,958	(8%)
Dividends per ordinary share (fully franked)	(cents)	76	76	–	38	38	–
Special dividend per ordinary share (fully franked)	(cents)	–	8	n/a	–	–	n/a
CASH EARNINGS BASIS							
Basic Earnings per Share (**EPS**)	(cents)	94.7	97.6	(3%)	48.2	46.5	4%
Diluted EPS	(cents)	89.3	93.9	(5%)	45.2	44.5	2%
Dividend payout ratio	(%)	80.7	78.3	240bps	79.5	82.0	(250bps)
STATUTORY BASIS							
Basic EPS	(cents)	85.5	90.9	(6%)	40.9	44.6	(8%)
Diluted EPS	(cents)	81.2	87.8	(8%)	38.8	42.7	(9%)
Dividend payout ratio	(%)	89.3	84.1	520bps	93.2	85.7	750bps

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For the year ended 31 August 2018

2.1 INCOME STATEMENT AND KEY METRICS (CONTINUED)

		Year End Performance			Half Year Performance		
Key Metrics		**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
PROFITABILITY AND EFFICIENCY MEASURES							
Cash Earnings basis							
Net Profit After Tax	($ million)	372	378	(2%)	190	182	4%
Underlying Profit [1]	($ million)	583	588	(1%)	295	288	2%
NIM [2]	(%)	1.98	1.93	5bps	1.98	1.97	1bp
CTI	(%)	47.5	46.6	90bps	47.3	47.6	(30bps)
Loan Impairment Expense to Gross Loans and Advances (**GLA**)	(bps)	9	11	(2bps)	8	10	(2bps)
ROE	(%)	9.9	10.4	(50bps)	10.0	9.9	10bps
ROTE [3]	(%)	12.9	13.7	(80bps)	13.0	12.9	10bps
STATUTORY BASIS							
Net Profit After Tax	($ million)	336	352	(5%)	162	174	(7%)
Underlying Profit [1]	($ million)	534	555	(4%)	256	278	(8%)
NIM [2]	(%)	1.98	1.93	5bps	1.98	1.97	1bp
CTI	(%)	52.4	49.6	280bps	54.8	49.9	490bps
Loan Impairment Expense to GLA	(bps)	9	11	(2bps)	8	10	(2bps)
ROE	(%)	8.9	9.7	(80bps)	8.5	9.5	(100bps)
ROTE [3]	(%)	11.6	12.7	(110bps)	11.1	12.4	(130bps)
ASSET QUALITY							
30 days past due (**dpd**) Arrears	($ million)	469	470	-	469	493	(5%)
90dpd Arrears	($ million)	260	257	1%	260	237	10%
Impaired Assets	($ million)	164	192	(15%)	164	173	(5%)
Specific Provisions to Impaired Assets	(%)	52.4	55.1	(270bps)	52.4	57.6	(520bps)
Collective Provisions to Risk Weighted Assets (**RWA**)	(%)	0.39	0.42	(3bps)	0.39	0.42	(3bps)
CAPITAL							
CET1 Ratio	(%)	9.31	9.39	(8bps)	9.31	9.42	(11bps)
Total Capital Adequacy Ratio	(%)	12.76	12.37	39bps	12.76	12.78	(2bps)
RWA	($ million)	29,669	28,644	4%	29,669	28,859	3%

(1) Profit before loan impairment expense and tax.

(2) NIM net of offset accounts.

(3) Based on after tax earnings applied to average shareholders' equity (excluding preference shares and treasury shares) less goodwill and identifiable intangible assets (customer related intangibles/brands and computer software).

DIRECTORS' REPORT

For the year ended 31 August 2018

2.2 NET INTEREST INCOME

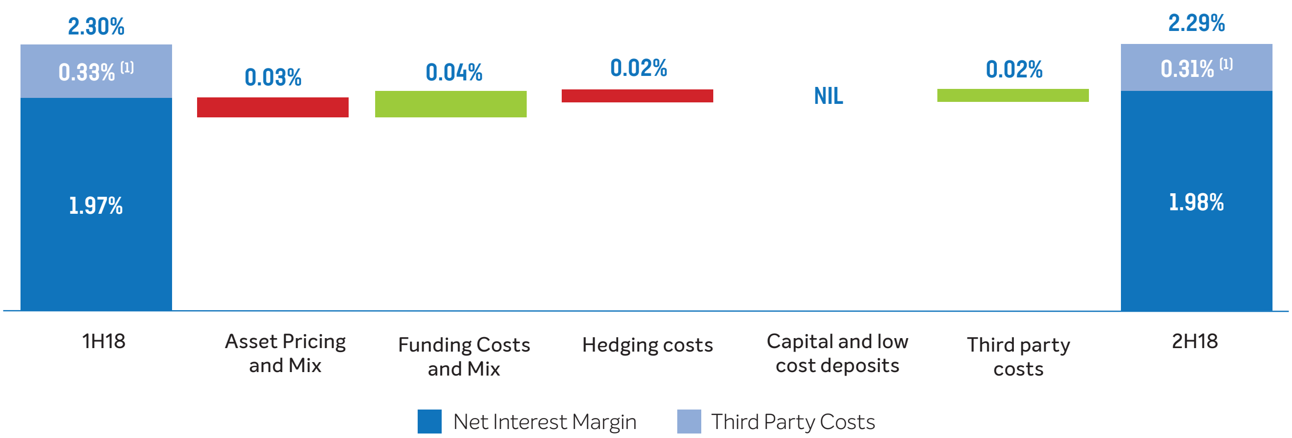
	Year End Performance			Half Year Performance		
$ million	**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
Net Interest Income	**965**	926	4%	**490**	475	3%
Average Interest Earning Assets	**48,818**	47,891	2%	**49,159**	48,519	1%
Net Interest Margin	**1.98%**	1.93%	5bps	**1.98%**	1.97%	1bp

Net interest income increased by four per cent or $39 million from FY17. This was driven by a five basis point improvement in NIM over FY18 combined with a two per cent increase in average interest earnings assets. The margin improvement was primarily due to an improvement in funding costs.

2H18 performance saw net interest income increasing by three per cent. This was due to an increase in average interest earning assets over 2H18 of one per cent, a one basis point increase in net interest margin and a two per cent increase due to a higher number of days in 2H18 than 1H18.

NIM during 2H18 benefitted two basis points due to an extension in the behavioural term of the housing portfolio increasing the period over which origination costs were amortised. Underlying NIM was down one basis point driven by ongoing front to back competition for lending and the impact of increased basis costs outweighing the benefit from term deposit / spread reduction and the repricing actions undertaken in July 2018.

Net Interest Margin - February 2018 to August 2018



(1) Third party costs largely represent commissions to Owner Managers and brokers.

Underlying movements within the NIM between 1H18 and 2H18 included the following:

Asset Pricing and Mix: Asset pricing and mix (excluding the impact of basis) decreased by three basis points. Lower rates being offered on new loans, the increased competition for owner occupied principal and interest housing loans, reduced interest only lending flows and repricing to retain existing customers, had a five basis point contractionary NIM effect. This was partially mitigated by loan repricing actions in July 2018. Lower liquidity levels in 2H18 contributed to a one basis point positive impact which was offset by a lower yielding liquids mix.

Funding Costs and Mix: Funding cost benefits increased NIM by four basis points. The Bank took the opportunity early in the calendar year to take advantage of favourable wholesale funding conditions to pre-fund 2H18 growth. The increased sophistication in pricing of the Bank's term deposit portfolios combined with a change in mix allowed the Bank to extract funding cost benefits.

Hedging costs: The impact of basis increased in 2H18 largely with portfolio spreads increasing from an average of 23 basis points to 34 basis points compared to 1H18. This reduced NIM by two basis points in 2H18. This is likely to represent an ongoing headwind in the first half of FY19 if basis remains at current levels.

Capital and Low Cost Deposits: The lower interest rate environment reduced the returns on BOQ's $4.2 billion replicating portfolio (covering BOQ's capital and low cost deposits) resulting in a one basis point reduction in NIM over 2H18. This was offset by an increase in non-invested capital due to a higher average three month BBSW rate.

Third party costs: Third party costs decreased two basis points in 2H18, largely a result of a one-off benefit arising from the extension of the behavioural weighted average life of the home loan portfolio reflecting lower customer attrition rates. This extended the period over which mortgage origination costs are amortised and contributed two basis points.

DIRECTORS' REPORT

For the year ended 31 August 2018

2.3 NON-INTEREST INCOME

$ million	Year End Performance Aug-18	Aug-17	Aug-18 vs Aug-17	Half Year Performance Aug-18	Feb-18	Aug-18 vs Feb-18
Banking Income	93	96	(3%)	47	46	2%
Insurance Income	19	21	(10%)	9	10	(10%)
Other Income	32	51	(37%)	15	17	(12%)
Trading Income	1	7	(86%)	(1)	2	(150%)
Total Non-Interest Income (1)	145	175	(17%)	70	75	(7%)

(1) Refer to Section 5.1 of the Operating and Financial Review Appendices (b) Non-Cash Earnings Reconciling Items for a reconciliation of Statutory Non-Interest Income to Cash Non-Interest Income.

Non-interest income of $145 million is down 17 per cent on FY17 ($14 million or nine per cent including the disposal of a vendor finance entity in FY17).

The industry-wide decline in income from interchange fees and lower merchant fees contributed to the three per cent reduction in banking income in FY18 combined with ongoing trends in customers choosing low or no fee banking products. There was some benefits in increased foreign exchange transactions with customers, particularly in 2H18, resulting in a two per cent increase in banking income over 1H18.

Other income decreased $19 million during FY18 and was 12 per cent lower in 2H18 versus 1H18. FY17 included a one-off benefit from the disposal of a vendor finance entity after the vendor partner exercised its option. This was combined with lower equipment sales income in the leasing entities in FY18.

The VMA white label product distribution business contributed $6 million to FY18, an increase of $1 million over FY17. This result was attributable to continued growth across its product lines particularly above system growth rates in credit card receivables during FY18.

The trading income contribution was down on FY17 as the Group held lower levels of traded liquidity instruments and 2H18 was impacted by elevated Cash/Bills basis spread.

The St Andrew's Insurance contribution is discussed in detail in Section 2.4 below.

2.4 INSURANCE OVERVIEW

$ million	Year End Performance Aug-18	Aug-17	Aug-18 vs Aug-17	Half Year Performance Aug-18	Feb-18	Aug-18 vs Feb-18
Gross Written Premium (net of refunds)	72	70	3%	35	37	(5%)
Net Earned Premium	66	68	(3%)	32	34	(6%)
Underwriting Result	15	17	(12%)	6	9	(33%)
Other Insurance Income	3	3	-	2	1	100%
Total Income	18	20	(10%)	8	10	(20%)
Consolidation Adjustment	1	1	-	1	-	-
Group Insurance Result	19	21	(10%)	9	10	(10%)

St Andrew's Insurance contributed $19 million or 13 per cent to Non-Interest Income, a $2 million or 10 per cent reduction from FY17.

Gross Written Premiums increased three per cent largely due to growth in wholesale partnerships, although Net Earned Premium did reduce due to lower consumer credit insurance sales levels and higher levels of reinsurance associated with the wholesale partnerships.

The Underwriting result decreased by $2 million to $15 million, with lower claims partly offsetting the decrease in net earned premium. The unemployment claims experience has improved notably in FY18 compared to FY17.

Whilst St Andrew's contribution has been steady over 1H18 and 2H18 across its existing lines of business, increased regulatory scrutiny continues to contribute to an uncertain performance outlook for the insurance sector.

DIRECTORS' REPORT

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2.5 OPERATING EXPENSES

	Year End Performance			Half Year Performance		
$ million	Aug-18	Aug-17	Aug-18 vs Aug-17	Aug-18	Feb-18	Aug-18 vs Feb-18
Employee Expenses	263	257	2%	133	130	2%
Occupancy Expenses	44	42	5%	22	22	-
General Expenses	81	85	(5%)	40	41	(2%)
IT Expenses	119	108	10%	60	59	2%
Other Expenses	20	21	(5%)	10	10	-
Total Operating Expenses (1) (2)	527	513	3%	265	262	1%
CTI	47.5%	46.6%	90bps	47.3%	47.6%	(30bps)
Number of employees (FTE) (1)	2,039	2,031	-	2,039	2,046	-

(1) FTE numbers and Operating Expenses exclude VMA third party costs as the net result is included in Non-Interest Income. Expenses relating to the VMA mortgage offering have been included in the above table.

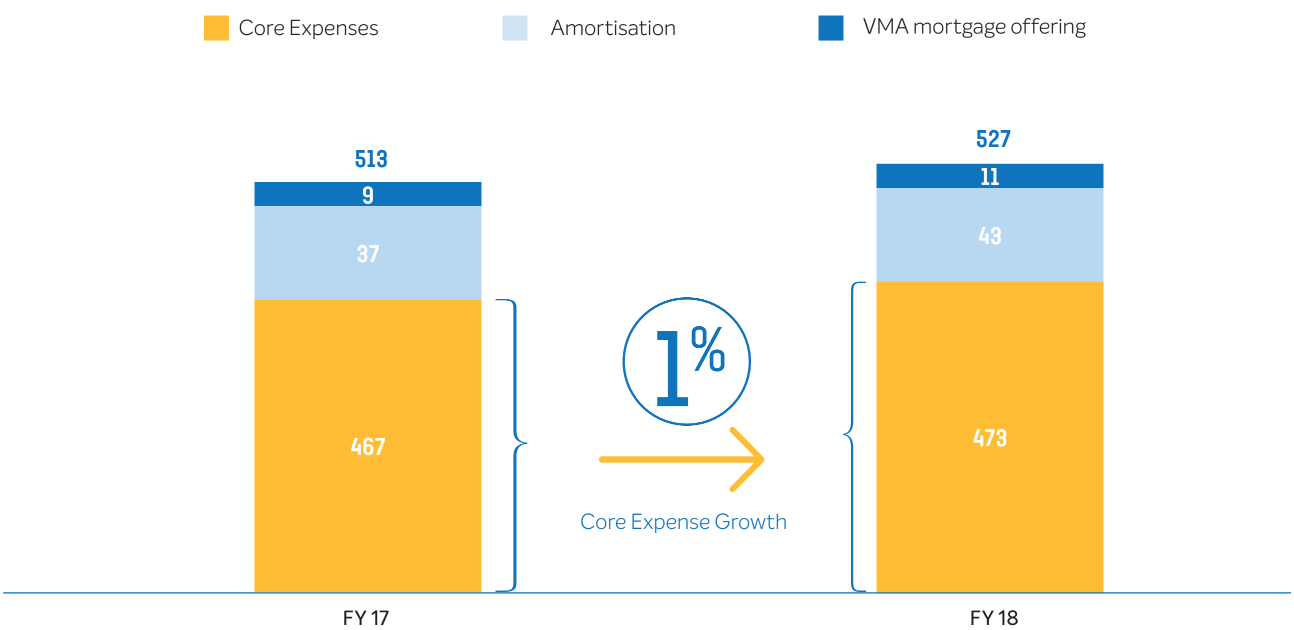
(2) Refer to Section 5.1 of the Operating and Financial Review Appendices (B) Non-Cash Earnings Reconciling Items for a reconciliation of Statutory Operating Expenses to Cash Operating Expense.

Operating expenses exclude expenses relating to the white label product distribution activities of VMA, where the net result is consolidated in non-interest income for the determination of cash earnings.

Operating expenses increased three per cent on FY17 to $527 million. On an underlying basis (per graph below), core operating expenses increased by one per cent compared to FY17. IT software amortisation expense associated with the Group's transformation agenda (refer Section 2.6 Capitalised Investment Expenditure) resulted in an additional $6 million being incurred in FY18.

A number of efficiency initiatives delivered in FY17 and FY18 have resulted in a reduction in the general expense profile in the provision of customer communications and increased digitisation within branches. This was achieved through leverage of existing partners' enhanced services with contemporary pricing. Increased investment in both strategic initiatives and regulatory compliance changes has resulted in an uplift to IT expenses above the $6 million increase in software amortisation.

Operating expenses analysis ($m)



DIRECTORS' REPORT

For the year ended 31 August 2018

2.6 CAPITALISED INVESTMENT EXPENDITURE

The Group's transformation program requires a number of significant investments to support BOQ's strategy.

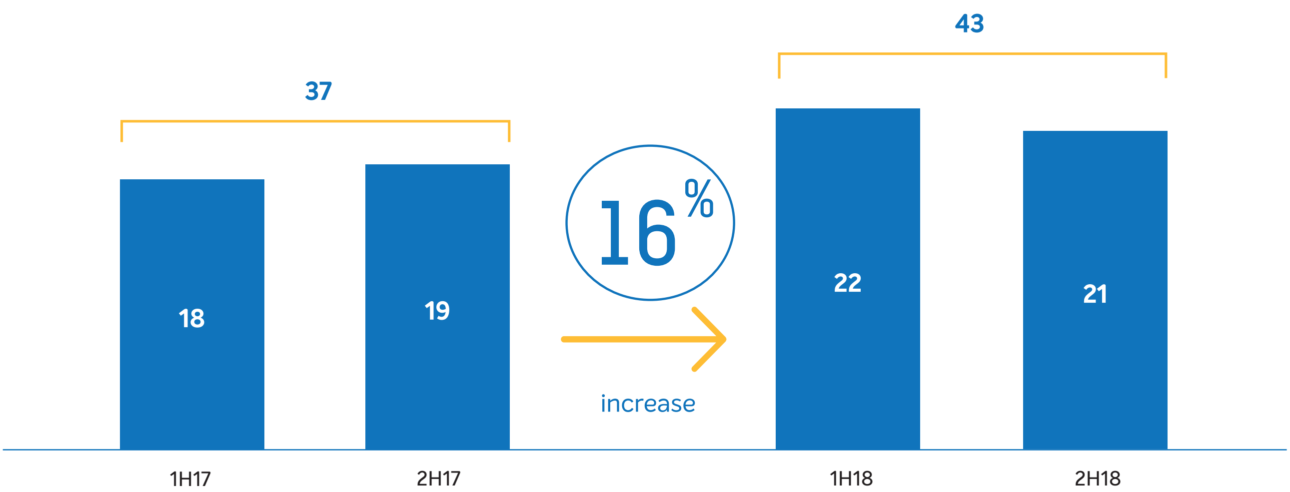
Investment continued into 2H18 across key programs of work including the New Payments Platform (**NPP**), a treasury & market risk systems upgrade, as well as developing capability for financial markets digital customer offerings and foreign currency accounts. These investments extend BOQ's digital banking capabilities, increase the Bank's ability to expand its product base and improve operational efficiency, whilst continuing to strengthen the Bank's risk management and control environment.

Infrastructure modernisation is a key pillar of the BOQ 2020 Technology Strategy, focused on improving capabilities, as well as removing technical complexity, and obsolescence risks.

Investment in assets under construction has accelerated in 2018, a direct result of the value in the key programs of work in progress, in addition to a general increase in the volume of assets under construction. The rate of growth in the carrying value of IT intangible assets has slowed over time reflecting an increasing annual amortisation charge. The software intangible asset balance was reduced by a one time expense of $16 million in 2H18, resulting from a policy change to increase minimum threshold for the capitalisation of intangible assets. In addition, a reassessment of the remaining useful life of intangible assets likely to be impacted by a roadmap of investment over the next three financial years was undertaken.

This approach considered intangible assets that were likely to be impacted with the deployment of additional capital across financial years 2019 and 2020 focused on delivering a contemporary digital banking experience, end-to-end lending process digitisation and enhanced customer omni-channel experiences.

IT intangible assets amortisation profile ($m)

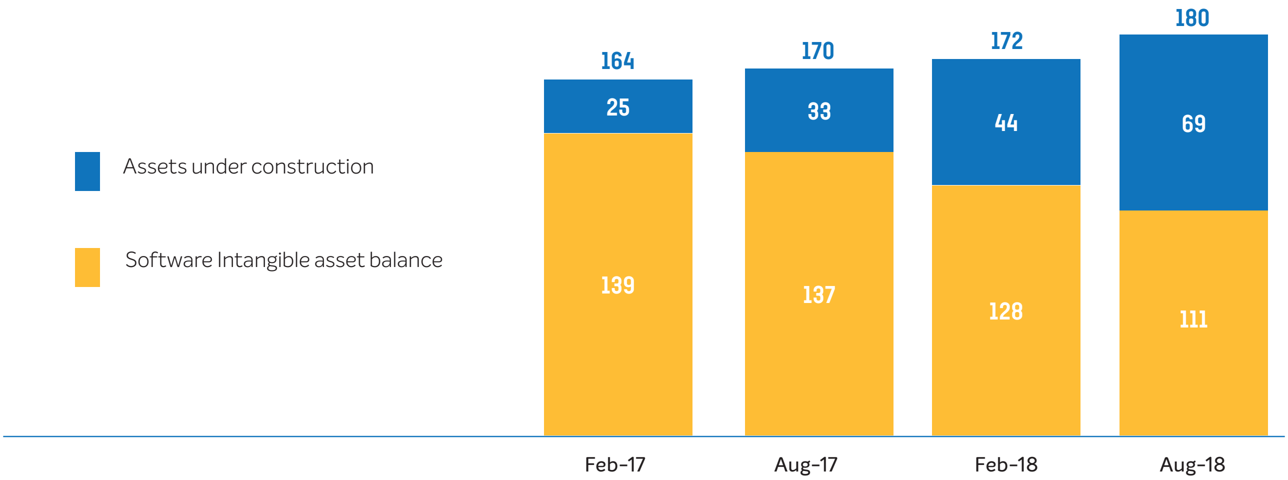


DIRECTORS' REPORT

For the year ended 31 August 2018

2.6 CAPITALISED INVESTMENT EXPENDITURE (CONTINUED)

Carrying value of IT intangible assets ($m)



2.7 LENDING

Lending growth improved in FY18. This was led by strong new business acquisition across the niche customer segments in BOQ Business and BOQ Finance with continued momentum in the VMA housing portfolio and improved retention across the BOQ branch network. BOQ balanced margin and asset quality during the year, with a focus on low cost deposit acquisition.

BOQ continues to maintain prudent credit standards, along with robust origination validation requirements in a market which is characterised by inconsistent application of evolving regulatory guidelines. The lending portfolio has maintained very low levels of arrears, an improving loan impairment expense profile and declining impaired asset balances reflecting adoption of prudent credit risk settings in prior years (refer Section 3.1 Asset Quality).

	As at				
$ million	Aug-18	Feb-18	Aug-17	Aug-18 vs Feb-18 (1)	Aug-18 vs Aug-17
Housing Lending	28,007	28,468	27,850	(3%)	1%
Housing Lending – APS 120 qualifying securitisation (2)	2,499	1,767	2,003	82%	25%
	30,506	30,235	29,853	2%	2%
Commercial Lending	9,881	9,589	9,312	6%	6%
BOQ Finance	4,595	4,360	4,345	11%	6%
Consumer	297	304	307	(5%)	(3%)
Gross Loans and Advances	45,279	44,488	43,817	4%	3%
Specific and Collective Provisions	(201)	(219)	(227)	(16%)	(11%)
Net Loans and Advances	45,078	44,269	43,590	4%	3%

(1) Growth rates have been annualised.
(2) Securitised loans subject to capital relief under APRA Prudential Standard APS 120 *Securitisation* (**APS 120**).

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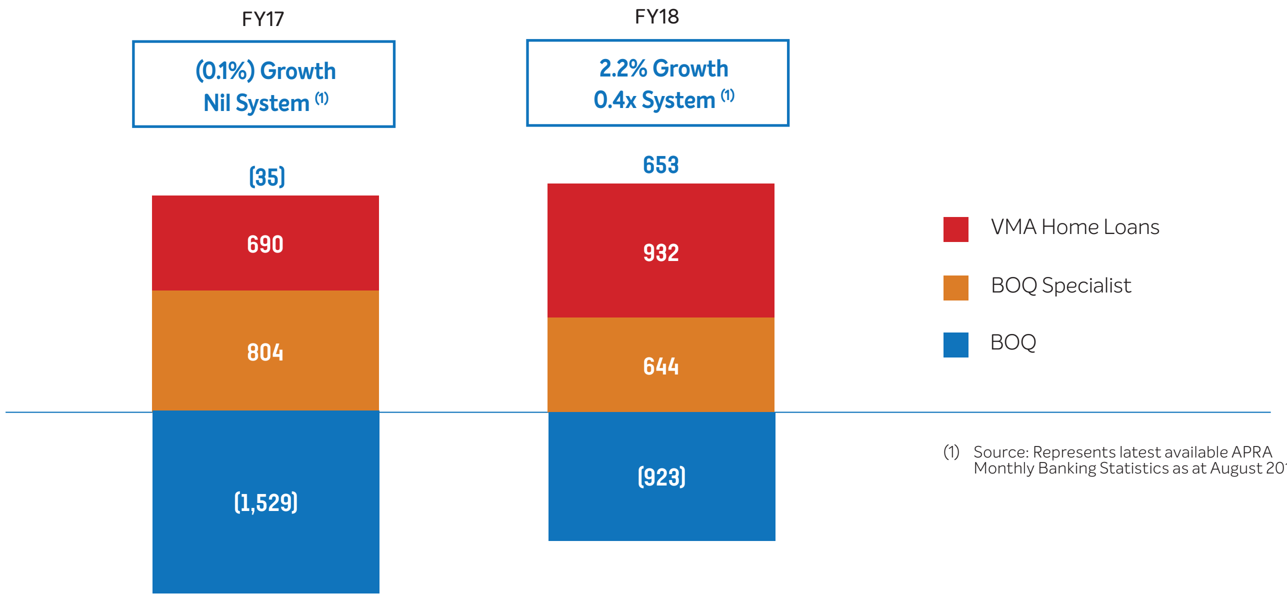
2.7 LENDING (CONTINUED)

Growth in Gross Loans & Advances

Growth in Housing ($m)



(1) Source: Represents latest available APRA Monthly Banking Statistics as at August 2018

Housing Lending

Total housing lending growth improved $688 million year on year in a market that is increasingly competitive. BOQ maintained prudent credit risk settings and took a conservative approach to regulatory compliance, moving earlier to adopt enhanced servicing, validation and responsible lending practices than many of its competitors. BOQ's relative under-representation in higher growth markets such as Sydney and Melbourne also constrained growth rates. BOQ's focus on building service and fulfillment capability through the retail lending origination platform and centralised mortgage processing capabilities, is delivering efficiencies and an improved customer experience.

The VMA mortgage offering is in its second year of operation and continued its growth profile over 2018 with over $1 billion in settlements taking the portfolio to $1.6 billion through its network of over 3,300 accredited brokers. The '*Reward Me*' mortgage product has resonated with a new customer demographic aligned to the Virgin brand, predominantly younger and geographically diversified from the traditional BOQ customer base. This year, VMA also introduced a direct online channel.

The BOQ Specialist mortgage offering to its niche, professional client base grew by 15 per cent in FY18. The portfolio had lower growth compared to prior years due to the maturing portfolio, however it continues to deliver solid above system growth. Momentum continued through a focus on building relationships with professionals in the early stages of their careers starting at university. The diversity offered through this portfolio in geography, profession and age, improves the overall risk profile of the housing lending portfolio in BOQ. It also creates future opportunities to meet the commercial lending needs of the targeted health professional market segments well into the future stages of career progression.

BOQ's branch network improved its housing performance, particularly across the Owner Manager channel, through improved retention rates whilst maintaining strong credit standards. BOQ has rebalanced the remuneration structure for its owner managers towards non-financial measures for 2019.

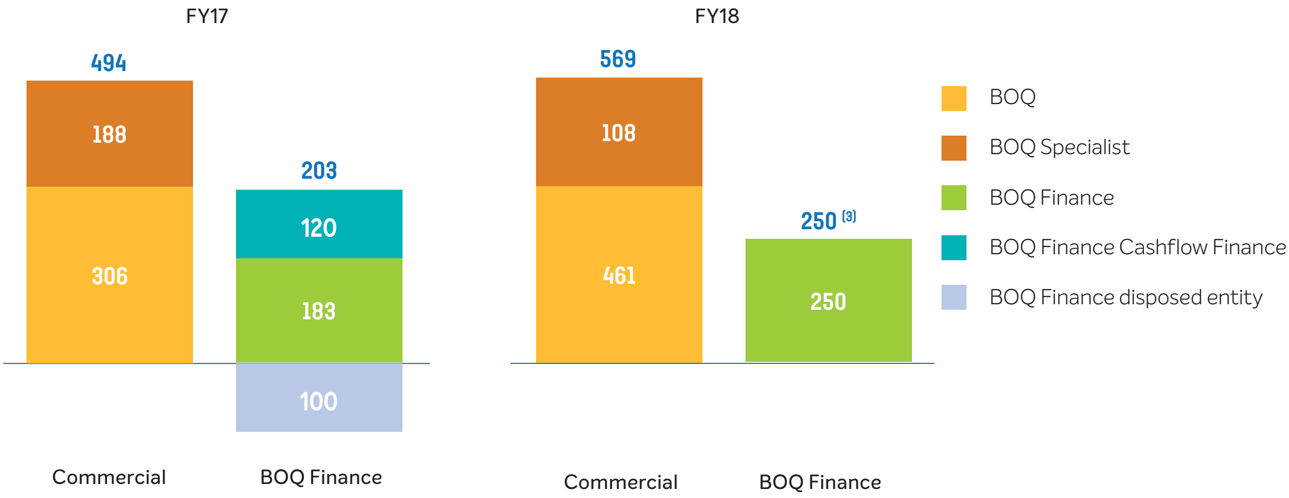
BOQ's growth through the mortgage broker channel improved in FY18 by $165 million. Flows returned as other market participants tightened their serviceability and validation practices. The broker support team has continued to work closely with key aggregator partners to further improve turnaround times and enhance the customer experience.

DIRECTORS' REPORT

For the year ended 31 August 2018

2.7 LENDING (CONTINUED)

Growth in Commercial & BOQ Finance ($m)



	FY17		FY18	
	Commercial	BOQ Finance	Commercial	BOQ Finance (2)
Growth rate	5.6%	4.4%	6.1%	5.8%
System growth (1)	6.3%	4.5%	5.1%	4.8%
Growth vs System	0.9x	1.0x	1.2x	1.2x

(1) Based on APRA and AFIA (previously known as AELA) system growth statistics as at August 2018.
(2) Excludes the acquisition of BOQF Cashflow Finance and disposal of a vendor finance entity.
(3) The FY18 BOQ Finance result includes the BOQF Cashflow Finance business following integration.

BOQ Business

The commercial lending portfolio grew by six per cent in FY18 to $10 billion continuing the momentum from FY17. Growth of 1.2x system was driven by strong existing banking relationships and targeted growth across niche segments.

BOQ Specialist delivered commercial loan book growth of four per cent in its core medical segment, maintaining an estimated market share of 22 per cent. Offering bespoke solutions to medical, dental and veterinary professionals results in building deeper customer relationships from graduation through to retirement. BOQ Specialist has captured a large part of the medical graduate market and is expected to sustain growth in the future as the lending needs of these customers transition through home lending to commercial lending over time.

BOQ Finance continues to provide profitable asset growth above system, growing six per cent to $4.6 billion in FY18. Investment in leasing systems has supported growth in novated leasing as well as new wholesale business. Growth in equipment finance, particularly in agricultural and structured finance solutions led to continued diversification of the exposures.

The BOQ branded commercial portfolio grew by $461 million or seven per cent with consistent performance over both 1H18 and 2H18. The Bank's niche segments of corporate healthcare & retirement living, hospitality & tourism and agribusiness all contributed strong levels of new customer acquisition. Diversification has improved significantly, with strong growth in New South Wales and a reduction in the Queensland concentration in the commercial book to 42 per cent.

The small business (**SME**) lending strategy continued to evolve, with strong referral volumes from the branch network to business bankers. The Bank's ongoing investment in the delivery of product and digital fulfillment capability was supported with the launch of the Square partnership, providing improved transactional capabilities for our small business clients.

Ongoing investment in developing financial markets services will support BOQ's SME and commercial offerings in the future.

DIRECTORS' REPORT

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3. BUSINESS SETTINGS

3.1 ASSET QUALITY

Loan impairment expense was down 15 per cent year on year to $41 million, or nine basis points of gross loans and advances. Impaired asset balances were $28 million lower than FY17 and BOQ maintains prudent provisioning coverage compared to industry peers. Arrears have remained largely flat from FY17 with only a slight increase in 90 dpd arrears attributable to the commercial portfolio.

		Year End Performance			Half Year Performance		
		Aug-18	**Aug-17**	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
Loan Impairment Expense	($ million)	**41**	48	(15%)	**19**	22	(14%)
Loan Impairment Expense / GLA	bps	**9**	11	(2bps)	**8**	10	(2bps)
Impaired Assets	($ million)	**164**	192	(15%)	**164**	173	(5%)
30dpd Arrears	($ million)	**469**	470	-	**469**	493	(5%)
90dpd Arrears	($ million)	**260**	257	1%	**260**	237	10%
Collective Provision & General Reserve for Credit Losses (**GRCL**) / RWA	bps	**67**	83	(16bps)	**67**	70	(3bps)

The table above summarises BOQ's key credit indicators with comparison against August 2017 and February 2018:

- Loan impairment expense reduced by $7 million (15 per cent) year on year to $41 million. This result includes the implementation of the Group's new collective provisioning and reserving model. Collective provisioning contributed $6 million to the decrease over the year and underlines the strong credit risk settings of the Bank. The result is supported by lower specific provisioning activity with only two large exposures contributing $4 million to impairment expense and $12 million in impaired asset balances.
- Impaired Assets decreased by $9 million (five per cent) over 2H18 and $28 million (15 per cent) for FY18 to $164 million. The decrease in impaired balances was driven by the partial settlement and clearance of the Group's largest impaired exposure for $11 million, with two exposures greater than $5 million moving to impaired status during 2H18. The impaired balances of these were $12 million in total. The Group now holds three exposures greater than $5 million in impaired status, totalling $25 million. At 1H18 the Group held one exposure for $28 million and at FY17 the Group held two exposures totalling $40 million.
- 30 day and 90 day arrears have decreased $1 million and increased $3 million year on year and the loan impairment expense to GLA percentage has declined by two basis points in both FY18 and 2H18. This includes three connections that have expired facilities in the 30 day arrears and 90 day arrears for a total of $15 million, and while all loans are being serviced and are considered performing, the full balance is considered in arrears. These are currently being renewed and equate to three basis points of GLAs.

DIRECTORS' REPORT

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3.1 ASSET QUALITY (CONTINUED)

Loan Impairment Expense

	Year End Performance				Half Year Performance			
	Aug-18		Aug-17		Aug-18		Feb-18	
	Expense ($m)	Expense/ GLA (bps)	Expense ($m)	Expense/ GLA (bps)	Expense ($m)	Expense/ GLA (bps)	Expense ($m)	Expense/ GLA (bps)
Retail Lending	15	5	20	7	4	3	11	7
Commercial Lending	11	11	13	14	1	3	10	21
BOQ Finance	15	33	13	30	14	60	1	5
Underlying Loan Impairment Expense	41	9	46	10	19	8	22	10
Large commercial exposure impairment	-	-	16	4	-	-	-	-
Collective provision model adjustment	-	-	(14)	(3)	-	-	-	-
Total Loan Impairment Expense	41	9	48	11	19	8	22	10

The table above highlights improvement across the Group's portfolios with impairment charges at historically low levels due to the low interest rate environment, prudent credit settings and active credit management. During 2H18, loan impairment expense in BOQ Finance returned to historical levels after two halves of unusually low loss performance.

The retail portfolio benefited from improved economic conditions through regional areas which resulted in lower provisioning activity through 2H18. The expense profile within BOQ Business (Commercial Lending and BOQ Finance) was affected by the Group's new collective provisioning model (**CP model**) driving movements between portfolios as performance and behaviour was enhanced following implementation of the new CP model.

FY17 includes the impact of a large commercial exposure impairment and a reduction in the CP model as outlined above.

Impaired Assets

$ million	As at Aug-18	Feb-18	Aug-17	Aug-18 vs Feb-18	Aug-18 vs Aug-17
Retail Lending	67	74	75	(9%)	(11%)
Commercial Lending	81	82	95	(1%)	(15%)
BOQ Finance	16	17	22	(6%)	(27%)
Total Impaired Assets	164	173	192	(5%)	(15%)
Impaired Assets / GLA	36bps	39bps	44bps	(3bps)	(8bps)

Impaired Assets decreased by $9 million or five percent from 1H18 and $28 million or 15 per cent from FY17 to $164 million with the specific provision coverage ratio reducing slightly to 52 per cent. This decline in impaired balances was driven by two connections being managed from the portfolio with $11 million clearing in 1H18 (the Group's second largest impaired connection), and $11 million clearing in 2H18 (the partial clearance of the Group's largest exposure). These were partially offset by two new large exposures for $6 million each. The Group now holds three exposures with impaired balances greater than $5 million for a combined total of $25 million. At 1H18 the Group held one exposure with an impaired balance greater than $5 million for $28 million and at FY17 the Group held two for a combined total of $40 million. The low impairment expense was supported by low specific provisioning activity which led to a lower level of new impairments recognised over FY18.

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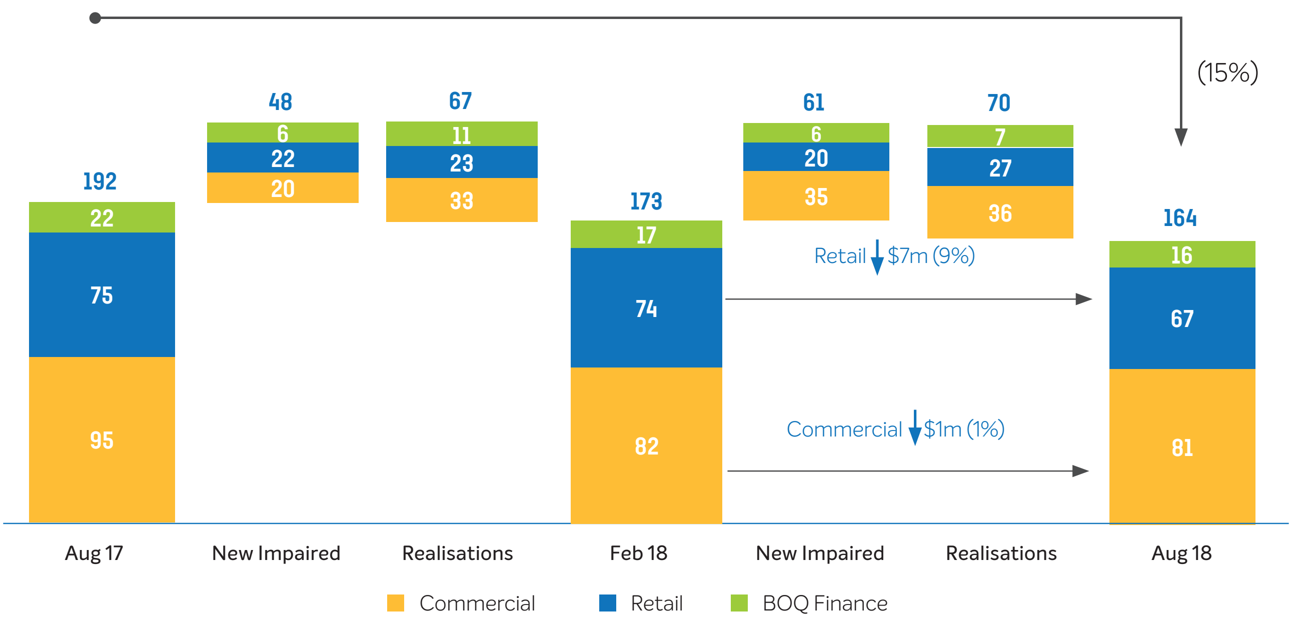
3.1 ASSET QUALITY (CONTINUED)

Impaired Assets ($m)



Provision Coverage

Total provisions decreased by $26 million or 11 per cent to $201 million during FY18. The majority of this reduction was due to the specific provisioning balance, which declined in line with the reduction in the impaired asset balance as realisations exceeded new specific provisioning. Specific provision coverage is at 52 per cent which is down three percentage points on FY17. The implementation of the new collective provisioning and reserving model was further refined over the year and is reflective of the Group's improved credit quality and model enhancements ahead of implementation of the requirements of AASB 9 *Financial Instruments* on 1 September 2018. Collective provision coverage reduced five per cent over FY18, with the GRCL reducing by $22 million (27 per cent), however, BOQ remains conservatively provisioned compared to industry peers.

	As at				
$ million	Aug-18	Feb-18	Aug-17	Aug-18 vs Feb-18	Aug-18 vs Aug-17
Specific Provision	86	99	106	(13%)	(19%)
Collective Provision	115	120	121	(4%)	(5%)
Total Provisions	201	219	227	(8%)	(11%)
GRCL	59	58	81	2%	(27%)
Specific Provisions to Impaired Assets	52%	57%	55%	(500bps)	(300bps)
Total Provisions and GRCL to Impaired Assets [1]	174%	175%	179%	(100bps)	(500bps)
Total Provisions and GRCL to RWA [1]	1.0%	1.0%	1.2%	(3bps)	(23bps)

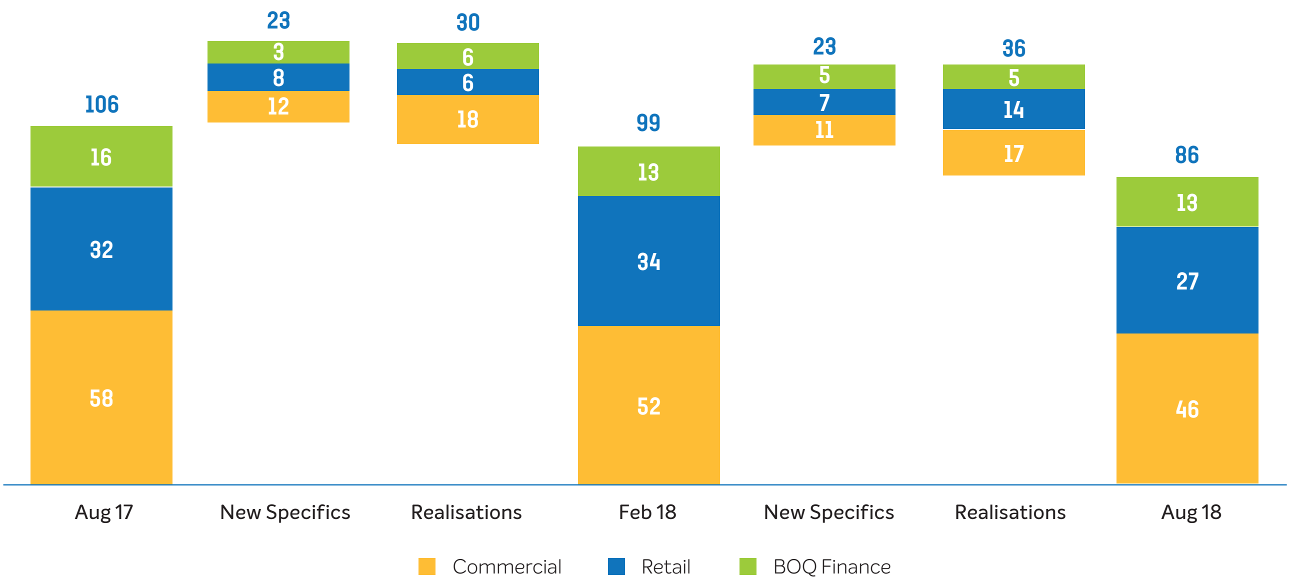
(1) GRCL gross of tax effect.

DIRECTORS' REPORT

For the year ended 31 August 2018

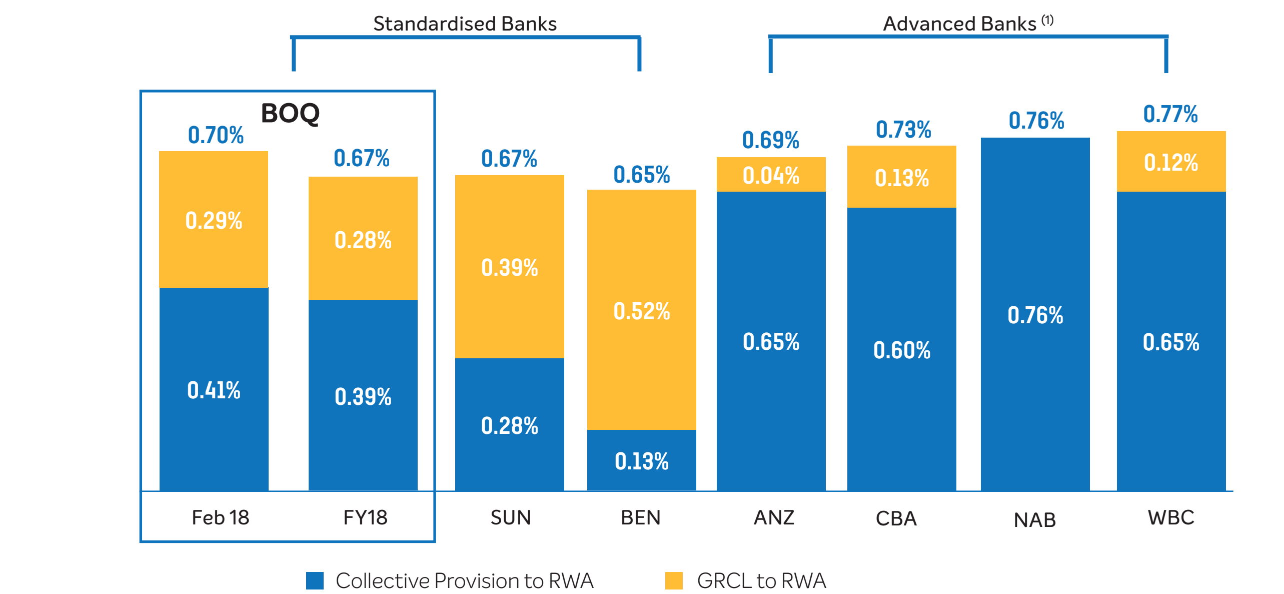
3.1 ASSET QUALITY (CONTINUED)

Specific Provisions ($m)



Collective Provision and GRCL/RWA vs Peers

The graph below provides BOQ's level of collective provisions and GRCL to RWA against the current levels of those of its peers, as published in their most recent financial reports. BOQ's coverage has dropped 16 basis points over FY18, however, BOQ remains prudently provisioned compared to industry peers.



(1) Advanced accredited approach to risk weightings causes coverage to appear higher on a relative basis to the standardised banks.

DIRECTORS' REPORT

For the year ended 31 August 2018

3.1 ASSET QUALITY (CONTINUED)

Arrears

Key Metrics	Portfolio Balance ($m) Aug-18	Aug-18	Feb-18	Aug-17	Aug-18 vs Feb-18	Aug-18 vs Aug-17
Total Lending - Portfolio balance ($ million)		45,279	44,488	43,817	2%	3%
30 days past due ($ million)		469	493	470	(5%)	-
90 days past due ($ million)		260	237	257	12%	1%
		Proportion of Portfolio				
30 days past due: GLAs		1.04%	1.11%	1.07%	(7bps)	(3bps)
90 days past due: GLAs		0.57%	0.53%	0.59%	4bps	(2bp)
By Product						
30 days past due: GLAs (Housing)	28,618	0.92%	0.99%	1.02%	(7bps)	(10bps)
90 days past due: GLAs (Housing)		0.44%	0.45%	0.50%	(1bp)	(6bps)
30 days past due: GLAs (Line of Credit)	1,888	2.33%	2.54%	2.19%	(21bps)	14bps
90 days past due: GLAs (Line of Credit)		1.17%	1.07%	1.25%	10bps	(8bps)
30 days past due: GLAs (Consumer)	297	1.35%	1.64%	1.30%	(29bps)	5bps
90 days past due: GLAs (Consumer)		0.67%	0.99%	0.98%	(32bps)	(31bps)
30 days past due: GLAs (Commercial)	9,881	1.38%	1.26%	1.22%	12bps	16bps
90 days past due: GLAs (Commercial)		1.08%	0.82%	0.86%	26bps	22bps
30 days past due: GLAs (BOQ Finance)	4,595	0.47%	0.82%	0.47%	(35bps)	-
90 days past due: GLAs (BOQ Finance)		0.07%	0.10%	0.13%	(3bps)	(6bps)

Retail Arrears

Housing arrears have continued to improve throughout FY18 reflective of the Group's enhanced servicing, validation and responsible lending practices. This combined with prudent collection practices and the current low interest rate environment has resulted in the continued improvement in credit quality in the housing portfolio.

BOQ Business Arrears

Commercial arrears have tracked upwards over 2H18. This includes three facilities totalling $15 million in both the 30 and 90 days arrears categories that are expected to return to the performing category in 1Q19. If these facilities are excluded, the combined impact of 15 basis points would bring the underlying performance in line with previous periods.

BOQ Finance 30 day arrears ended the year at similar levels to 2H17 and decreased from 1H18 as expected following the usual seasonal increase while 90 day arrears remained low throughout FY18.

DIRECTORS' REPORT

For the year ended 31 August 2018

3.2 FUNDING AND LIQUIDITY

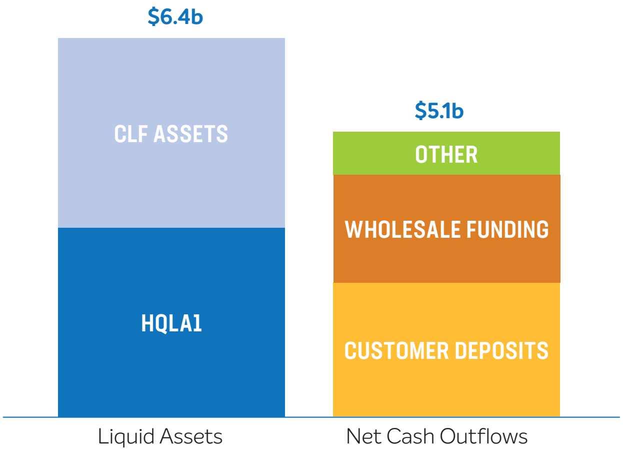
BOQ's liquidity strategy and risk appetite are designed to ensure it has the ability to meet payment obligations as and when they fall due. To manage liquidity risk BOQ maintains a portfolio of unencumbered, high quality liquid assets, giving the Bank a buffer to withstand a range of stress events, including those involving the loss or impairment of both unsecured and secured funding sources.

Liquidity Coverage Ratio (LCR)

APRA requires LCR ADIs to maintain a minimum 100 per cent LCR. The LCR requires sufficient Tier 1 high quality liquid assets (**HQLA1**) and alternative liquid assets (covered by the Committed Liquidity Facility (**CLF**)) to meet net cash outflows over a 30 day period, under a regulator defined liquidity stress scenario. BOQ manages its LCR on a daily basis and actively maintains a buffer above the regulatory minimum in line with BOQ's prescribed risk appetite and management ranges.

The Bank's LCR at 31 August 2018 was 127 per cent , which is two per cent higher than 1H18 and down from the LCR at 31 August 2017 of 132 per cent. BOQ's net cash outflows increased over the year on the back of balance sheet growth and higher wholesale funding maturities in September 2018 rolling into the LCR window. BOQ averaged an LCR of 135 per cent for 1H18 and 136 per cent over FY18.

LCR – August 2018 (127%)



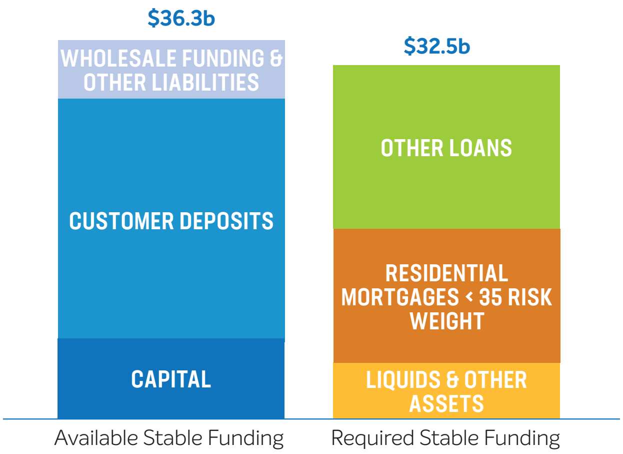
Net Stable Funding Ratio (NSFR)

APRA's objective in implementing the NSFR is to strengthen funding and liquidity resilience. The NSFR encourages ADIs to reduce the amount of liquidity transformation by funding their lending activities with more stable sources of funding, and thereby promoting greater balance sheet resilience.

The NSFR establishes a minimum stable funding requirement based on the liquidity characteristics of the ADI's assets and off-balance sheet activities over a one year time horizon. The NSFR is defined as the ratio of the amount of Available Stable Funding (**ASF**) to the amount of Required Stable Funding (**RSF**). APRA requires ADIs to maintain an NSFR of at least 100 per cent. BOQ manages its NSFR on a daily basis and actively maintains a buffer above the regulatory minimum in line with BOQ's prescribed risk appetite and management ranges.

BOQ's NSFR at 31 August 2018 was 112 per cent, which is a three per cent increase on the Bank's NSFR at the 1 January 2018 implementation. The main driver for the increase in NSFR has been growth in customer deposits. The average NSFR since inception on 1 January 2018 has been 110.7 per cent.

NSFR – August 2018 (112%)

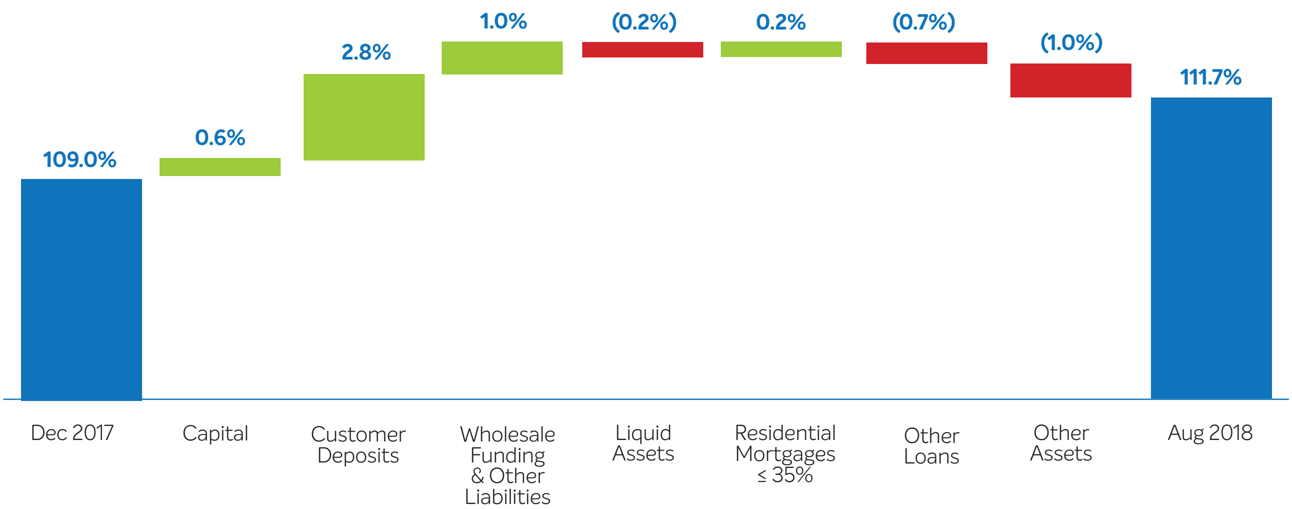


DIRECTORS' REPORT

For the year ended 31 August 2018

3.2 FUNDING AND LIQUIDITY (CONTINUED)

NSFR Waterfall 31 December 2017 - 31 August 2018

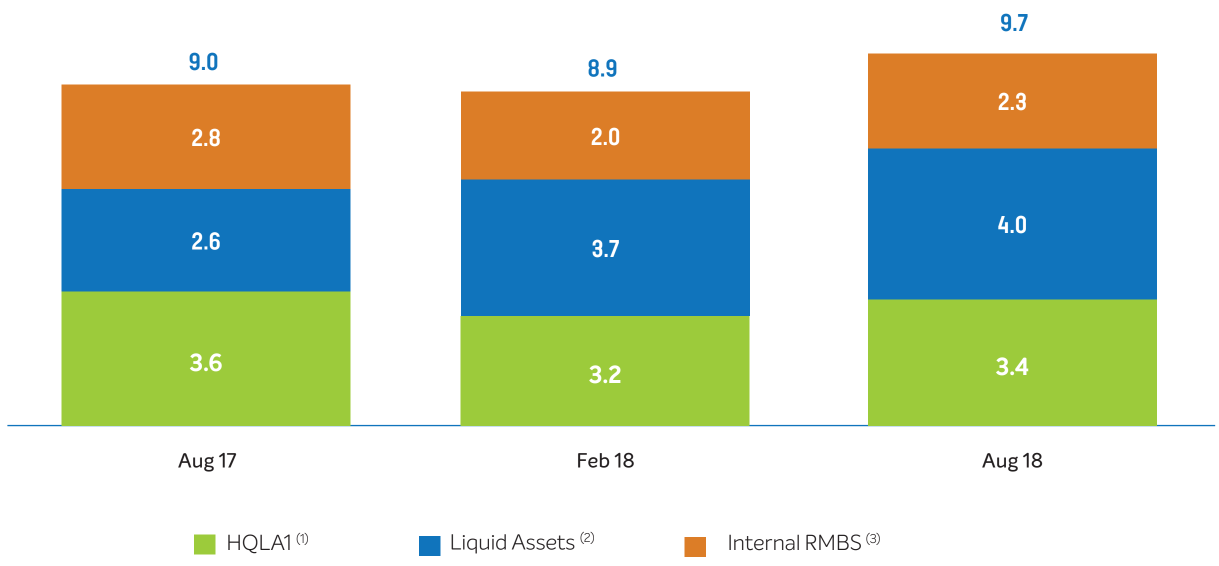


Liquid Assets

BOQ maintains a portfolio of high quality, diversified liquid assets to facilitate balance sheet liquidity and meet internal and regulatory requirements. Liquid assets are comprised of HQLA1 (cash, Australian Semi-Government and Commonwealth Government securities) and alternative liquid assets covered under the CLF from the Reserve Bank of Australia (**RBA**). CLF assets include senior unsecured bank debt, covered bonds, Asset Backed Securities (**ABS**) and Residential Mortgage Backed Securities (**RMBS**) that are eligible for repurchase with the RBA.

BOQ was granted a $3.2 billion RBA CLF for the 2018 calendar year, enabling BOQ to meet its minimum regulatory requirement of greater than 100 per cent LCR. BOQ increased its contingent liquidity in line with the increase in CLF to ensure it maintains a sufficient buffer to its core liquidity.

Liquidity Composition ($b)



(1) HQLA1 includes government and semi-government securities, cash held with RBA and notes & coins.

(2) Liquid Assets include all unencumbered RBA repurchase eligible liquid assets able to be pledged as collateral to the RBA under the CLF.

(3) Internal RMBS are able to be pledged as collateral to the RBA CLF.

DIRECTORS' REPORT

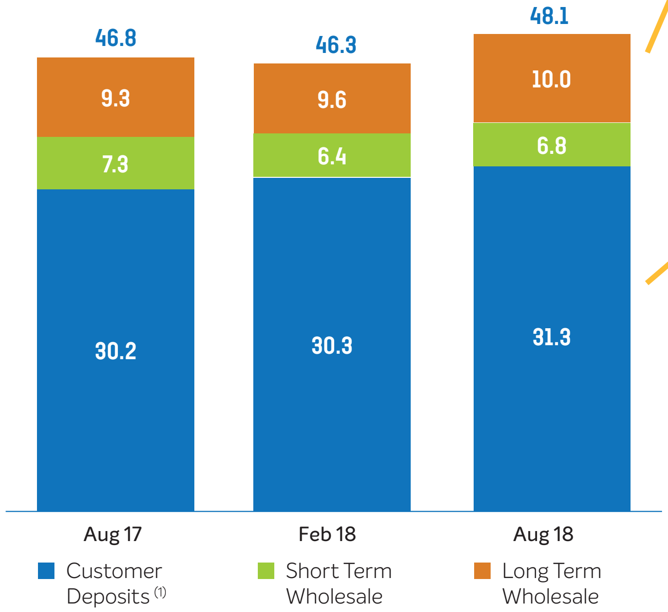
For the year ended 31 August 2018

3.2 FUNDING AND LIQUIDITY (CONTINUED)

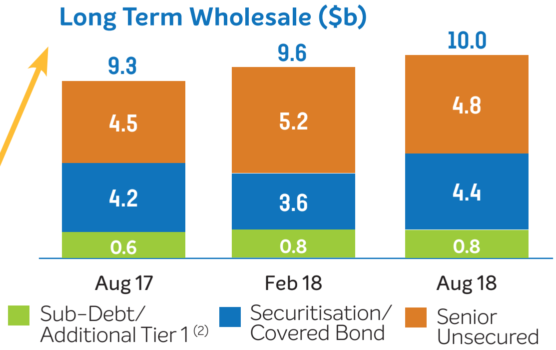
Funding

The Bank's funding strategy and risk appetite reflects both the Group's business strategy, adjusts for the current economic environment and is managed to allow for various scenarios that could impact its funding position.

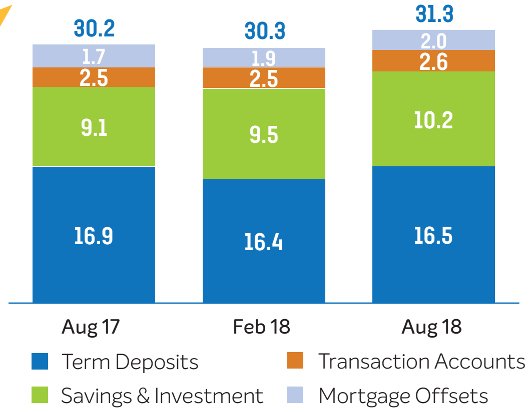
Funding Mix ($b)



Long Term Wholesale ($b)



Customer Deposits ($b)



(1) The classification of customer deposits is defined as all deposits excluding those from financial institutions as defined under APS 210 Liquidity.

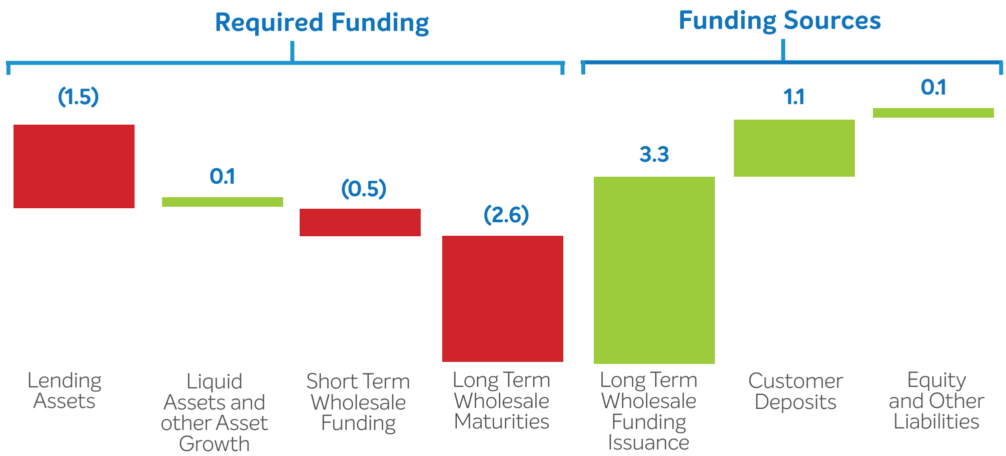
(2) Additional Tier 1 notes.

Wholesale funding

BOQ focuses on three main strategic elements in delivering its wholesale funding objectives – capacity growth, resilience and diversity – while minimising the cost of funds and maintaining its ability to take advantage of opportunities in the most appropriate markets.

The Bank continues to focus on increasing longer dated, stable funding sources whilst reducing reliance on short dated wholesale funding. In FY18, customer deposit growth coupled with net long term wholesale funding growth predominantly funded lending growth and targeted runoff of short term wholesale funding. The Bank's deposit to loan ratio has increased to 69 per cent up one per cent from 1H18 and flat for FY18 through strong customer deposit growth in the Bank's retail channels.

2018 Funding Summary ($b)



DIRECTORS' REPORT

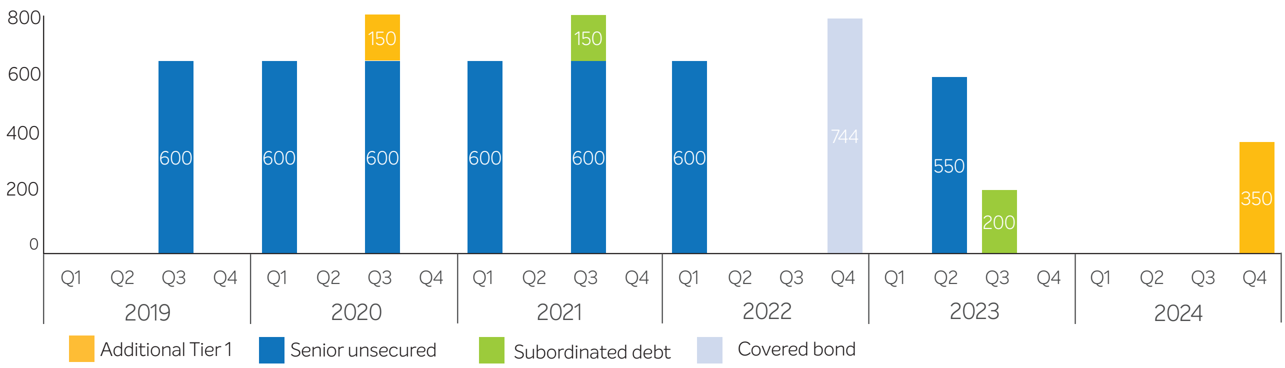
For the year ended 31 August 2018

3.2 FUNDING AND LIQUIDITY (CONTINUED)

Term funding issuance

During FY18, BOQ issued a combination of benchmark sized senior unsecured debt transactions and private placements (both domestically and offshore) to extend its senior unsecured credit curve. The Bank issued two senior unsecured debt transactions, $600 million for four years and $550 million for five years in November 2017 and February 2018 respectively, coupled with a $350 million Capital Notes transaction (December 2017), a $200 million subordinated debt transaction (May 2018) and a $1 billion RMBS capital relief securitisation (May 2018). These transactions have increased the tenor of the wholesale portfolio and provided diversification benefits whilst maintaining manageable refinancing towers over the next five years.

Major Maturities ($m) (1) (2) (3) (4)



(1) Any transaction issued in a currency other than AUD is shown in the applicable AUD equivalent hedged amount.
(2) Senior unsecured maturities greater than or equal to $50 million shown, excludes private placements.
(3) Redemption of subordinated debt notes and Additional Tier 1 notes at the scheduled call date is at BOQ's option and is subject to obtaining prior written approval from APRA.
(4) Quarters are reflected in line with the Bank's financial reporting year.

3.3 CAPITAL MANAGEMENT

Capital Adequacy

$ million	As at Aug-18	Feb-18	Aug-17	Aug-18 vs Feb-18	Aug-18 vs Aug-17
Common Equity Tier 1 (**CET1**)	2,762	2,719	2,690	2%	3%
Additional Tier 1 Capital	500	641	450	(22%)	11%
Total Tier 2	524	328	402	60%	30%
Total Capital Base	3,786	3,688	3,542	3%	7%
Total RWA	29,669	28,859	28,644	3%	4%
CET1 Ratio	9.31%	9.42%	9.39%	(11bps)	(8bps)
Total Capital Adequacy Ratio	12.76%	12.78%	12.37%	(2bps)	39bps

DIRECTORS' REPORT

For the year ended 31 August 2018

3.3 CAPITAL MANAGEMENT (CONTINUED)

The Group's CET1 ratio decreased by 11 basis points during 2H18 to 9.31 per cent.

Underlying Capital Generation was two basis points. Lending growth concentrated in higher risk weighted commercial and BOQ Finance assets was more pronounced in 2H18 which resulted in higher RWA Growth. The ordinary dividend impact was also slightly higher as the dividend reinvestment plan participation rate of 32% for the interim dividend was lower than previous periods.

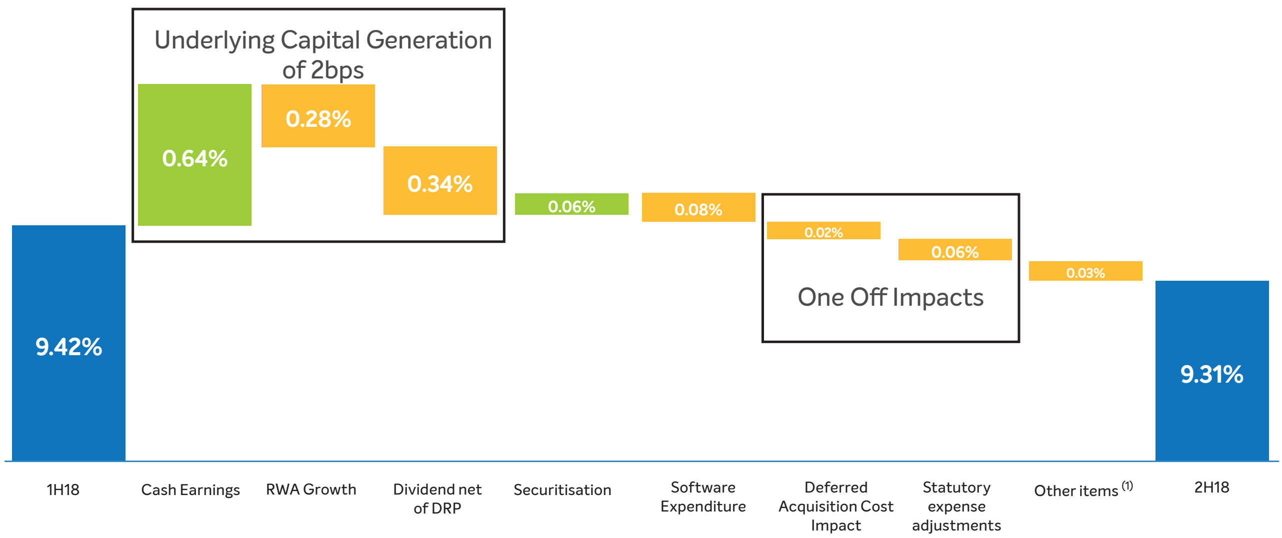
There was an eight basis points one-off impact to CET1 due to increased non-cash items attributed to regulatory/compliance costs, legacy items and increased deductions due to the behavioural life extension of housing loans which impacted deferred acquisition costs. A non-recurring adjustment to the carrying value of Intangible IT assets was offset by the statutory profit reduction associated with the accelerated amortisation, and the creation of a deferred tax asset (**DTA**).

During 2H18, there were CET1 deductions of eight basis points due to an increase in IT intangible asset investment (software spend) that occurred during FY18, which was more pronounced in 2H18.

This was largely offset by the completion of a one billion dollar capital efficient securitisation issue, providing a six basis points increase to CET1.

Other items included increased deferred acquisition costs, reductions in the Available-for-Sale reserve and increased off balance sheet risk weights through changed regulatory treatment. These items were only partially offset by reduced DTA balances.

Common Equity Tier 1 2H18 V 1H18



(1) Other items increased off balance sheet risk weights through changed regulatory treatment net of reduced deferred tax asset deductions.

3.4 TAX EXPENSE

Tax expense arising on cash earnings for FY18 amounted to $170 million. This represented an effective tax rate of 31.3 per cent. This rate is consistent with previous years , which is higher than the prima facie income tax expense rate of 30 per cent primarily due to the non-deductible interest payable on convertible preference shares issued in FY13 (redeemed during FY18), Wholesale Capital Notes issued in FY15 and Capital Notes issued in FY18, together with non-deductible accounting amortisation. The rate appears higher in comparison to FY17 (30.0 per cent), however the rate was unusually low in that year due to the utilisation of previously unrecognised capital losses against the profit on the disposal of a vendor finance entity.

DIRECTORS' REPORT

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4. DIVISIONAL PERFORMANCE

4.1 RETAIL INCOME STATEMENT, KEY METRICS AND FINANCIAL PERFORMANCE REVIEW

Retail Banking provides solutions to personal customers managed through the owner managed and corporate branch network, third party intermediaries and VMA distribution channels.

The Retail Banking division continued its strategy of expanding distribution channels during 2018, with solid growth in lending volumes through VMA and BOQ Broker channels with these channels contributing 40 per cent of housing loan settlements for Retail Banking during 2H18. Whilst the Branch network saw GLAs retreat over FY18, an improvement in customer retention over FY18 was evident across the Owner Manager network.

Retail asset growth was flat over FY18 with a continued focus on quality origination and managing margin in the current competitive landscape. BOQ's customer fulfilment proposition continues to improve as many competitors in the market revisit their lending standards. There has been a stabilisation in the consumer shift away from interest only loans following the introduction of macro prudential limits and investor lending continues to contract, leading to heightened price competition for new owner occupied principal and interest loans.

The VMA 'Reward Me' mortgage offering continues to be well received by customers and brokers, with the mortgage portfolio now exceeding $1.6 billion. These home loan customers provide geographic diversification from the Group's traditional markets in addition to broadening the customer profile to a younger demographic.

The branch network saw an improvement in customer retention compared to prior periods, whilst transitioning to a more productive network footprint better reflecting consumer preferences. The branch network has also demonstrated solid growth in relationship based deposits, with compound annual growth of seven per cent over the past two years in transaction account balances. This helped to support a reduction in more expensive negotiated term deposit balances, improving overall funding costs.

Retail Banking commenced the implementation of its digital enablement strategy with the launch of the new BOQ website, which provides a much improved user experience for customers. Retail Banking continues to invest in its digital program to better meet customer needs.

	Year End Performance			Half Year Performance		
$ million	**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	**Feb-18**	Aug-18 vs Feb-18
Net interest income	458	446	3%	231	227	2%
Non-interest income	67	69	(3%)	34	33	3%
Total income	525	515	2%	265	260	2%
Operating expenses	(281)	(274)	3%	(140)	(141)	(1%)
Underlying profit	244	241	1%	125	119	5%
Loan impairment expense	(15)	(14)	7%	(5)	(10)	(50%)
Profit before tax	229	227	1%	120	109	10%
Income tax expense	(72)	(70)	3%	(38)	(34)	12%
Cash earnings after tax	157	157	-	82	75	9%

Cash earnings after tax of $157 million for FY18 was flat compared to FY17.

Net interest income of $458 million increased $12 million or three per cent over the year. This reflected higher GLA growth whilst managing margins through improved funding composition and product mix.

Non-interest income of $67 million for FY18 was $2 million or three per cent lower than FY17. This reflected lower ATM fees and costs relating to branch conversions offset by an improved contribution from the VMA credit card portfolio.

Operating expenses of $281 million increased $7 million during FY18 (three per cent) reflecting increased amortisation, compliance and branch distribution costs, though this was mitigated by tight cost disciplines across support functions and a reduction in non-lending losses.

Impairment expense of $15 million increased $1 million from FY17. Retail impairment expense reduced in 2H18 as realisations exceeded new impairments resulting in favourable write backs, and collective provision adjustments. Underlying specific provisions and arrears continue to trend lower as regional areas which had experienced economic declines in recent periods began to stablise.

DIRECTORS' REPORT

For the year ended 31 August 2018

4.1 RETAIL INCOME STATEMENT, KEY METRICS AND FINANCIAL PERFORMANCE REVIEW (CONTINUED)

		Year End Performance			Half Year Performance		
Key metrics		**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
CASH EARNINGS BASIS							
CTI	(%)	53.5	53.2	30bps	52.8	54.2	(140bps)
ASSET QUALITY							
90dpd arrears	($ million)	148	163	(9%)	148	147	1%
Impaired assets	($ million)	59	68	(13%)	59	70	(16%)
Loan impairment expense / GLA	(bps)	6	6	-	4	8	(4bps)
BALANCE SHEET							
GLA	($ million)	25,252	25,265	-	25,252	25,258	-
Housing	($ million)	*25,170*	*25,171*	-	*25,170*	*25,167*	-
Other retail	($ million)	*82*	*94*	(13%)	*82*	*91*	(10%)
CREDIT RWA (1)	($ million)	8,841	9,755	(9%)	8,841	9,225	(4%)
CUSTOMER DEPOSITS (2)(3)	($ million)	15,192	14,490	5%	15,192	14,618	4%
Term Deposits	($ million)	*6,650*	*7,029*	(5%)	*6,650*	*6,770*	(2%)
Mortgage Offsets	($ million)	*1,329*	*1,153*	15%	*1,329*	*1,234*	8%
Savings & Investment	($ million)	*5,762*	*4,897*	18%	*5,762*	*5,199*	11%
Transaction Accounts	($ million)	*1,451*	*1,411*	3%	*1,451*	*1,415*	3%
DEPOSIT TO LOAN RATIO	(%)	71	68	300bps	71	68	300bps

(1) Housing Credit RWAs reduced in 1H18 as a result of the change in APS 120.

(2) Treasury managed deposits are included in Other Segment.

(3) August 2017 and February 2018 have been restated to reflect the new operating segment model implemented in FY18.

DIRECTORS' REPORT

For the year ended 31 August 2018

4.2 BOQ BUSINESS INCOME STATEMENT, KEY METRICS AND FINANCIAL PERFORMANCE REVIEW

BOQ Business includes the BOQ branded commercial lending activity, BOQ Finance and BOQ Specialist businesses. The division provides tailored business banking solutions including commercial lending, equipment finance and leasing, cashflow finance, foreign exchange, interest rate hedging, transaction banking and deposit solutions for commercial customers.

The BOQ Business division has delivered on its strategy to grow in niche target segments in FY18, by providing a tailored relationship offering to customers with overall loan growth of $1.5 billion.

BOQ branded commercial loan growth was underpinned by an ongoing focus on quality and appropriate return for risk. Growth in the Bank's niche segments of corporate healthcare & retirement living, hospitality & tourism and agribusiness has also contributed to further diversification of the loan portfolio by geography, industry and asset class, with the Queensland concentration down to 42 per cent.

BOQ Business has enhanced its focus on deposit growth through relationship banking (transaction and savings accounts) as well as moderate growth in Term Deposits. Capability in this area continues to improve with a number of transaction banking solutions being rolled out. These include the launch of the partnership with a digital payments provider (Square) and new merchant capability.

BOQ Specialist continued to drive increasing loan settlement activity whilst the maturing of both the commercial and home lending book has slowed overall growth from earlier periods. The mortgage offering delivered excellent new customer acquisition with housing loans up 15 per cent in the year. This provides a good pipeline of customers with potential commercial lending needs in the future. BOQ Specialist focuses on very clearly defined niches and has developed a distinctive competitive advantage offering tailored consumer and commercial products and services to assist professionals through their practicing life cycles.

BOQ Finance remained focused on cementing its strong position in the market with above system growth and diversification of product mix. Growth and profitability in this business continues to grow year on year, through structured programs in its target vendor & equipment finance customer segments.

	Year End Performance			Half Year Performance		
$ million	**Aug-18**	Aug-17 (1)	Aug-18 vs Aug-17	**Aug-18**	**Feb-18**	Aug-18 vs Feb-18
Net interest income	514	482	7%	263	251	5%
Non-interest income	59	78	(24%)	29	30	(3%)
Total income	573	560	2%	292	281	4%
Operating expenses	(228)	(220)	4%	(116)	(112)	4%
Underlying profit	345	340	1%	176	169	4%
Loan impairment expense	(26)	(34)	(24%)	(14)	(12)	17%
Profit before tax	319	306	4%	162	157	3%
Income tax expense	(100)	(90)	11%	(50)	(50)	-
Cash earnings after tax	219	216	1%	112	107	5%

(1) Includes the disposal of a vendor finance entity.

Cash earnings after tax of $219 million for FY18 was $19 million higher than FY17 after adjusting for the $16 million profit on disposal of a vendor finance entity in 2H17.

Net interest income of $514 million for FY18 increased $32 million or seven per cent from FY17. This was driven by lending growth of eight per cent or $1.5 billion with all parts of the business delivering solid growth rates. Net interest spread reduced in line with the increasing cost of short term funding and the higher growth rate in BOQ Specialist mortgage lending relative to higher margin commercial lending.

Non-interest income of $59 million was $19 million lower than FY17, primarily due to the disposal of a vendor finance entity ($16 million). Non-interest income generated by financial markets activity has increased, however this was offset by a reduction in income from the sale of assets in equipment finance and lower corporate banking fees.

Operating expenses of $228 million have increased by four per cent from FY17 due to inflation, amortisation from investment in technology and salary costs associated with managing growing portfolio.

Impairment expense of $26 million continued the declining trend year on year following the continued strong performance in the BOQ Finance portfolio and improvement in mix in the commercial lending book. Specific provisions have decreased from FY17 with some small increases in other areas due to the changes in the CP model.

DIRECTORS' REPORT

For the year ended 31 August 2018

4.2 BOQ BUSINESS INCOME STATEMENT, KEY METRICS AND FINANCIAL PERFORMANCE REVIEW (CONTINUED)

		Year End Performance			Half Year Performance		
Key metrics		**Aug-18**	Aug-17 (1)	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
CASH EARNINGS BASIS							
CTI	(%)	39.8	38.3	50bps	39.7	39.9	(20bps)
ASSET QUALITY							
90dpd arrears	($ million)	113	94	20%	113	90	26%
Impaired assets	($ million)	104	124	(16%)	104	103	2%
Loan impairment expense / GLA	(bps)	13	18	(5bps)	14	13	1bp
BALANCE SHEET							
GLA	($ million)	20,027	18,552	8%	20,027	19,230	4%
Housing	($ million)	*5,336*	*4,682*	14%	*5,336*	*5,068*	5%
Commercial and other	($ million)	*10,096*	*9,525*	6%	*10,096*	*9,802*	3%
BOQ Finance	($ million)	*4,595*	*4,345*	6%	*4,595*	*4,360*	5%
CREDIT RWA	($ million)	16,317	15,016	9%	16,317	15,627	4%
CUSTOMER DEPOSITS (2)(3)	($ million)	8,004	7,363	9%	8,004	7,644	5%
Term Deposits	($ million)	*1,739*	*1,524*	14%	*1,739*	*1,596*	9%
Mortgage Offsets	($ million)	*671*	*523*	28%	*671*	*617*	9%
Savings & Investment	($ million)	*4,453*	*4,251*	5%	*4,453*	*4,346*	2%
Transaction Accounts	($ million)	*1,141*	*1,065*	7%	*1,141*	*1,085*	5%
DEPOSIT TO LOAN RATIO	(%)	68	70	(200bps)	68	69	(100bps)

(1) Includes the disposal of a vendor finance entity.

(2) Treasury managed deposits are included in Other Segment.

(3) August 2017 and February 2018 have been restated to reflect the new operating segment model implemented in FY18.

DIRECTORS' REPORT

For the year ended 31 August 2018

4.3 OTHER SEGMENT INCOME STATEMENT AND FINANCIAL PERFORMANCE REVIEW

Other includes Group Treasury, St Andrew's Insurance and Group Head Office.

	Year End Performance			Half Year Performance		
$ million	**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	**Feb-18**	Aug-18 vs Aug-17
Net interest income	(7)	(2)	250%	(4)	(3)	33%
Non-interest income	19	28	(32%)	7	12	(42%)
Total income	12	26	(54%)	3	9	(67%)
Operating expenses	(18)	(19)	(5%)	(9)	(9)	-
Underlying profit	(6)	7	(186%)	(6)	-	-
Loan impairment expense	-	-	-	-	-	-
Profit before tax	(6)	7	(186%)	(6)	-	-
Income tax expense	2	(2)	(200%)	2	-	-
Cash earnings / (loss) after tax	(4)	5	(180%)	(4)	-	-

Other segment cash loss after tax for FY18 is $4 million. Net interest income in 2H18 is largely in line with 1H18.

Non-interest income includes St Andrew's Insurance and trading income. The reduction from FY17 is largely attributed to reduced trading income in 2H18.

Operating expenses have remained relatively stable across periods.

DIRECTORS' REPORT

For the year ended 31 August 2018

5. APPENDICES

5.1 RECONCILIATION OF STATUTORY PROFIT TO CASH EARNINGS

Cash earnings is used to present a clear view of BOQ's underlying operating results. This excludes a number of items that introduce volatility or one off distortions of the current year performance, and allows for a more effective comparison of BOQ's performance across reporting periods.

The main exclusions relate to: Regulatory / compliance costs ($9 million after tax) which include external costs and other related costs associated with the Royal Commission, BEAR, Code of Banking Practice and other regulatory matters; Legacy Items ($5 million after tax) which includes external legal and net settlement costs associated with the Petersen class action; and Software changes ($11 million after tax) which include a non-recurring adjustment due to a re-assessment of useful lives of existing assets aligned with the Group's Investment Roadmap and a change to the capitalisation policy.

(A) RECONCILIATION OF CASH EARNINGS TO STATUTORY NET PROFIT AFTER TAX

	Year End Performance			Half Year Performance		
$ million	**Aug-18**	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
Cash Earnings after Tax	**372**	378	(2%)	**190**	182	4%
Amortisation of acquisition fair value adjustments	**(7)**	(13)	(46%)	**(2)**	(5)	(60%)
Hedge ineffectiveness	**(3)**	(9)	(67%)	**(2)**	(1)	100%
Integration / transaction costs	**(1)**	(1)	-	**(1)**	-	-
Regulatory / compliance	**(9)**	-	-	**(8)**	(1)	700%
Software changes	**(11)**	-	-	**(11)**	-	-
Legacy items	**(5)**	(3)	67%	**(4)**	(1)	300%
Statutory Net Profit after Tax	336	352	(5%)	162	174	(7%)

(B) NON-CASH EARNINGS RECONCILING ITEMS

$ million	Cash Earnings Aug-18	VMA	Amortisation of fair value adjustments	Hedge ineffectiveness	Integration/ transaction costs	Regulatory / compliance	Software changes	Legacy items	Statutory Net Profit Aug-18
Net Interest Income	**965**	-	-	-	-	-		-	**965**
Non-Interest Income	**145**	15	-	(4)	-	-		-	**156**
Total Income	**1,110**	15	-	(4)	-	-		-	**1,121**
Operating Expenses	**(527)**	(15)	(8)	-	(1)	(13)	(16)	(7)	**(587)**
Underlying Profit	**583**	-	(8)	(4)	(1)	(13)	(16)	(7)	**534**
Loan Impairment Expense	**(41)**	-	-	-	-	-	-	-	**(41)**
Profit before Tax	**542**	-	(8)	(4)	(1)	(13)	(16)	(7)	**493**
Income Tax Expense	**(170)**	-	1	1	-	4	5	2	**(157)**
Profit after Tax	372	-	(7)	(3)	(1)	(9)	(11)	(5)	336

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5.2 OPERATING CASH EXPENSES

	Year End Performance			Half Year Performance		
	Aug-18	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
EMPLOYEE EXPENSES						
Salaries	**214**	208	3%	**107**	107	–
Superannuation contributions	**20**	20	–	**11**	9	22%
Payroll tax	**13**	12	8%	**7**	6	17%
Employee Share Programs	**10**	11	(9%)	**5**	5	–
Other	**6**	6	–	**3**	3	–
	263	257	2%	**133**	130	2%
OCCUPANCY EXPENSES						
Lease expense	**32**	30	7%	**16**	16	–
Depreciation of Fixed Assets	**9**	9	–	**4**	5	(20%)
Other	**3**	3	–	**2**	1	100%
	44	42	5%	**22**	22	–
GENERAL EXPENSES						
Marketing	**15**	16	(6%)	**8**	7	14%
Commissions to Owner Managed Branches	**5**	6	(17%)	**2**	3	(33%)
Communications and postage	**17**	20	(15%)	**8**	9	(11%)
Printing and stationery	**3**	4	(25%)	**1**	2	(50%)
Impairment	**2**	1	100%	**1**	1	–
Processing costs	**15**	10	50%	**8**	7	14%
Other operating expenses	**24**	28	(14%)	**12**	12	–
	81	85	(5%)	**40**	41	(2%)
IT EXPENSES						
Data processing	**75**	70	7%	**39**	36	8%
Amortisation of Intangible Assets	**43**	37	16%	**21**	22	(5%)
Depreciation of Fixed Assets	**1**	1	–	**–**	1	(100%)
	119	108	10%	**60**	59	2%
OTHER EXPENSES						
Professional fees	**13**	13	–	**7**	6	17%
Directors' fees	**2**	2	–	**1**	1	–
Other	**5**	6	(17%)	**2**	3	(33%)
	20	21	(5%)	**10**	10	–
Total Operating Expenses	**527**	513	3%	**265**	262	1%

DIRECTORS' REPORT

For the year ended 31 August 2018

5.2 OPERATING CASH EXPENSES (CONTINUED)

Employee Expenses

Employee costs grew two per cent on FY17 with a relatively flat number of employees (FTE) over FY18.

Occupancy Expenses

Occupancy expenses have increased five per cent on FY17 with non-recurring lease benefits being recognised in 2H17.

General Expenses

General expenses have reduced $4 million or five per cent on FY17. A number of initiatives have delivered this outcome including a continued shift towards electronic provision of customer communications, digitisation of cheque processing reducing courier costs, renegotiated telecommunications contract for contemporary market pricing, upgraded services for branches and lower non-lending losses. Processing costs in FY17 included a non-recurring benefit.

IT Expenses

Capitalised investment expenditure (refer Section 2.6 Capitalised Investment Expenditure) has resulted in an uplift of $6 million in software amortisation in FY18. This increased expenditure covered both strategic and regulatory investment that was accompanied by an operating expense component which covers software licensing, external specialists and outsourced operations which is recognised within data processing costs.

5.3 PROPERTY, PLANT & EQUIPMENT (CONSOLIDATED)

$ million	Leasehold improvements $m	Plant furniture and equipment $m	IT equipment $m	Capital works in progress $m	Assets under Operating Lease $m	Total $m
COST						
Balance as at 31 August 2017	74	33	33	4	18	162
Additions	7	1	1	-	5	14
Disposals	(2)	(1)	-	-	(7)	(10)
Transfers between categories	3	-	-	(3)	-	-
Balance as at 31 August 2018	82	33	34	1	16	166
DEPRECIATION AND LOSS ON DISPOSAL / IMPAIRMENT						
Balance as at 31 August 2017	38	23	29	-	12	102
Depreciation for the year	7	2	1	-	5	15
Disposals	(2)	(1)	-	-	(5)	(8)
Balance as at 31 August 2018	43	24	30	-	12	109
Carrying amount as at 31 August 2017	36	10	4	4	6	60
Carrying amount as at 31 August 2018	39	9	4	1	4	57

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5.4 CASH EPS CALCULATIONS

		Year End Performance			Half Year Performance		
		Aug-18	Aug-17	Aug-18 vs Aug-17	**Aug-18**	Feb-18	Aug-18 vs Feb-18
Basic EPS	(cents)	**94.7**	**97.6**	(3%)	**48.2**	46.5	4%
Diluted EPS	(cents)	**89.3**	**93.9**	(5%)	**45.2**	44.5	2%
Reconciliation of Cash Earnings for EPS							
Cash Earnings available for ordinary shareholders	($ million)	372	378	(2%)	190	182	(6%)
Add: CPS Dividend	($ million)	7	15	(53%)	1	6	(86%)
Add: WCN	($ million)	7	7	-	4	3	-
Add: Capital Notes [1]	($ million)	9	-	-	7	2	-
Cash Diluted Earnings available for ordinary shareholders	($ million)	395	400	(1%)	202	193	(6%)
Weighted Average Number of Shares (**WANOS**)							
Basic WANOS	(million)	393	387	2%	395	392	1%
Add: Effect of award rights	(million)	2	2	-	2	2	-
Add: Effect of CPS	(million)	12	25	(52%)	3	20	(85%)
Add: Effect of WCN	(million)	14	12	17%	14	12	17%
Add: Effect of Capital Notes [1]	(million)	21	-	-	32	10	200%
Diluted WANOS for Cash Earnings EPS	(million)	442	426	3%	446	436	2%

(1) In December 2017, the Bank issued 3,500,000 Capital Notes at a price of $100 per note.

5.5 ISSUED CAPITAL

Ordinary shares

	Consolidated	
	2018 Number	2018 $m
Movements during the year		
Balance at the beginning of the year – fully paid	391,739,729	3,396
Issue of ordinary shares [1]	852,809	11
Dividend reinvestment plan [2]	4,719,312	47
Balance at the end of the year – fully paid	397,311,850	3,454

(1) On 26 October 2017, 850,000 ordinary shares were issued at $13.28 and on 17 May 2018 2,809 ordinary shares were issued at $10.02 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

(2) 32 per cent was taken up by shareholders on 17 May 2018 as part of the Dividend Reinvestment Plan.

DIRECTORS' REPORT

For the year ended 31 August 2018

5.6 AVERAGE BALANCE SHEET AND MARGIN ANALYSIS

	August 2018 (Full Year)			August 2017 (Full Year) [1]		
$ million	Average Balance $m	Interest $m	Average Rate %	Average Balance $m	Interest $m	Average Rate %
INTEREST EARNING ASSETS						
Gross loans & advances at amortised cost	42,763	1,927	4.52	41,702	1,899	4.55
Investments & other securities	6,055	142	2.35	6,189	147	2.37
Total interest earning assets	48,818	2,069	4.25	47,891	2,046	4.27
Non-interest earning assets						
Property, plant & equipment	59			58		
Other assets	1,555			1,525		
Provision for impairment	(220)			(253)		
Total non-interest earning assets	1,394			1,330		
Total Assets	50,212			49,221		
INTEREST BEARING LIABILITIES						
Retail deposits	28,729	578	2.02	28,335	611	2.16
Wholesale deposits & borrowings	16,928	526	3.12	16,427	509	3.10
Total interest bearing liabilities	45,657	1,104	2.42	44,762	1,120	2.50
Non-interest bearing liabilities	755			783		
Total liabilities	46,412			45,545		
Shareholders' funds	3,800			3,676		
Total Liabilities & Shareholders' Funds	50,212			49,221		
INTEREST MARGIN & INTEREST SPREAD						
Interest earning assets	48,818	2,069	4.25	47,891	2,046	4.27
Interest bearing liabilities	45,657	1,104	2.42	44,762	1,120	2.50
Net interest spread			1.83			1.77
Benefit of net interest-free assets, liabilities and equity			0.15			0.16
NIM – on average interest earning assets	48,818	965	1.98	47,891	926	1.93

[1] NIM has been adjusted for mortgage offset balances to align with industry practice. Average mortgage offset balances were $1,506m in FY17.

DIRECTORS' REPORT

For the year ended 31 August 2018

5.6 AVERAGE BALANCE SHEET AND MARGIN ANALYSIS (CONTINUED)

	August 2018 (Six month period)			February 2018 (Six month period)		
$ million	Average Balance $m	Interest $m	Average Rate %	Average Balance $m	Interest $m	Average Rate %
INTEREST EARNING ASSETS						
Gross loans & advances at amortised cost	43,227	980	4.50	42,427	947	4.50
Investments & other securities	5,932	72	2.41	6,092	70	2.32
Total interest earning assets	49,159	1,052	4.25	48,519	1,017	4.23
Non-interest earning assets						
Property, plant & equipment	58			59		
Other assets	1,566			1,534		
Provision for impairment	(214)			(226)		
Total non-interest earning assets	1,410			1,367		
Total Assets	50,569			49,886		
INTEREST BEARING LIABILITIES						
Retail deposits	28,907	290	1.99	28,659	288	2.03
Wholesale deposits & borrowings	17,139	272	3.15	16,649	254	3.08
Total interest bearing liabilities	46,046	562	2.42	45,308	542	2.41
Non-interest bearing liabilities	700			803		
Total liabilities	46,746			46,111		
Shareholders' funds	3,823			3,775		
Total Liabilities & Shareholders' Funds	50,569			49,886		
INTEREST MARGIN & INTEREST SPREAD						
Interest earning assets	49,159	1,052	4.25	48,519	1,017	4.23
Interest bearing liabilities	46,046	562	2.42	45,308	542	2.41
Net interest spread			1.83			1.82
Benefit of net interest-free assets, liabilities and equity			0.15			0.15
NIM – on average interest earning assets	49,159	490	1.98	48,519	475	1.97

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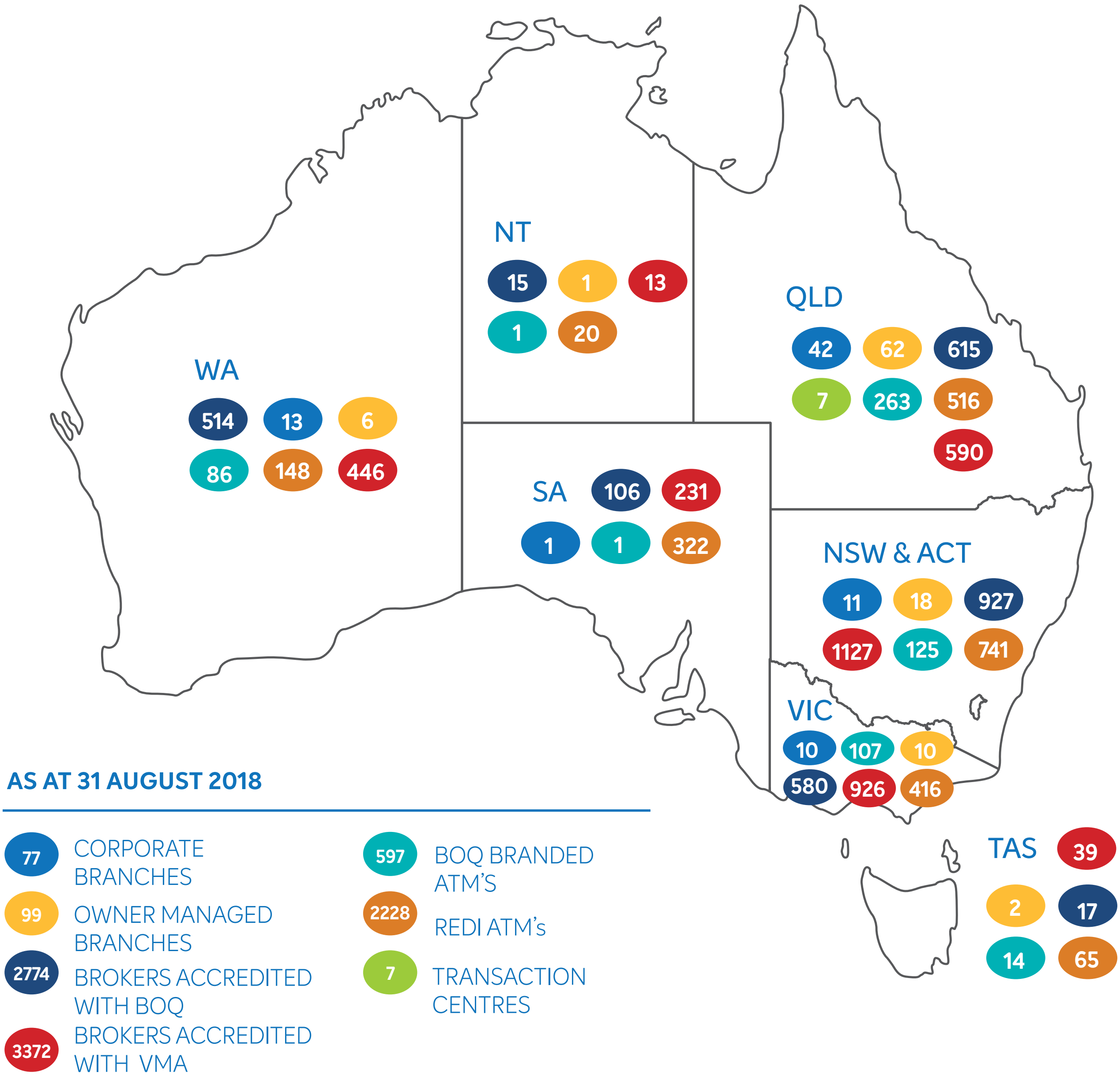
5.7 DISTRIBUTION FOOTPRINT

BOQ has evolved its Customer in Charge strategic pillar to allow customers to engage through the channel of their choice. This could be through a preferred broker (aligned to BOQ or VMA), directly with BOQ through its owner managed and corporate branches, online via digital, social media and mobile banking, or on the phone to BOQ's customer contact centres.

Branch numbers reduced by seven during 2018. The majority of BOQ's owner managers (81 per cent) have transitioned to the new franchise agreement which better aligns the network with the strategic objectives of the Bank and has delivered significant operational performance improvements. The Bank remains committed to support its unique owner manager franchise model and continues to recruit experienced bankers and small business practitioners who are aligned to BOQ's service ethic to customers.

Accredited Broker numbers have reduced from last year as BOQ adopts a more targeted approach to growth through the third party channels which are continuing to grow at above system levels and where the Bank is historically under represented.

In a market where many customers prefer using third party channels, BOQ continued to build its broker presence during 2018 with 30 per cent of housing settlements being originated through the VMA and BOQ branded accredited brokers. The large majority of these brokers are domiciled outside of Queensland, which continues to accelerate the geographic diversification of the portfolio and provide deeper access to the Sydney and Melbourne markets, where the Group has traditionally been under represented.



DIRECTORS' REPORT

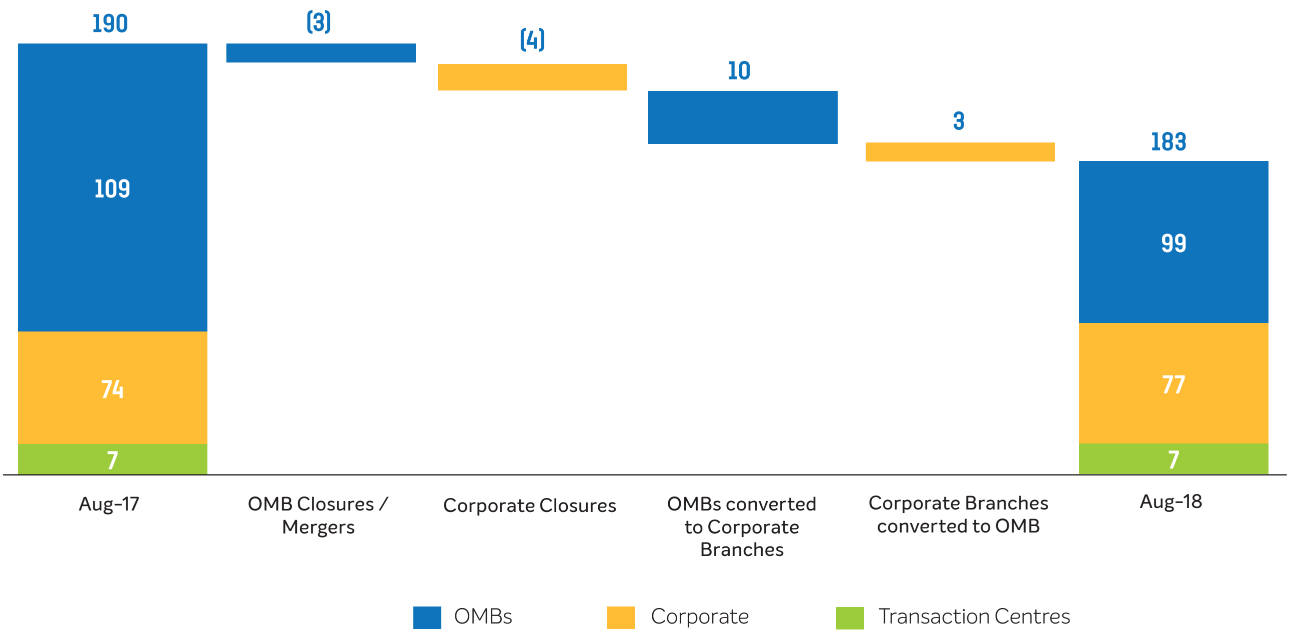
For the year ended 31 August 2018

5.7 DISTRIBUTION FOOTPRINT (CONTINUED)

As at Aug-18	QLD	NSW / ACT	VIC	WA	NT	TAS	SA	Total
Corporate Branches	42	11	10	13	–	–	1	77
Owner Managed Branches	62	18	10	6	1	2	–	99
Transaction Centres	7	–	–	–	–	–	–	7
	111	29	20	19	1	2	1	183

As at Aug-17	QLD	NSW / ACT	VIC	WA	NT	TAS	SA	Total
Corporate Branches	41	11	8	13	–	–	1	74
Owner Managed Branches	68	18	12	8	1	2	–	109
Transaction Centres	7	–	–	–	–	–	–	7
	116	29	20	21	1	2	1	190

Corporate, Owner Managed Branches (OMB) & Transaction Centres



5.8 CREDIT RATING

The Bank monitors rating agency developments closely. Entities in the Group are rated by S&P, Moody's Investor Service and Fitch Ratings.

BOQ's current debt ratings are shown below.

Rating Agency	Short Term	Long Term	Outlook
S&P	A2	BBB+	Stable
Fitch	F2	A-	Stable
Moody's	P2	A3	Stable

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5.9 REGULATORY DISCLOSURES

The APS 330 Capital Disclosure Template and Regulatory Capital reconciliation (included in the relevant Pillar 3 Disclosures document) and the Capital Instruments Disclosures are available at the Regulatory Disclosures section of the Bank's website at the following address.

https://www.boq.com.au/regulatory_disclosures

5.10 LIQUIDITY COVERAGE RATIO

APRA requires authorised deposit-taking institutions to maintain a minimum 100 per cent LCR. The LCR requires sufficient HQLA1 and alternative liquid assets (covered by the CLF) to meet net cash outflows over a 30 day period, under a regulator defined liquidity stress scenario. BOQ manages its LCR on a daily basis with a buffer above the regulatory minimum in line with the BOQ prescribed risk appetite and management ranges. BOQ's average LCR over the August quarter was 136 per cent which is slightly higher than the previous May quarter average of 134 per cent. The increase in the average HQLA1 and cash inflows over the quarter was partly off-set by an increase in customer deposits. The following table presents detailed information on the average LCR composition for the two quarters. 92 data points were used in calculating the average figures for the two quarters.

BOQ maintains a portfolio of high quality, diversified liquid assets to facilitate balance sheet liquidity and meet internal and regulatory requirements. Liquid assets comprise of HQLA1 (cash, Australian Semi-Government and Commonwealth Government securities) and alternative liquid assets covered by the CLF from the RBA. Assets eligible for the CLF include senior unsecured bank debt, covered bonds, asset backed securities, RMBS and internal RMBS that are eligible for repurchase with the RBA.

BOQ has a stable, diversified and resilient deposit and funding base that mitigates the chance of a liquidity stress event across various funding market conditions. BOQ uses a range of funding instruments including customer deposits, securitisation and short term and long term wholesale debt instruments. The Group increased customer funding and long-term wholesale issuance in the period as part of its overall funding strategy to lengthen tenor and add to its stable funding base. Bank lending is predominantly funded from stable funding sources, with short term wholesale funding primarily used to manage timing mismatches and fund liquid assets.

The liquid assets composition has remained relatively stable over the year, the allocation to HQLA1 as a percentage of Net Cash Outflows (**NCO**) for the August Quarter averaged 74 per cent. BOQ does not have significant derivative or currency exposures that could adversely affect its LCR.

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5.10 LIQUIDITY COVERAGE RATIO (CONTINUED)

	Average Quarterly Performance			
	August Quarter		May Quarter	
$ million	Total Unweighted Value $m	Total Weighted Value $m	Total Unweighted Value $m	Total Weighted Value $m
LIQUID ASSETS, OF WHICH				
High quality liquid assets	n/a	3,520	n/a	3,325
Alternative liquid assets	n/a	2,981	n/a	2,981
Total Liquid Assets	n/a	6,501	n/a	6,306
CASH OUTFLOWS				
Customer deposits and deposits from small branch customers, of which	15,141	1,521	14,780	1,464
stable deposits	*6,924*	*346*	*6,893*	*345*
less stable deposits	*8,217*	*1,175*	*7,887*	*1,119*
Unsecured wholesale funding, of which	4,123	2,511	4,044	2,415
non-operational deposits	*3,206*	*1,594*	*3,179*	*1,550*
unsecured debt	*917*	*917*	*865*	*865*
Secured wholesale funding	n/a	32	n/a	30
Additional requirements, of which	1,781	610	535	441
outflows related to derivatives exposures and other collateral requirements	*548*	*548*	*436*	*436*
credit and liquidity facilities	*1,233*	*62*	*99*	*5*
Other contractual funding obligations	1,016	663	946	638
Other contingent funding obligations	9,595	561	11,084	624
Total Cash Outflows	31,656	5,898	31,389	5,612
CASH INFLOWS				
Secured lending (e.g. reverse repos)	208	–	67	–
Inflows from fully performing exposures	790	437	650	341
Other cash inflows	680	680	578	578
Total Cash Inflows	1,678	1,117	1,295	919
Total Net Cash Outflows	29,978	4,781	30,094	4,693
Total Liquid Assets	n/a	6,501	n/a	6,306
Total Net Cash Outflows	n/a	4,781	n/a	4,693
Liquidity Coverage Ratio (%)	n/a	136%	n/a	134%

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5.11 NET STABLE FUNDING RATIO

APRA's objective in implementing the NSFR is to strengthen funding and liquidity resilience. The NSFR encourages ADIs to reduce the amount of liquidity transformation by funding their lending activities with more stable sources of funding, and thereby promoting greater balance sheet resilience.

The NSFR establishes a minimum stable funding requirement based on the liquidity characteristics of the ADI's assets and off-balance sheet activities over a one year time horizon. The NSFR is defined as the ratio of the amount of ASF to the amount of RSF. APRA requires ADIs to maintain an NSFR of at least 100 per cent. BOQ manages its NSFR on a daily basis and actively maintains a buffer above the regulatory minimum in line with BOQ's prescribed risk appetite and management ranges.

BOQ's NSFR at 31 August 2018 was 112 per cent, which is a 3 per cent increase at implementation on 1 January 2018. The main drivers for the increase in NSFR has been strong growth in customer deposits. The average NSFR since inception on 1 January 2018 has been 111 per cent.

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5.11 NET STABLE FUNDING RATIO (CONTINUED)

AUGUST 2018	Unweighted value by residual maturity				
	No maturity	< 6 months	6 months to < 1 year	> 1 year	Weighted value
AVAILABLE STABLE FUNDING (ASF) ITEM					
Capital	3,960	–	–	850	4,810
of which: Regulatory capital	*3,960*	–	–	*850*	*4,810*
Retail deposits and deposits from small business customers	14,018	8,480	–	–	20,708
of which: Stable deposits	*6,544*	*2,640*	–	–	*8,726*
of which: Less stable deposits	*7,474*	*5,840*	–	–	*11,982*
Wholesale funding	1,754	13,558	1,334	5,431	10,660
of which: Other wholesale funding	*1,754*	*13,558*	*1,334*	*5,431*	*10,660*
Other liabilities	785	58	–	73	73
of which: NSFR derivative liabilities	*n/a*	*53*	–	–	*n/a*
of which: All other liabilities and equity not included in the above categories	*785*	*5*	–	*73*	*73*
Total ASF	n/a	n/a	n/a	n/a	**36,251**
REQUIRED STABLE FUNDING (RSF) ITEM					
Total NSFR (HQLA)	n/a	n/a	n/a	n/a	150
ALA	n/a	n/a	n/a	n/a	320
Deposits held at other financial institutions for operational purposes	337	–	–	–	276
Performing loans and securities	–	3,096	2,274	35,691	29,173
of which: Performing loans to financial institutions secured by Level 1 HQLA	–	*100*	–	–	*10*
of which: Performing loans to financial institutions secured by non-Level 1 HQLA and unsecured performing loans to financial institutions	–	*441*	–	*173*	*239*
*of which: Performing loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns, central banks and public sector entities (**PSEs**) of which:*	–	*1,904*	*1,715*	*10,223*	*10,418*
With a risk weight of less than or equal to 35% under APS 112	–	*104*	*100*	*801*	*623*
of which: Performing residential mortgages, of which:	–	*651*	*559*	*25,295*	*18,507*
With a risk weight equal to 35% under APS 112	–	*165*	*177*	*20,148*	*13,698*
Other assets:	1,683	440	46	536	2,369
*of which: Assets posted as initial margin for derivative contracts and contributions to default funds of central counterparties (**CCPs**)*	*n/a*	–	–	*1*	*1*
of which: NSFR derivative assets	*n/a*	–	–	*16*	*16*
of which: NSFR derivative liabilities before deduction of variation margin posted	*n/a*	–	–	*59*	*59*
of which: All other assets not included in the above categories	*1,683*	*440*	*46*	*461*	*2,293*
Off-balance sheet items	–	–	–	3,820	188
Total RSF	n/a	n/a	n/a	n/a	**32,477**
Net Stable Funding Ratio (%)	n/a	n/a	n/a	n/a	**112%**

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5.11 NET STABLE FUNDING RATIO (CONTINUED)

MAY 2018	Unweighted value by residual maturity				
	No maturity	< 6 months	6 months to < 1 year	> 1 year	Weighted value
AVAILABLE STABLE FUNDING (ASF) ITEM					
Capital	3,986	–	–	850	4,746
of which: Regulatory capital	*3,986*	–	–	*850*	*4,746*
Retail deposits and deposits from small business customers	13,527	8,401	–	–	20,192
of which: Stable deposits	*6,537*	*2,588*	–	–	*8,669*
of which: Less stable deposits	*6,990*	*5,813*	–	–	*11,523*
Wholesale funding	1,677	13,957	1,078	5,551	10,526
of which: Other wholesale funding	*1,677*	*13,957*	*1,078*	*5,551*	*10,526*
Other liabilities	766	68	–	75	75
of which: NSFR derivative liabilities	*n/a*	*57*	–	–	*n/a*
of which: All other liabilities and equity not included in the above categories	*766*	*11*	–	*75*	*75*
Total ASF	n/a	n/a	n/a	n/a	**35,539**
REQUIRED STABLE FUNDING (RSF) ITEM					
Total NSFR (HQLA)	n/a	n/a	n/a	n/a	152
ALA	n/a	n/a	n/a	n/a	320
Deposits held at other financial institutions for operational purposes	379	–	–	–	320
Performing loans and securities	–	3,590	2,180	34,959	28,811
of which: Performing loans to financial institutions secured by Level 1 HQLA	–	*501*	–	–	*50*
of which: Performing loans to financial institutions secured by non-Level 1 HQLA and unsecured performing loans to financial institutions	–	*312*	–	*134*	*180*
*of which: Performing loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns, central banks and public sector entities (**PSEs**) of which:*	–	*2,143*	*1,542*	*9,875*	*10,196*
With a risk weight of less than or equal to 35% under APS 112	–	*97*	*124*	*670*	*546*
of which: Performing residential mortgages, of which:	–	*616*	*638*	*24,951*	*18,376*
With a risk weight equal to 35% under APS 112	–	*153*	*166*	*19,479*	*13,257*
of which: Securities that are not in default and do not qualify as HQLA, including exchange-traded equities	–	*18*	–	–	*9*
Other assets:	1,557	414	44	493	2,237
*of which: Assets posted as initial margin for derivative contracts and contributions to default funds of central counterparties (**CCPs**)*	*n/a*	–	–	*1*	*1*
of which: NSFR derivative assets	*n/a*	–	–	*5*	*5*
of which: NSFR derivative liabilities before deduction of variation margin posted	*n/a*	–	–	*56*	*56*
of which: All other assets not included in the above categories	*1,557*	*414*	*44*	*431*	*2,175*
Off-balance sheet items	–	–	–	3,274	167
Total RSF	n/a	n/a	n/a	n/a	**32,007**
Net Stable Funding Ratio (%)	n/a	n/a	n/a	n/a	**111%**

REMUNERATION REPORT

For the year ended 31 August 2018

CONTENTS

Dear Shareholder,

Introduction

On behalf of the BOQ Board I am pleased to present the FY2018 Remuneration Report to shareholders.

During the past year we have again met a number of shareholders and proxy advisors to hear and understand your views. The feedback is welcomed. The revised report format adopted last year has been well received and we have retained the same format for the 2018 report with the addition of a section covering changes to remuneration arrangements for FY18/FY19.

The core of our remuneration practice and outcomes is included in the first part of the report and in the second part we have included further detail and information required by the regulators and legislation under which we operate.

Changes to our 2018 Remuneration Framework

Over the past twelve months we have been working to ensure early implementation of both the Sedgwick Report recommendations and the Banking Executive Accountability Regime (**BEAR**). In 2018 we have:

- Extended the Key Management Personnel (**KMP**) short term incentive (**STI**) deferral period from two to three years.
- Extended the performance period under the KMP long term Incentive (**LTI**) program from three to four years.
- Established a range for the allocation of performance award rights (**PAR**s) as part of the LTI. Previously these have been allocated at 100 per cent of fixed remuneration where there is now a range of 80 per cent to 120 per cent. The 2018 allocations range between 95 per cent and 105 per cent of fixed remuneration.
- Removed commission incentives in the BOQ owned retail network and substantially modified the Owner Manager Branch Scorecard.

2018 Remuneration Outcomes

No KMP will receive fixed remuneration increases for the 2019 year. The Board will not be receiving an increase in fees nor requesting shareholder approval for any increase in the fee pool. The last increases in KMP fixed remuneration occured in FY16. Non-executive director fees were last increased in FY14.

Within the operation of the BOQ STI scheme the Board considers items which may be regarded as one off. In previous years, we have allowed and not allowed adjustments in determining remuneration outcomes for profit-related Key Performance Indicators (KPI). In 2018, the Board used the published cash net profit after tax for the purposes of calculating the STI under the Bank's schemes.

In considering the STI pools for the bank as a whole and the KMP, the Board have reviewed the outcomes from the STI scheme based on the Group metrics set at the beginning of the year. Group performance was assessed as being between Threshold and Performing and individual KMP performance was assessed within the Performing range.

Further the Board discussed use of its overlay which provides a review of performance with the benefit of hindsight and to consider factors relevant to performance which could not have been contemplated when the KPIs were set prior to the beginning of the 2018 financial year. In this regard our discussions included:

- Broader risk and customer outcomes
- Further strengthening of risk systems and processes
- The quality of strategy work undertaken during the year
- Progress on significant projects
- One year comparative TSR
- Various regulatory and sector reviews together with changing community expectations.

In applying its judgement, the Board reduced the individual KMP outcomes calculated under the STI scheme by an average of five per cent. The total KMP STI pool reduced by 32 per cent in comparison with the previous year, the lowest level in the past five years. After allowing for the reduction in the number of KMPs, the STI pool reduced by 21 per cent. The bank wide STI pool was approximately 16 per cent less than last year.

LTI awards are made on the basis of retention, potential and performance. These have been made at an average of approximately 100 per cent of fixed remuneration. The LTI awards are made on a face value basis. LTI grants made in 2014 were tested in December 2017. The 2014 grants achieved a vesting rate of 55 per cent based on relative TSR performance over the three year performance cycle.

Overall the Board views 2018 as a challenging year characterised

REMUNERATION REPORT

For the year ended 31 August 2018

by low growth, the impact of the Royal Commission on the sector, increased competition and increasing regulation balanced by improving internal risk systems, continued focus on customer outcomes and significant progress on strategy.

Governance and Remuneration

For the 2018 year we have ensured that the performance measures and overlay considerations of risk and outcomes for customers are more explicit in the manner they are reported, considered, discussed and the impact they have on remuneration outcomes.

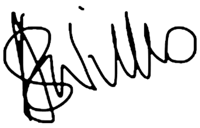
Remuneration outcomes have been discussed with the Chief Risk Officer and the Chair of the Risk Committee with positive or negative adjustments for behaviours which add to or detract from stakeholders interests.

Conclusion

The BOQ Board remains committed to continuous improvement of its remuneration governance. We seek and receive feedback from all stakeholders. Additionally we closely review developments via the regulators and several inquiries underway or completed. With this input we seek to balance the interests of our BOQ stakeholders.

In light of the outcomes from our remuneration process including the overlay it is the Board's view that the 2018 remuneration is appropriate.

Yours sincerely,



David Willis
Chairman, BOQ Human Resources and Remuneration Committee

REMUNERATION REPORT

For the year ended 31 August 2018

EXECUTIVE SUMMARY

This Remuneration Report has been prepared for consideration by shareholders at the 2018 Annual General Meeting (**AGM**) of the Bank. It outlines the overall remuneration strategy, framework and practices adopted by the Consolidated Entity for the period 1 September 2017 to 31 August 2018. It has been prepared in accordance with Section 300A of the *Corporations Act 2001*. The following Executive Summary captures key highlights for the year.

BOQ Strategic Pillars	**Customer in Charge** Placing the customer in charge of their banking and delivering exceptional outcomes	**Grow the Right Way** Achieving the right balance between risk and return for all stakeholders	**There's Always a Better Way** Pursuit of operational efficiency	**Loved Like No Other** Developing a culture of passion, excellence, fairness, equity and safety
How we performed against our strategy	Continued growth of the Virgin Money product suite. Improved customer digital offerings across BOQ brands. Customer Advocate team implemented to respond to customer issues and resolve complaints. Continued roll out of a business wide customer service program, "Heart Beat".	Continued asset growth across all areas of the business with a focus on credit quality. Cautious lending approach applied over the past few years has contributed to the ongoing quality of the asset portfolio.	Continued implementation of IT infrastructure upgrades for improved performance and efficiency. Consolidation of operational support areas resulting in streamlined processes, cost efficiencies and improved customer responsiveness.	Diversity and Inclusion strategy launched via 'One BOQ' and Reconciliation Action Plan implemented. Number of women in senior leadership roles increased. Gender pay audit undertaken and gaps for similar roles addressed. Continued focus on BOQ values.

What did this deliver to executives?

Group Executive KPIs are aligned to delivery of the strategy. For FY18 the Group Performance Indicators included specific metrics focused on Customer and People & Culture with shared accountability to achieve improvement across the Group. These were in addition to the growth, return, liquidity, risk and productivity metrics updated for FY18.

Overall performance across the Group metrics was within the Threshold to Performing range. Performance against the Cash net profit after tax (**NPAT**), return on equity and people & culture metrics was just below the Performing target range. Risk, liquidity and customer metrics were between Performing and Superior. The productivity metric, measured by cost to income, generated a result below Threshold. This latter result was due to a combination of market conditions affecting overall income, higher costs due to the investment in information technology and higher employee costs. Performance against Group metrics is discussed in more detail at Section 3.3.

Individual performance ratings were within the Performing range and reflected delivery of key strategic, financial and operational outcomes at a divisional level.

The total cost of KMP STI reduced by 32 per cent. In part this was due to a reduced number of eligible KMP. On a like for like basis total STI awarded to KMP decreased by 21 per cent compared to FY17.

LTI grants made in 2014 were tested in December 2017. The 2014 grants achieved a vesting rate of 55 per cent based on relative TSR performance over the three year performance cycle.

REMUNERATION REPORT

For the year ended 31 August 2018

How executives' interests align with stakeholders	Group metrics within the STI plan are aligned to shareholder and other stakeholders' interests. Specifically Cash NPAT and Return on Equity are key financial measures. Prudent management of credit risk, as measured by loan impairment expense to gross loans and advances is a key indicator of asset quality. The customer satisfaction metric shared by Group Executives ensures a direct focus on outcomes for customers and the communities with whom we interact. People & Culture metrics include diversity targets and employee engagement demonstrating the importance of a committed workforce that is representative of the customers and communities we serve. The STI rewards a participant's achievement against a Group scorecard moderated by an assessment of the individual's performance and then subject to the Board's overlay. The STI awarded each year varies to reflect performance. The STI earned by Group Executives is subject to deferral of 50 per cent of the amount awarded. Deferred awards vest over three years and are subject to clawback. This ensures Group Executives are accountable for the quality of results over the medium term and their behaviours remain consistent with BOQ values. Over the longer term, the award of LTI with relative EPS and TSR performance hurdles ensures alignment with shareholder interests.
How we remain competitive in attracting and retaining management talent	During 2018 the Managing Director and Chief Executive Officer (**MD & CEO**) made structural changes at the Group Executive level to strengthen succession within the leadership team. The role of Chief Operating Officer (**COO**) was reinstated and a number of changes were made to other KMP. This is detailed in Section 1. There were no changes to executive fixed remuneration following the Group Executive restructure. Recent KMP appointments were the Group Executive Retail and Group Executive People & Culture. The realignment of functions under the COO is improving operational efficiency, enhancing customer experience and realising efficiencies from developing digital capability. Investment continues in executive development programs to enhance capability at Group Executive and management levels below.
Emerging trends affecting remuneration	The Board has approved changes to both the LTI and the STI deferral for KMP and other Accountable Persons. In summary the vesting period for LTI grants has been extended from three to four years and the STI deferral has been extended from two years to three years. This will ensure that the plans are compliant and meet the BEAR test for mid-sized ADIs twelve months in advance of the July 2019 timing requirement. Details of the changes are outlined in Section 2.1 Remuneration Changes for FY18 and FY19. While not strictly applicable to KMP, the Board has approved enhancements to employee remuneration across the organisation which are consistent with the Sedgwick recommendations and reflective of the particular circumstances of BOQ's Owner Manager model. For our BOQ employees, we: – Removed sales commissions within our BOQ-owned retail branch network; – Are reviewing sales commissions within BOQ Business; and – Use a Balanced Scorecard with performance measures weighted at 60 per cent non-financial (customer, risk, compliance and migration to digital) and 40 per cent financial. For KMP, Group performance measures are weighted at 45 per cent non-financial and 55 per cent financial. For the Owner Manager network, this year, we substantially re-shaped the balanced scorecard applicable to payments to our Owner Managers (none of whom are BOQ employees) to better align with Sedgwick recommendations. The Board will continue to monitor the outcomes of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) and other relevant developments, in light of BOQ's particular circumstances, business model and in the interests of all stakeholders.

REMUNERATION REPORT

For the year ended 31 August 2018

1. KEY MANAGEMENT PERSONNEL (KMP)

The table below identifies Executive and Non-Executive Directors and Group Executives identified as KMP and the changes that occurred in FY18 to both Non-Executive Directors and Group Executives.

Changes to the Group Executive were announced on 10 May 2018. The purpose of the restructure was to provide greater succession depth and consolidate operations under the COO to improve support for front line employees.

There were several changes to KMP over the period.

TABLE 1 – DIRECTORS AND GROUP EXECUTIVES

Directors (Executive and Non-Executive)

Current	
Roger Davis	Chairman (Non-Executive)
Jon Sutton	Managing Director & Chief Executive Officer
Bruce Carter	Director (Non-Executive)
Richard Haire	Director (Non-Executive)
John Lorimer	Director (Non-Executive)
Warwick Negus	Director (Non-Executive)
Karen Penrose	Director (Non-Executive)
Margaret Seale	Director (Non-Executive) *Resigned 28 June 2018*
Michelle Tredenick	Director (Non-Executive)
David Willis	Director (Non-Executive)

Group Executives

Current	
Anthony Rose *(from 1 June 2018)*	Chief Operating Officer
Anthony Rose *(to 31 May 2018)* Matthew Baxby *(from 1 June 2018)*	Chief Financial Officer
Peter Deans	Chief Risk Officer
Matthew Baxby *(to 31 May 2018)* Lyn McGrath *(from 1 August 2018)*	Group Executive Retail Banking
Brendan White	Group Executive BOQ Business
Donna-Maree Vinci	Chief Digital & Information Officer
Belinda Jefferys *(to 3 April 2018)*	Group Executive People and Culture
Michelle Thomsen *(to 29 June 2018)*	General Counsel

During the relevant period Group Executives acted in the vacant roles to provide management coverage.

Robert Felix was Acting Group Executive People and Culture from 3 April 2018 and continued in this capacity until 31 August 2018. Debra Eckersley commenced in the role on 3 September 2018.

Dale Cliff was appointed as Acting General Counsel on 2 July 2018 and continued in this capacity until the date of this report. Following the Group Executive restructure the General Counsel reports to the Chief Operating Officer and will no longer be a KMP.

Mr Felix and Mr Cliff did not assume full KMP responsibility and therefore their remuneration is not disclosed.

REMUNERATION REPORT

For the year ended 31 August 2018

2. REMUNERATION STRATEGY & FRAMEWORK SUMMARY

This section provides shareholders with a view of the remuneration strategy, principles and framework covering employees within BOQ including the remuneration framework specifically applicable to KMPs. Our principles are:

- The remuneration strategy endorsed by the Board is supported by objectives and principles that are common to all employees;
- Attraction and retention of appropriately skilled and experienced executives and employees through the provision of market competitive remuneration;
- No distinction or difference in pay between genders for those that are performing the same role, other than where this is a difference as a result of performance, skill and experience;
- Provide opportunities for executives and employees to earn incentives linked to achievement of the Bank's objectives and performance, the performance of their business unit and their individual contribution over the short and long term within an appropriate risk control framework;
- Align executive and employee interests with those of the Bank's stakeholders;
- Ensure that remuneration structures and their operation encourage behaviours that are consistent with the Bank's values and deliver good customer outcomes; and
- Provide remuneration structures that remain current and keep pace with the prevailing remuneration trends, practice and governance frameworks.

2.1 REMUNERATION CHANGES FOR FY18 AND FY19

Changes to the remuneration framework covering KMP were made during FY18 to meet compliance requirements for executive remuneration under the BEAR legislation and to better align with community expectations.

Revised Group performance metrics for the STI were applied for FY18. These remain aligned to BOQ's four strategic pillars:

- Non-financial metrics related to customer, risk and people & culture were strengthened and reweighted at 15 per cent each. The people & culture metrics reference leadership, diversity and employee engagement.
- Financial metrics of Cash NPAT, ROE, retail deposits to gross loan asset and cost to income were retained with weightings adjusted.

The performance metrics for FY18 achieved an improved balance between focus on the customer, people and risk at 45 per cent and financial performance weighted at 55 per cent. The Board will continue to refine the Group performance metrics for FY19.

Changes were also made to the vesting period applied to deferred STI for KMP, delivered as Restricted Shares. The vesting period was extended from two years to three years and will be applied to grants to be made in December 2018. The result is that 50 per cent of any STI granted will be paid as cash and the remaining 50 per cent will vest progressively at 20 per cent after one year, 15 per cent after two years and 15 per cent after three years. The Restricted Shares remain subject to claw back at the Boards discretion.

The Board approved changes to the LTI PARs. This included extending the performance testing and vesting period for both the TSR and the EPS tranches from three to four years. Further, the Board approved an adjustment to the range of grants to between 80 per cent and 120 per cent of a Group Executive's fixed remuneration. The Board retains discretion to reduce the grant in any year to zero. This change was implemented for grants to be made in December 2018 and achieves BEAR legislation compliance requirements 12 months in advance of the required timeframe for non-major banks.

Under the LTI plan rules both the relative TSR and EPS tranche may vest independent of each other. The 2015 LTI grant was the first to include the additional relative EPS tranche weighted at 20 per cent. The testing process for the EPS tranche will be completed in December 2018 following the 2018 AGM. Any vesting outcomes remain subject to Board discretion.

The Board anticipates further changes to the remuneration framework in FY19 in response to the findings of the Royal Commission, changes required by regulators and consideration of market and community expectations.

REMUNERATION REPORT

For the year ended 31 August 2018

2.2 REMUNERATION FRAMEWORK SUMMARY - KMP

The remuneration structure in place for Group Executives and Responsible Persons **(RPs)** is consistent with the Consolidated Entity's Remuneration Policy and is based on a total remuneration approach, comprising an appropriate mix of fixed (salary and benefits) and variable (at-risk) pay in the form of cash and equity-based incentives.

The components of the executive remuneration structure, reflecting changes made in FY18, are set out in more detail in this section.

TABLE 2 - REMUNERATION FRAMEWORK

Component	Performance Measure	At Risk Weighting	Performance to Reward Link
Fixed Remuneration (FR) Salary & other benefits including superannuation.	Role Profile defines key result areas, skill, experience and behaviours for the role.		• Fixed remuneration determined by role and responsibility, periodically benchmarked to internal relativities and external market. Fixed remuneration reflects competence and capability of the position holder.
+			
Short Term Incentives Annual at risk remuneration consisting of 50% cash and 50% deferred equity vesting progressively over three years. Deferred STI delivered as Restricted Shares.	**STI plan gateway tests:** Earnings per Share: 90% of budgeted basic EPS; and Behavioural and Risk metrics. **Group Measures & Weighting:** Customer Satisfaction – 15% People & Culture – 15% Cash NPAT – 20% Return on Equity – 10% Risk – 15% Liquidity – 15% Cost to Income – 10% **Individual Performance Measures:** Combination of financial and non-financial metrics relevant to each division. Shared risk, culture, safety and diversity metrics are included in individual measures.	**At Performing - % of FR** MD & CEO: 90% Line Roles: 75% Functional Roles: 53% **At Maximum - % of FR** MD & CEO: 150% Line Roles: 140% Functional Roles: 100% The Individual Performance Measures act as a moderator in the plan design. The individual score complements the Group score to allow scaling across the performance range up to the maximum capped outcome. The individual score can also result in the overall STI amount being scaled down to zero.	• Gateway test allows for non-payment of awards where inappropriate behaviour occurs. • Rewards performance at Group and individual levels. • Individual performance score acts as a moderator on Group performance result. • Customer, risk and people & culture metrics provide a focus for executives on non-financial metrics. • Financial performance measures align to strategy, encourage financial performance and prudent cost management. • Division specific financial and non-financial targets aligned to delivery of business strategy. • Promotes leadership behaviours consistent with achieving the Group's long term objectives in areas including customer experience, workplace health & safety, diversity, and employee engagement. • Deferred STI is subject to clawback.
STI is calculated on the following basis: Fixed Remuneration x STI target% opportunity x Group Score x Individual Score = STI Outcome			
+			
Long Term Incentive Annual grant of equity delivered as PARs on a face value basis. Vesting period has been three years and will change to four years for the December 2018 allocation.	**Metrics:** **80% weighted to relative TSR** Comparator Group drawn from ASX 200; Reviewed annually. **20% weighted to relative EPS** EPS performance assessed on a relative basis against comparator group comprising major and regional banks. The EPS testing to determine vesting for awards from the 2015 grant will take place once all comparator companies have disclosed cash EPS performance in early December.	KMP grants of LTI can be made up to 120% of FR subject to Board discretion. Grants typically expected in a range of 80% to 120%.	• Ensures alignment to creation of long term shareholder value. • Metrics chosen as they provide a relative performance test against relevant comparator groups. • From December 2018 grants will vest over a four year period. • Minimum 50th percentile performance required to vest TSR tranche and 60th percentile for EPS tranche. • At 75th percentile performance or above the TSR tranche vests at 100%. At 90th or above percentile performance for the EPS tranche, 100% of the tranche vests. • All LTI awards yet to vest are subject to Board discretion and claw back.
=			
Total Remuneration	Market competitive remuneration, with appropriately weighted "at risk" variable components aligned to stakeholders' interests.		

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For the year ended 31 August 2018

2.3 REMUNERATION MIX

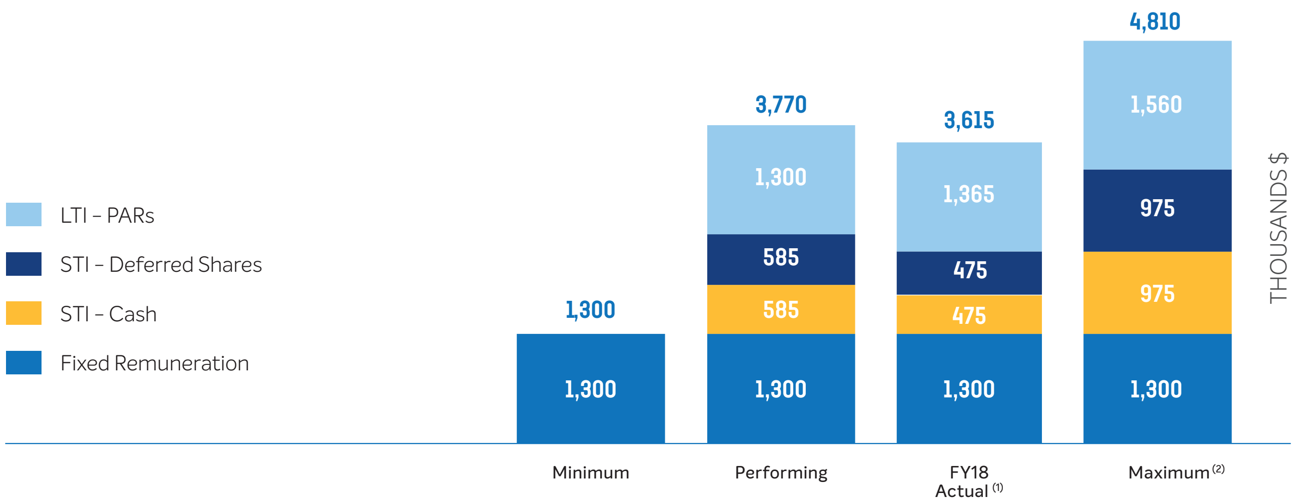
The distribution of remuneration elements for executives is designed to provide a balanced weighting between fixed, short term and long term at risk components. The change to the maximum grant of LTI from 100 per cent up to a maximum of 120 per cent of fixed remuneration affects the weighting of components if maximum awards are made. The 2018 awards are proposed to be made at 95 per cent to 105 per cent of fixed remuneration.

The remuneration mix for the MD & CEO and the Group Executives (Line and Functional) are illustrations only and are modelled based on an example of the targeted remuneration. The value ascribed for LTI (PARs) is at face value at the grant date in the current year and does not reflect the probability of vesting based on performance or the value at vesting which is determined by the future share price.

The distribution between remuneration components is assessed by the Board annually against the targeted remuneration mix. The current remuneration mix is deemed appropriately weighted.

The FY18 actual remuneration for the MD & CEO is included in the graph below for reference. The FY18 actual remuneration includes the 2018 proposed LTI grant which is awarded at face value, is conditional over four years and may or may not vest in full or in part. Actual total reward value earned in 2018 is set out in Table 7.

Figure 2.3.1 - CEO Remuneration: FY18 Potential vs Actuals

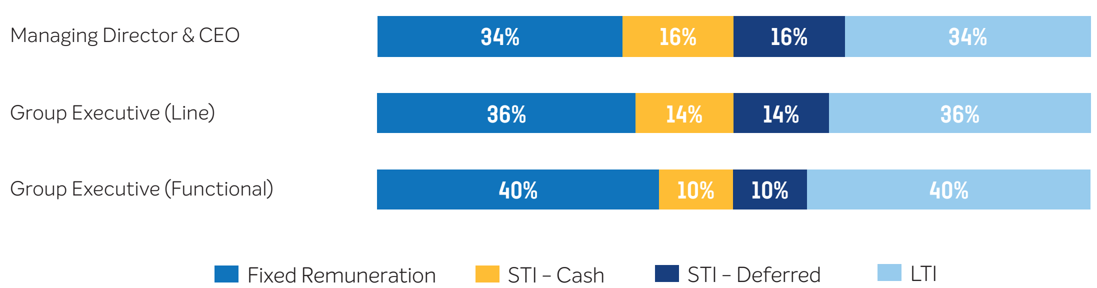


(1) For FY18 Actual column $950,000 STI and 105% LTI.

(2) For Maximum column 120% LTI and maximum STI at 150% of fixed remuneration.

The targeted remuneration mix at the Performing level for the Group Executive, distinguishing between line (Group Executives Retail and Business) and functional roles, are provided in the illustration below. The various components of fixed and variable remuneration are expressed as a percentage of total reward. Unlike the table above, the illustration does not reflect actual remuneration awarded in FY18.

Figure 2.3.2 - Remuneration Mix (at Performing level)



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3. REMUNERATION OUTCOMES

Linking company performance to remuneration outcomes is a key reward principle of BOQ. The following narrative and tables illustrate how the remuneration outcomes for FY18, including those that are cash and equity based, operate in alignment with company performance and stakeholder interests.

3.1 FIXED REMUNERATION CHANGES FY18

Fixed remuneration for all KMP remained unchanged in FY18. The fixed remuneration for newly appointed Group Executive Retail and Group Executive People and Culture was in line with market benchmark data. No adjustment was made to fixed remuneration of the executive appointed as COO.

3.2 LINKING PERFORMANCE & REWARD OUTCOMES – VARIABLE REMUNERATION

Performance at the Group level is a key determinant of the variable reward components and is a critical indicator of shareholder value creation. The table below provides a summary of key business performance metrics over the past five years.

TABLE 3 – CONSOLIDATED ENTITY PERFORMANCE

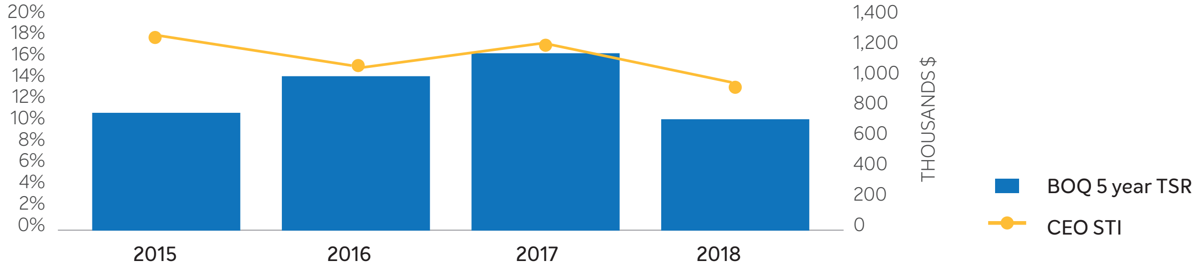
5 Year Company Performance	2018	2017	2016	2015	2014
Statutory NPAT	$336m	$352m	$338m	$318m	$261m
Cash NPAT (1)	$372m	$378m	$360m	$357m	$301m
Cash Basic earnings per share (**EPS**) (1)	94.7c	97.6c	95.6c	97.3c	89.5c
Cash cost to income ratio (**CTI**) (1)	47.5%	46.6%	46.8%	46.0%	43.9%
Share price at balance sheet date	$11.49	$12.59	$10.55	$12.67	$12.58
Total Shareholder Return (**TSR**)(1)	-2.7%	+26.5%	-10.7%	+6.3%	+39.2%
Value of Dividends paid	$341m	$308m	$300m	$272m	$216m
KMP STI Awarded ($m)	$2.73	$4.02	$3.55	$3.73	$3.94
KMP STI Awarded as % of Cash NPAT	0.7%	1.0%	1.0%	1.0%	1.3%

(1) Non-statutory measures are not subject to audit

The following graphs illustrate MD & CEO STI payments relative to key business performance metrics over the past four year period which is the period Mr Sutton has held the position.

Although not a metric used in determining STI outcomes, the FY18 TSR performance is considered as part of the Board discretionary overlay.
The rolling five year TSR performance updated for each period relative to MD & CEO STI outcomes are plotted on the graph below. The STI paid to the MD & CEO has tracked consistently with general trend changes in TSR performance.

Figure 3.2.1 - CEO STI vs 5 year TSR



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3.2 LINKING PERFORMANCE & REWARD OUTCOMES – VARIABLE REMUNERATION (CONTINUED)

The following graphs illustrate MD & CEO STI over the past four year period relative to the key Group metrics against which performance is measured.

Figure 3.2.2 - CEO STI vs NPAT

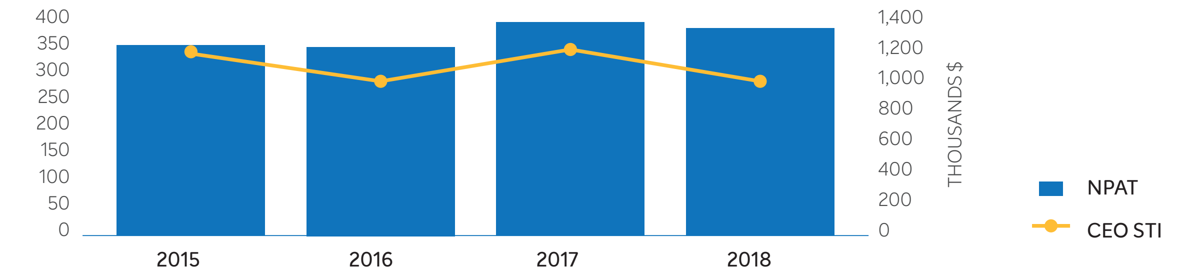


Figure 3.2.3 - CEO STI vs ROE

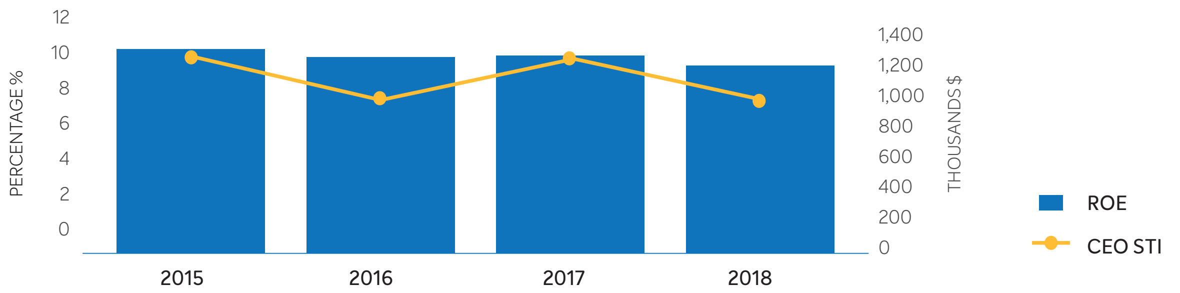


Figure 3.2.4 - CEO STI vs CTI

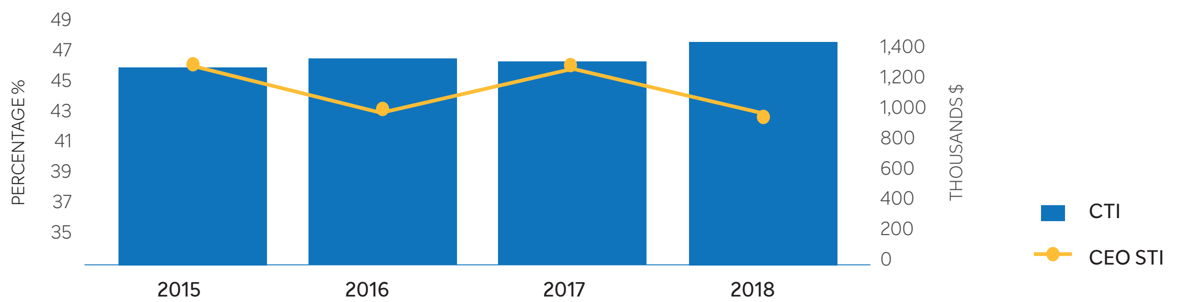
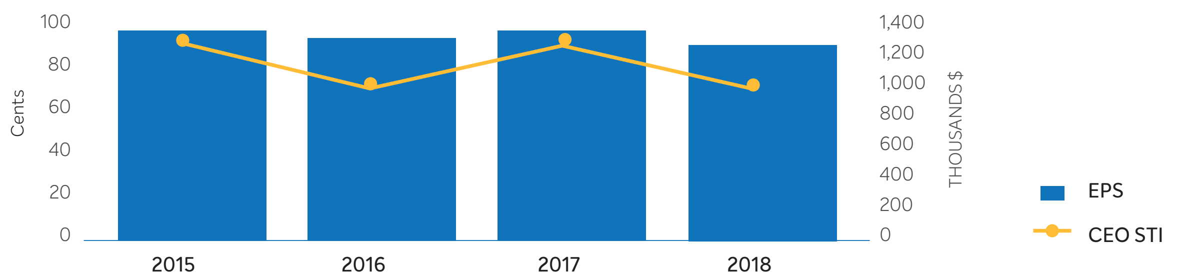


Figure 3.2.5 - CEO STI vs EPS



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For the year ended 31 August 2018

3.3 GROUP EXECUTIVE PERFORMANCE ASSESSMENT AND STI – HOW PERFORMANCE IS LINKED TO STI OUTCOMES

The Board reviewed the Consolidated Entity's performance and the performance of each Group Executive against the Group and individual performance measures.

All KMP share common Group performance metrics. The strengthening of the Customer and People metrics and re-weighting of financial and non-financial metrics were designed to broaden the measures of performance. Performance was assessed on a full year basis for Group Executives in their substantive role.

Group Executives STI is calculated on the following basis:

Assess Gateway Test Performance → Fixed Rem X STI target % opportunity × Group Performance Score × Individual Performance Score = STI Outcome (subject to Board overlay and discretion)

STI Gateway Test

The STI plan gateway tests were met for all KMP in FY18. The test requires achievement of at least 90 per cent of budgeted basic cash EPS. Basic cash EPS achieved for FY18 was 94.7 cents, which met the EPS hurdle. An additional gateway requires demonstration of appropriate risk behaviours and values. The KMP were assessed by the Human Resources and Remuneration Committee (**HRRC**) in conjunction with the Risk Committee following review of all risk issues. No STI awards are possible where the gateway tests are not met regardless of the Group or individual's performance.

Group Scorecard Outcomes

The weighting of Group metrics are designed to achieve a balance between financial performance, enhancing customer satisfaction, people, culture and prudent risk management. Performance intervals are developed across a range of outcomes.

Each metric is assessed individually and overall performance is determined by the weighted averaged outcome. STI is not awarded where overall performance is Below Threshold. STI may be earned across the performance range up to a capped maximum at Exceptional.

The performance result across Group metrics in FY18 is represented in the table below. The final weighted average result was between Threshold and Performing.

Summary of Group Performance Outcomes

TABLE 4 – GROUP PERFORMANCE OUTCOMES [1]

		Group Scorecard Outcomes FY18				
Group Performance Metric	Weighting	Below Threshold	Threshold	Performing	Superior	Exceptional
Customer Satisfaction – NPS Ranking Position in Group	15%				●	
People & Culture – Diversity and Employee Engagement	15%		●			
Cash NPAT	20%		●			
ROE	10%		●			
Risk – Loan Impairment Expense to GLA (bps)	15%					●
Retail Deposit to Lending Funding Ratio	15%				●	
CTI	10%	●				

(1) Non-statutory measures are not subject to audit

REMUNERATION REPORT

For the year ended 31 August 2018

3.3 GROUP EXECUTIVE PERFORMANCE ASSESSMENT AND STI – HOW PERFORMANCE IS LINKED TO STI OUTCOMES (CONTINUED)

The following table provides brief commentary on performance against each of the Group performance metrics.

Customer Satisfaction Position Ranking: FY18 Result Superior

This metric was included as a Group metric in FY18. BOQ improved Net Promoter Score to third against the comparator group of the Major and Regional Banks. Performance is assessed by independent survey firm RFI and the result was assessed at the Superior level.

People and Culture: FY18 Result Threshold

There were three components to this metric being leadership, diversity and employee engagement. A leadership program was developed and implemented for the top 100 executives. Representation of females in senior roles increased from 39 per cent to 41 per cent and continues to improve. Employee engagement deteriorated over the FY17 survey results. On balance the combined performance was rated at Threshold.

Cash Net Profit after Tax: FY18 Result Threshold (1)

The $372 million result was impacted by the prevailing market conditions and difficult operating environment in FY18. The result was above analysts' consensus. The performance was rated at the high end of Threshold.

Cash Return on Equity (ROE): FY18 result Threshold (1)

The cash ROE result of 9.9 per cent was just below the performing level. The result reflects the difficult operating environment and market conditions that affected financial performance during FY18. Performance was assessed as being at the high end of the Threshold range.

Loan impairment expense to GLA (bps): FY18 Result Exceptional (1)

The asset portfolio remained sound due to prudent risk settings in place since late 2012. As a result the loan impairment expense to GLA outcome of 9bps was delivered at an Exceptional level and significantly better than budget expectations.

Retail Deposit to Lending Funding Ratio: FY18 Result Superior (1)

Customer deposit growth has a significant impact on the funding of lending growth for the year. The result was positive at 69 per cent. An improvement in the mix of deposits was also evident as maturing term deposits were offset against growth in lower cost deposits. This continued to have a positive effect on the cost of funding our lending portfolio which was important given the volatility in funding markets and overall increase in costs of funds.

Cash Cost to Income Ratio: FY18 Result Below Threshold (1)

The Cost to Income ratio at 47.5 per cent was impacted by the challenging environment for revenue growth, higher employee costs, increases in amortisation costs and additional investment in IT systems and infrastructure. Investment in IT systems will yield improved customer experience and reduced IT support costs over the medium term.

(1) Non-statutory measures are not subject to audit

Individual Scorecard Outcomes

Individual performance metrics for each Group Executive are approved by the Board at the beginning of the period and aligned to delivery of Group and divisional strategy. They include a mix of financial and non-financial metrics that are specific to divisional performance.

In FY18 a number of changes were made to the Individual performance metrics. These included a reduction in the number of metrics to ensure focus on strategic issues and reduce dilution of results. All KMP had a weighting of 50 per cent of their individual metrics aligned to delivery of BOQ strategy and the adoption of a shared risk metric that reflects performance against audit, compliance and safety.

Group Executive performance is assessed for each individual metric and reviewed by the Board. The overall rating is determined by the average across all rating outcomes. This scorecard result is then applied to the weighted average Group result to determine individual Group Executive STI outcomes.

For the revenue generating divisions, metrics consist of divisional contribution to Cash NPAT, growth in deposits, customer metrics and delivery of strategic initiatives such as digital solutions, implementation of improved systems such as mortgage processing and the consolidated Customer Connect area, product enhancements and further improvements to customer contact channels.

For the non-revenue generating divisions the main focus was on developing and enhancing frameworks, improving risk management processes, compliance, efficient cost management and improving leadership and management capability.

Performance ratings for each of the Group Executives were assessed by the MD & CEO and following review by the HRRC and Board, were rated between the low and high range within the Performing level.

REMUNERATION REPORT

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3.3 GROUP EXECUTIVE PERFORMANCE ASSESSMENT AND STI – HOW PERFORMANCE IS LINKED TO STI OUTCOMES (CONTINUED)

FY18 STI Outcomes

Where individual performance is assessed as Below Threshold, no STI is paid even where the Group performance result may have triggered a positive outcome.

Applying the STI calculation method based on Group and individual performance results and following the overlay applied by the Board, Group Executive STI payments were at between 41 per cent and 52 per cent of KMP's maximum STI opportunity. This was 10 per cent to 15 per cent lower relative to maximum STI, year on year, as noted in the table below.

KMP that resigned during the period were not eligible to receive a pro-rated STI.

STI amounts of $100,000 or greater are subject to 50 per cent deferral as Restricted Shares vesting progressively over three years. The Board approved an extension to the vesting period from two years to three years to be applied to the FY18 STI deferral. Deferred STI awards are subject to forfeiture and claw back under certain conditions and at Board discretion.

The table below shows STI amounts awarded in FY17 and FY18 for comparative purposes and represents STI as a percentage of maximum STI opportunity.

TABLE 5 – COMPARISON OF STI FY17 TO FY18

Name	Position Title	FY18 Fixed Remuneration	STI % of FR at Maximum	2018 STI Awarded	2018 STI as % of Maximum	2017 STI Awarded	2017 STI as % of Maximum
Jon Sutton	Managing Director and Chief Executive Officer	1,300,000	150%	950,000	49%	1,200,000	62%
Anthony Rose	Chief Operating Officer	710,000	100%	330,000	46%	410,000	58%
Peter Deans	Chief Risk Officer	675,000	100%	330,000	49%	420,000	62%
Matt Baxby	Chief Financial Officer	655,000	140%	380,000	41%	500,000	55%
Brendan White	Group Executive BOQ Business	690,000	140%	440,000	46%	540,000	56%
Donna-Maree Vinci	Chief Digital & Information Officer	580,000	100%	300,000	52%	365,000	63%
Belinda Jefferys	Group Executive People & Culture	525,000	100%	-	-	295,000	56%
Michelle Thomsen	General Counsel	403,000	100%	-	-	205,000	51%

3.4 LTI OUTCOMES

Awards Vesting in FY18

A description of the LTI plan and performance award rights including grants, vesting arrangements and performance testing conditions is summarised in the table below.

PARs awarded to KMP in 2014 had a vesting date in December 2017 and were tested in the current period. The results of the testing and percentage of vested awards are set out in the table below.

The 2014 LTI grant had one performance hurdle being relative TSR. At the date of performance testing and at the vesting date, in order to qualify, KMP must be employed, not serving out a notice period and not subject to performance review due to any adverse risk behaviours.

The statutory tables in Section 6 set out the detail of LTI awards that vested to individual qualifying KMP during the period.

LTI TESTING OUTCOMES

Grant Date	Performance Period	Vesting Hurdle	Performance Outcome	Percentage of Award Vested
16 December 2014	8 October 2014 to 12 October 2017	TSR ranking of at least 50th percentile.	BOQ TSR achieved a ranking of 52nd percentile resulting in the awards vesting.	55%

REMUNERATION REPORT

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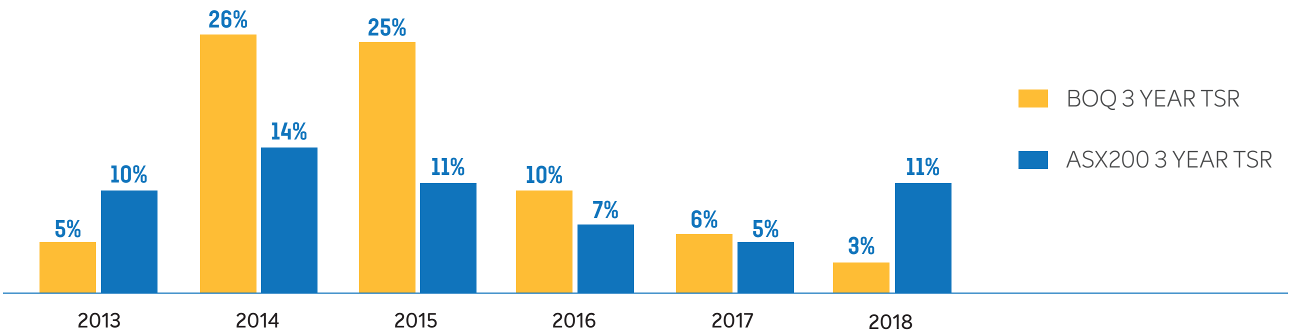
3.4 LTI OUTCOMES (CONTINUED)

The chart below demonstrates the three year rolling TSR performance for BOQ compared to the ASX200 Accumulation Index. (Note: TSRs for 2018 are as at 31 August 2018). The vesting outcome for the 2014 grants references the BOQ three year relative TSR outcome for the periods 2014 to 2017.

Figure 3.4.1 - 3 year rolling TSR: BOQ vs ASX200



LTI Grants Awarded for FY18

The Board determined that an LTI grant will be awarded for the current period in December 2018, noting that awards for the MD & CEO are subject to shareholder approval at the 2018 AGM.

These awards will be subject to changes to the vesting period from three years to four years.

The table below summarises LTI grants (PARs) proposed for 2018. Grants are subject to the vesting period, performance testing and are made at face value. The Board approved an extension to the maximum LTI awards up to 120 per cent of fixed remuneration from 2018 within a nominal range of 80 per cent to 120 per cent. Grants for 2018 are within a range of 95 per cent to 105 per cent.

TABLE 6– LTI GRANTS FOR FY18

Name	Fixed Rem $	LTI% of Fixed Remuneration	LTI Grant at Face Value $
Jon Sutton	1,300,000	105	1,365,000
Anthony Rose	710,000	100	710,000
Peter Deans	675,000	95	641,250
Matt Baxby	655,000	100	655,000
Brendan White	690,000	105	724,500
Donna-Maree Vinci	580,000	105	609,000
Lyn McGrath	635,000	100	635,000
Debra Eckersley	525,000	100	525,000

LTI grants for Lyn McGrath and Debra Eckersley are consistent with executive service agreements, provide for executive retention and are conditional over the four year vesting period.

PARs are granted at face value with the number of rights determined by applying a five day volume weighted average price (**VWAP**) commencing on the day following announcement of full year results. The table below sets out the dates, performance period and tranche weighting for the 2018 grant. The actual grant date allows for the completion of the offer period and acceptance following approval at the AGM.

Proposed Grant Date	Performance Period	Tranche %	Performance Hurdle Description
11 December 2018	4 years	TSR 80%	BOQ relative TSR ranking at or above 50th percentile triggers 50 per cent vesting of the award tranche. Relative TSR ranking at or above the 75th percentile triggers 100 per cent vesting of the award tranche.
		EPS 20%	BOQ relative EPS ranking at or above the 60th percentile triggers 50 per cent vesting of the award tranche. Relative EPS ranking at or above the 90th percentile triggers 100 per cent vesting of the award tranche.

REMUNERATION REPORT

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3.5 SUMMARY OF KMP TOTAL REWARD (NON-STATUTORY REMUNERATION) OUTCOMES FOR FY18

The table below provides an overall summary of remuneration earned and paid to KMP over the period to 31 August 2018 and consolidates the information referenced earlier in the report. The amounts for Group Executive People & Culture and the General Counsel are pro-rated for service during the period.

This is a non-statutory table and does not contain detail of FY18 LTI grants.

TABLE 7 - GROUP EXECUTIVE NON-STATUTORY REMUNERATION

Position Title	2018 Base plus Super (1) $	Value of Benefits (2) $	FY18 STI Cash (3) $	FY18 STI Deferred (4) $	Total Value STI $	FY18 Total Cash Payments (5) $	Value of Deferred Equity Vested in Period (6) $	Value of LTI Vested in Period (7) $	Total Reward Value in Period $
Managing Director and Chief Executive Officer	1,295,135	70,477	475,000	475,000	950,000	1,770,135	578,495	425,201	2,773,831
Chief Operating Officer	707,395	–	165,000	165,000	330,000	872,395	221,845	379,641	1,473,881
Chief Risk Officer	669,318	49,808	165,000	165,000	330,000	834,318	221,845	394,828	1,450,991
Chief Financial Officer	652,606	–	190,000	190,000	380,000	842,606	248,844	318,908	1,410,358
Group Executive BOQ Business	687,472	20,669	220,000	220,000	440,000	907,472	284,583	364,454	1,556,509
Chief Digital & Information Officer	571,458	47,803	150,000	150,000	300,000	721,458	96,633	–	818,091
Group Executive People and Culture (8)	334,966	15,185	–	–	–	334,966	41,206	–	376,172
General Counsel (9)	379,455	–	–	–	–	379,455	93,674	–	473,129
Group Executive Retail Banking (10)	56,252	1,722	–	–	–	56,252	–	–	56,252

Additional Information – Non-Statutory Remuneration Methodology:

(1) Base remuneration and superannuation make up a Group Executive's fixed remuneration.
(2) Relates to parking and accommodation benefits, not included in total cash payments.
(3) This is 50% of the 2018 STI for performance during FY18 (payable November 2018).
(4) This represents 50% of the 2018 STI award that is deferred until 1 October 2019 (20%), 1 October 2020 (15%) and 1 October 2021 (15%). The deferred awards are subject to Board review at the time of payment and are deferred into restricted shares subject to vesting conditions.
(5) This is the total $ value of cash STI, base and superannuation relating to 2018.
(6) The value of all deferred cash and /or equity awards (closing share price on vesting date) that vested during FY18. This excludes deferred equity awards granted in previous years which have not vested in FY18.
(7) This relates to PARs that vested during the financial year (closing share price on vesting date).
(8) To 3 April 2018.
(9) To 29 June 2018.
(10) Pro-rated from 1 August 2018.

REMUNERATION REPORT

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4. REMUNERATION GOVERNANCE

Remuneration is governed by principles, policy and oversight of the HRRC in accordance with its charter and on behalf of the Board. The HRRC and Board may exercise discretion in accordance with parameters described below.

The remuneration strategy and the principles adopted in support of remuneration governance are described in Section 2 on page 65. In accordance with its charter the remuneration policy was updated during the period and was reviewed for regulatory compliance by external legal experts prior to Board approval. We will continue to consider strategy and policy as part of our annual review of remuneration effectiveness and the changing regulatory and external environment.

The Chair of the Risk Committee submitted and then presented a report to the HRRC for consideration in assessing executive performance in FY18. The Board reviewed and approved all KMP remuneration for FY18.

4.1 REMUNERATION PRINCIPLES

- Total reward is linked to performance and reflects stakeholder interests;
- Fixed and total remuneration for each KMP is periodically benchmarked to the market;
- Key performance measures apply to all executives, covering both financial and non-financial categories and targets;
- The Bank's LTI is awarded on the basis of a volume-weighted average share price (face value) and not a risk adjusted value (fair value);
- Total remuneration for KMP is targeted to achieve a balanced mix between fixed, short term and long term variable at risk remuneration;
- Variable remuneration is capped and subject to deferral and/or claw back of unvested short term deferred and long term incentives (LTI);
- Cash payments are not made to executives on joining BOQ; and
- The Board has discretion on all remuneration outcomes.

4.2 HRRC CHARTER

Under the Consolidated Entity's HRRC charter, the Committee undertakes to conduct regular reviews and provide advice to the Board on the following:

- Review the Consolidated Entity's Remuneration Policy, at least on a biennial basis, to ensure compliance with the Consolidated Entity's objectives including the risk management framework and reflect changes in the regulatory environment;
- Provide recommendations to the Board on remuneration, recruitment, succession, retention and termination policies for Group Executives;
- Undertake an annual review of the individual remuneration arrangements for Group Executives (i.e. MD & CEO) and his direct reports) and all other Responsible Persons (as defined by the APRA Prudential Standard CPS 520 *Fit and Proper*) and provide annual recommendations to the Board;
- Review and provide annual recommendations to the Board on the remuneration principles for employees in Group Risk, Finance and Legal and recommendations on the remuneration for all remaining groups of employees not otherwise specified; and
- Consider and recommend Non-Executive Director (NED) remuneration, including ensuring that the structure of NED remuneration is clearly distinguished from that of Group Executives.

Where necessary, the Board seeks advice from independent experts and advisors, including remuneration consultants. The remuneration consultants are engaged by the HRRC which ensures, upon engagement, that an appropriate level of independence exists from the Consolidated Entity's Management. Reports provided by independent consultants are submitted directly to the Chairman of the HRRC. Where the consultant's engagement requires a recommendation, this is discussed directly with the Chairman in accordance with the requirements of the *Corporations Act 2001*.

4.3 BOARD DISCRETION

Group Executives remuneration is determined by the remuneration strategy, policy and programs such as STI and LTI. Remuneration outcomes are assessed against a range of performance measures and awarded in accordance with the plan design and plan rules.

The Board and HRRC recognise that there are a number of factors which are specific to the current year and may be taken into account when considering the overall remuneration outcomes. To account for these factors, the HRRC and Board make discretionary adjustments to the outcomes for Group Executives that may impact their remuneration negatively or positively.

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For the year ended 31 August 2018

4.3 BOARD DISCRETION (CONTINUED)

Through this process, remuneration outcomes have been adjusted both positively and negatively in past periods.

Criteria used by the HRRC to apply discretionary adjustments include:

- Factors either not known or relevant at the beginning of a financial year, which can impact performance positively or negatively during the course of the financial year;
- The degree of 'stretch' implicit in the measures and targets and the environment and market context in which the targets were set;
- Whether the operating environment during the financial year was materially different than forecast and consensus;
- Comparison between the performance of the Group and its competitors;
- The emergence of any major positive or negative risk or reputational issues;
- The quality of the financial result as shown by its composition and consistency;
- Whether leadership behaviours and BOQ values have been consistently demonstrated throughout the year; and
- Any other matters that the Board and the HRRC deem to be relevant and which are not outlined above.

In assessing final performance, STI outcomes and LTI grants for the period, the Board applied an overlay that reduced STI amounts below the calculated outcome and 21 per cent lower than FY17.

4.4 CLAWBACK OF DEFERRED STI AND LTI

Each of the variable remuneration programs including STI, STI deferral and LTI are governed by plan rules reviewed prior to each grant.

Group Executives are not eligible to receive STI if they are terminated for misconduct or poor performance, however the Board has discretion to consider a pro-rated STI in circumstances where they meet the "good leaver" definition, usually in the case of redundancy, retirement or death in service.

Clawback of unvested equity awards, either deferred STI or LTI is set out in plan rules. In circumstances where it becomes evident that there was a material misstatement of financial results or serious misconduct by an individual where this may result in reputational damage to the Bank, the Board can exercise discretion to reduce or forfeit (clawback) a pro-rated amount or the full value of any unvested awards.

4.5 EXECUTIVE CONTRACTS

The remuneration and terms of Group Executives are formalised in their employment agreements. Each of these employment agreements provide for the payment of fixed and performance-based variable remuneration, superannuation and other benefits such as statutory leave entitlements. Employment terms are governed by Executive Service Agreements as set out in the table below.

TABLE 8 - GROUP EXECUTIVE NOTICE PERIODS

Position Title	Notice Period by Executive	Employer Notice Period	Termination Payment (includes Notice Period)
Managing Director and Chief Executive Officer	9 months	9 months	No additional benefit
Chief Operating Officer	3 months	3 months	6 months fixed remuneration
Group Executive Retail Banking	3 months	3 months	6 months fixed remuneration
Chief Financial Officer	3 months	3 months	6 months fixed remuneration
Group Executive BOQ Business	3 months	3 months	6 months fixed remuneration
Chief Digital & Information Officer	3 months	3 months	6 months fixed remuneration
Chief Risk Officer	3 months	3 months	3 months fixed remuneration
Group General Counsel	3 months	3 months	6 months fixed remuneration
Group Executive People and Culture	3 months	3 months	6 months fixed remuneration

New Group Executives Lyn McGrath and Debra Eckersley were appointed during FY18 on BOQ standard Executive Service Agreements.

Lyn McGrath's appointment included provision of a "make good" award of $300,000 in lieu of foregone incentives. There are conditions attached to release of this award and 50 per cent of this amount will be paid in FY19 and 50 per cent delivered as Restricted Shares subject to a further two year vesting period. In addition there is a buyout of her former employer's equity equivalent to 54,274 BOQ Restricted Shares that vest in tranches up to FY20. No payments were made to Lyn McGrath on commencement of her employment.

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5. NON-EXECUTIVE DIRECTOR REMUNERATION

5.1 FEE POOL

NED fees are determined within an aggregate fee pool limit. The pool currently stands at $2,800,000 (inclusive of superannuation) and was approved by shareholders on 30 November 2016. The fee pool allows the Board flexibility in dealing with changes to its size and composition as a means of ensuring an appropriate mix of skills and experience is represented.

5.2 REMUNERATION FRAMEWORK

NED fees are set to attract and retain individuals of appropriate calibre to the BOQ Board and Committees. Fees are reviewed annually by the HRRC having regard to periodic advice provided by independent remuneration consultants principally to ensure market comparability.

The Chairman's fee is determined independently to the fees of other Directors and are also based upon information provided periodically by independent remuneration consultants. The Chairman is not present at any discussions relating to the determination of his own remuneration.

In order to maintain independence and impartiality, NEDs do not receive any performance-related remuneration including shares, award rights or share options in addition to their prescribed fees. NEDs are not provided with retirement benefits apart from statutory superannuation.

The Board has been considering the formation of a fee sacrifice equity plan. The plan will allow Directors to prospectively nominate a percentage of their fees to acquire restricted rights on a fee sacrifice basis. Following completion of the mandatory elapsed period, rights will convert to shares that will be purchased "on market". Vested shares will be subject to a minimum disposal period.

Additionally over the past year, all Directors have been required to meet the minimum shareholding thresholds, equivalent to one times their base fees and as at balance date, all Directors were compliant. The table below sets out the current Board and Committee membership fee structure. There have been no changes to fees since FY14 and no changes proposed for FY19. Fees in the table below are exclusive of superannuation.

TABLE 9 – DIRECTORS' ANNUAL FEES [(1)]

Directors' Annual Fees	01/09/17 – 31/08/18 Chairman/Committee Chair $	01/09/17 – 31/08/18 Directors/Committee Members $
Fixed component of remuneration for Directors [(2)]	–	150,000
Chairman [(3)]	400,000	–
Additional remuneration is paid to NED for Committee work:		
St Andrews' Board of Directors [(4)]	–	45,000
Audit Committee	45,000	22,500
Risk Committee	45,000	22,500
Nomination & Governance Committee	15,000	10,000
Human Resources & Remuneration Committee	35,000	17,500
Investment Committee [(5)]	2,250	1,500
Due Diligence Committee [(5)]	2,250	1,500
Information Technology Committee	35,000	17,500

(1) Fees remain unchanged since FY14.
(2) Directors receive one fee for serving on Bank and subsidiary Committees. A separate fee is received for serving on St Andrew's Board.
(3) The Chairman receives no additional remuneration for involvement with Committees.
(4) David Willis is also a member of the St Andrew's Board of Directors.
(5) Per meeting.

6. STATUTORY TABLES

6.1 STATUTORY DISCLOSURES

The following tables include details of the nature and amount, as required by the *Corporations Act 2001*, of each major element of the remuneration of each Director and Group Executive of the Group, calculated in accordance with accounting standards.

REMUNERATION REPORT

For the year ended 31 August 2018

6.1 STATUTORY DISCLOSURES (CONTINUED)

TABLE 10 – DIRECTOR'S REMUNERATION

Details of the nature and amount of each major element of the remuneration of each Director of the Consolidated Entity are as outlined in the table below:

		Short-Term					Long-Term	Share Based Payments				
		Salary and fees $	STI at risk [1] $	Non-monetary benefits [2] $	Other short term benefits $	Total short term benefits $	Post employment [3] $	Other long term [4] $	Rights [5] $	Shares and units [6] $	Total $	Proportion of remuneration performance related %	Value of rights as proportion of remuneration %
Executive Director [7]													
Jon Sutton – Managing Director & Chief Executive Officer	2018	1,352,041	475,000	20,669	49,808	1,897,518	20,169	26,056	757,289	511,458	3,212,490	54%	24%
	2017	1,268,451	600,000	19,382	49,808	1,937,641	20,795	29,377	712,025	558,333	3,258,171	63%	22%
Non-Executive Directors – Current [7]													
Roger Davis	2018	400,000	–	–	–	400,000	20,169	–	–	–	420,169	–	–
	2017	400,000	–	–	–	400,000	21,359	–	–	–	421,359	–	–
Bruce Carter	2018	243,208	–	–	–	243,208	19,308	–	–	–	262,516	–	–
	2017	225,833	–	–	–	225,833	19,308	–	–	–	245,141	–	–
Richard Haire	2018	249,958	–	–	–	249,958	19,308	–	–	–	269,266	–	–
	2017	242,500	–	–	–	242,500	19,308	–	–	–	261,808	–	–
John Lorimer	2018	190,000	–	–	–	190,000	17,733	–	–	–	207,733	–	–
	2017	190,000	–	–	–	190,000	18,307	–	–	–	208,307	–	–
Warwick Negus	2018	165,333	–	–	–	165,333	15,849	–	–	–	181,182	–	–
	2017	145,977	–	–	–	145,977	13,440	–	–	–	159,417	–	–
Karen Penrose	2018	200,500	–	–	–	200,500	18,233	–	–	–	218,733	–	–
	2017	193,000	–	–	–	193,000	18,193	–	–	–	211,193	–	–
Michelle Tredenick	2018	235,000	–	–	–	235,000	19,616	–	–	–	254,616	–	–
	2017	235,000	–	–	–	235,000	19,616	–	–	–	254,616	–	–
David Willis	2018	263,651	–	–	–	263,651	19,616	–	–	–	283,267	–	–
	2017	260,651	–	–	–	260,651	19,667	–	–	–	280,318	–	–
Non-Executive Directors – Former [7]													
Margaret Seale [8]	2018	154,167	–	–	–	154,167	14,369	–	–	–	168,536	–	–
	2017	185,000	–	–	–	185,000	17,575	–	–	–	202,575	–	–

(1) STI at risk reflects 50 per cent of the amounts paid or accrued in respect of FY18. Refer to Section 2.2 Current Remuneration Framework for a discussion of the Bank's STI arrangements.
(2) Relates to parking expenses.
(3) This includes superannuation benefits.
(4) Comprises long service leave accrued or utilised during the financial year.
(5) The fair value of the rights is calculated at the date of grant using an industry accepted option pricing model and allocated to each reporting period evenly over the period from grant date to vesting date. The value disclosed is the portion allocated to this reporting period.
(6) Represents restricted shares awarded through deferred STI payments.
(7) The Bank has also paid insurance premiums in respect of Directors' and Officers' Liability Insurance which is not reflected in the above table as there is no appropriate basis for allocation.
(8) Resigned 28 June 2018

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6.1 STATUTORY DISCLOSURES (CONTINUED)

TABLE 11 – GROUP EXECUTIVE REMUNERATION

Details of the nature and amount of each major element of the remuneration of each Group Executive of the Consolidated Entity are as outlined in the table below:

		Short-Term					Long-Term		Share Based Payments				
		Salary and fees $	STI at risk (1) $	Non-monetary benefits (2) $	Other short term benefits $	Total short term benefits $	Post employment (3) $	Other long term (4) $	Rights (5) $	Shares and units (6) $	Total $	Proportion of remuneration performance related %	Value of rights as proportion of remuneration %
Executives – Current													
Matthew Baxby	2018	631,755	190,000	-	-	821,755	20,169	13,046	355,322	214,584	1,424,876	53%	25%
	2017	640,768	250,000	-	-	890,768	20,795	16,297	321,791	241,250	1,490,901	60%	22%
Peter Deans	2018	651,301	165,000	-	49,808	866,109	15,157	13,626	398,745	180,625	1,474,262	50%	27%
	2017	638,476	210,000	-	49,808	898,284	20,795	15,595	381,426	204,792	1,520,892	56%	25%
Lyn McGrath (7)	2018	55,211	-	1,722	-	56,933	4,880	149	-	-	61,962	-	-
Anthony Rose	2018	704,229	165,000	-	-	869,229	20,169	13,983	393,220	178,542	1,475,143	50%	27%
	2017	680,070	205,000	-	-	885,070	20,795	17,296	368,449	202,708	1,494,318	56%	25%
Donna-Maree Vinci	2018	553,101	150,000	47,803		750,904	20,169	5,242	491,008	160,625	1,427,948	63%	34%
	2017	567,989	182,500	47,598	-	798,087	20,795	4,517	361,829	146,875	1,332,103	45%	27%
Brendan White	2018	660,696	220,000	20,669	-	901,365	20,169	13,916	385,735	234,583	1,555,768	54%	25%
	2017	678,683	270,000	19,382	-	968,065	20,795	17,292	357,567	262,292	1,628,011	60%	22%
Executives – Former													
Belinda Jefferys (8)	2018	276,048	-	15,185	-	291,233	10,576	-	178,211	73,541	553,561	31%	32%
	2017	485,642	147,500	20,800	-	653,942	20,795	2,695	214,599	91,667	983,698	35%	22%
Michelle Thomsen (9)	2018	337,082	-	-	-	337,082	15,873	-	184,059	56,875	593,889	19%	31%
	2017	398,423	102,500	-	-	500,923	20,795	3,132	144,508	93,542	762,900	48%	19%

(1) STI at risk reflects 50 per cent of the amounts paid or accrued in respect of FY18. Refer to Section 2.1 Current Remuneration Framework for a discussion of the Bank's STI arrangements.
(2) Relates to accommodation and parking expenses.
(3) This includes superannuation.
(4) Comprises long service leave accrued or utilised during the financial year.
(5) The fair value of the rights is calculated at the date of grant using an industry accepted option pricing model and allocated to each reporting period evenly over the period from grant date to vesting date. The value disclosed is the portion of the fair value of the rights allocated to this reporting period.
(6) Represents restricted shares awarded through deferred STI payments.
(7) Lyn McGrath was appointed as an executive on 1 August 2018.
(8) Belinda Jeffreys ceased to be an executive on 3 April 2018.
(9) Michelle Thomsen ceased to be an executive on 29 June 2018.

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6.2 EQUITY HELD BY GROUP EXECUTIVES

The movement during FY18 in the number of rights over ordinary shares held by each Group Executive as part of their remuneration, are as follows:

TABLE 12 – MOVEMENT IN RIGHTS HELD BY GROUP EXECUTIVES DURING THE FINANCIAL YEAR 2018

					Movements during the 2018 Financial Year				
Group Executive	Type	Grant Date	Share Price at Grant Date $	Balance at 1 Sep 2017	Granted [1]	Exercised	Lapsed	Balance at 31 August 2018 [1] [2]	Vested during the Year [3] (%)
Current									
Jon Sutton	2014 PARs	16/12/2014	11.70	103,721	–	57,046	46,675	–	55%
	2015 PARs	15/12/2015	13.02	97,774	–	–	–	97,774	–
	Restricted Shares	15/12/2015	13.02	23,466	–	23,466	–	–	50%
	2016 PARs	23/12/2016	11.95	117,865	–	–	–	117,865	–
	Restricted Shares	23/12/2016	11.95	45,333	–	22,666	–	22,667	50%
	2017 PARs	13/12/2017	12.71	–	99,239	–	–	99,239	–
	Restricted Shares	13/12/2017	12.71	–	45,803	–	–	45,803	–
Matthew Baxby	2014 PARs	16/12/2014	11.70	43,563	–	23,960	19,603	–	55%
	2015 PARs	15/12/2015	13.02	44,194	–	–	–	44,194	–
	Restricted Shares	15/12/2015	13.02	9,191	–	9,191	–	–	50%
	2016 PARs	23/12/2016	11.95	54,399	–	–	–	54,399	–
	Restricted Shares	23/12/2016	11.95	21,306	–	10,653	–	10,653	50%
	2017 PARs	13/12/2017	12.71	–	50,002	–	–	50,002	–
	Restricted Shares	13/12/2017	12.71	–	19,085	–	–	19,085	–
Peter Deans	2014 PARs	16/12/2014	11.70	53,935	–	29,664	24,271	–	55%
	2015 PARs	15/12/2015	13.02	52,798	–	–	–	52,798	–
	Restricted Shares	15/12/2015	13.02	9,191	–	9,191	–	–	50%
	2016 PARs	23/12/2016	11.95	61,199	–	–	–	61,199	–
	Restricted Shares	23/12/2016	11.95	17,000	–	8,500	–	8,500	50%
	2017 PARs	13/12/2017	12.71	–	51,528	–	–	51,528	–
	Restricted Shares	13/12/2017	12.71	–	16,031	–	–	16,031	–
Anthony Rose	2014 PARs	16/12/2014	11.70	51,860	–	28,523	23,337	–	55%
	2015 PARs	15/12/2015	13.02	50,843	–	–	–	50,843	–
	Restricted shares	15/12/2015	13.02	9,191	–	9,191	–	–	50%
	2016 PARs	23/12/2016	11.95	58,932	–	–	–	58,932	–
	Restricted shares	23/12/2016	11.95	17,000	–	8,500	–	8,500	50%
	2017 PARs	13/12/2017	12.71	–	54,200	–	–	54,200	–
	Restricted shares	13/12/2017	12.71	–	15,649	–	–	15,649	–

(1) This represents the maximum number of award rights that may vest to each Executive.
(2) Balance amounts as at 31 August 2018 are unvested and not yet exercisable.
(3) Percentage of initial rights granted.

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For the year ended 31 August 2018

6.2 EQUITY HELD BY GROUP EXECUTIVES (CONTINUED)

TABLE 12 – MOVEMENT IN RIGHTS HELD BY GROUP EXECUTIVES DURING THE FINANCIAL YEAR 2018 (CONTINUED)

					Movements during the 2018 Financial Year				
Group Executive	Type	Grant Date	Share Price at Grant Date $	Balance at 1 Sep 2017	Granted (1)	Exercised	Lapsed	Balance at 31 August 2018 (1) (2)	Vested during the Year (3) (%)
Current									
Donna-Maree Vinci	2015 PARs	15/12/2015	13.02	44,585	–	–	–	44,585	–
	2016 PARs	29/02/2016	10.55	52,076	–	–	–	52,076	–
	2016 PARs	23/12/2016	11.95	51,679	–	–	–	51,679	–
	Restricted shares	23/12/2016	11.95	15,413	–	7,706	–	7,707	50%
	2017 PARs	13/12/2017	12.71	–	44,276	–	–	44,276	–
	Restricted shares	13/12/2017	12.71	–	13,932	–	–	13,932	–
Brendan White	2014 PARs	16/12/2014	11.70	49,786	–	27,382	22,404	–	55%
	2015 PARs	15/12/2015	13.02	50,061	–	–	–	50,061	–
	Restricted shares	15/12/2015	13.02	11,928	–	11,928	–	–	50%
	2016 PARs	23/12/2016	11.95	58,026	–	–	–	58,026	–
	Restricted shares	23/12/2016	11.95	21,533	–	10,766	–	10,767	50%
	2017 PARs	13/12/2017	12.71	–	52,673	–	–	52,673	–
	Restricted shares	13/12/2017	12.71	–	20,611	–	–	20,611	–
Former									
Belinda Jeffreys	2016 PARs	29/02/2016	10.55	45,681	–	–	8,819	36,862	–
	2016 PARs	23/12/2016	11.95	47,599	–	–	25,806	21,793	–
	Restricted Shares	23/12/2016	11.95	6,573	–	3,286	–	3,287	50%
	2017 PARs	13/12/2017	12.71	–	40,078	–	35,720	4,358	–
	Restricted Shares	13/12/2017	12.71	–	11,260	–	–	11,260	–
Michelle Thomsen	2015 PARs	15/12/2015	13.02	30,897	–	–	2,926	27,971	–
	Restricted shares	15/12/2015	13.02	3,617	–	3,617	–	–	50%
	2016 PARs	23/12/2016	11.95	35,813	–	–	16,397	19,416	–
	Restricted shares	23/12/2016	11.95	7,707	–	3,853	–	3,854	50%
	2017 PARs	13/12/2017	12.71	–	30,764	–	24,850	5,914	–
	Restricted shares	13/12/2017	12.71	–	7,825	–	–	7,825	–

(1) This represents the maximum number of award rights that may vest to each Executive.
(2) Balance amounts as at 31 August 2018 are unvested and not yet exercisable.
(3) Percentage of initial rights granted.

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For the year ended 31 August 2018

6.2 EQUITY HELD BY GROUP EXECUTIVES (CONTINUED)

The table below shows the total value of any rights that were granted, exercised or lapsed to Group Executives.

TABLE 13 – VALUE OF RIGHTS HELD BY GROUP EXECUTIVES DURING THE FINANCIAL YEAR 2018

Group Executive	Grant	Grant Date	Fair Value per Right at Grant Date $	Value at Grant Date (1) $	Exercise Date	Share Price at Exercise Date (2) $	Value at Exercise Date (3) $	Expiry / Lapsing Date
Current								
Jon Sutton	2012 PARs	26/02/2012	5.18	386,568	27/10/2015	13.76	1,026,868	16/12/2017
	2012 DARs	18/12/2012	6.20	43,456	05/02/2014	10.84	15,187	18/12/2017
					02/01/2015	12.20	25,657	18/12/2017
					18/12/2015	13.55	47,493	18/12/2017
	2012 PARs	18/12/2012	1.74 (4)	97,571	27/10/2015	13.76	771,592	18/12/2017
	2013 PARs	16/12/2013	7.63	459,242	24/10/2016	11.20	435,478	16/12/2018
	2013 DARs	16/12/2013	10.38	93,711	02/01/2015	12.20	22,021	16/12/2018
					18/12/2015	13.55	36,693	16/12/2018
					22/12/2016	12.00	54,180	16/12/2018
	2014 PARs	16/12/2014	6.13	635,810	27/10/2017	13.31	759,282	16/12/2019
	Restricted shares	16/12/2014	11.70	388,335	16/12/2015	13.31	220,879	16/12/2024
					16/12/2016	11.50	190,854	16/12/2024
	2015 PARs	15/12/2015	7.67	749,927	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	611,055	15/12/2016	11.50	269,859	16/12/2025
					15/12/2017	12.61	295,906	16/12/2025
	2016 PARs	23/12/2016	6.80	801,482	–	–	–	16/12/2021
	Restricted Shares	23/12/2016	11.95	541,729	15/12/2017	12.61	285,818	16/12/2026
	2017 PARs	13/12/2017	7.14	708,566	–	–	–	13/12/2022
	Restricted Shares	13/12/2017	13.10	600,019	–	–	–	13/12/2027
Matthew Baxby	2012 PARs	01/02/2012	5.18	383,134	27/10/2015	13.76	1,017,745	18/12/2017
	2012 DARs	18/12/2012	6.20	32,593	09/07/2014	12.15	12,770	18/12/2017
					30/12/2014	12.20	19,239	18/12/2017
					31/12/2015	13.94	36,648	18/12/2017
	2012 PARs	18/12/2012	1.74 (4)	73,177	27/10/2015	13.76	578,691	18/12/2017
	2013 PARs	16/12/2013	7.63	344,433	24/10/2016	11.20	326,603	16/12/2018
	2013 DARs	16/12/2013	10.38	52,720	30/12/2014	12.20	12,383	16/12/2018
					31/12/2015	13.94	21,231	16/12/2018
					27/01/2017	12.21	31,026	16/12/2018
	2014 PARs	16/12/2014	6.13	267,041	29/10/17	13.47	322,741	16/12/2019
	Restricted shares	16/12/2014	11.70	266,982	16/12/2015	13.31	151,854	16/12/2024
					16/12/2016	11.50	131,215	16/12/2024

(1) Represents rights held at 1 September 2017 or granted during FY18.
(2) Closing share price on exercise date of rights that have a nil exercise price.
(3) Closing share price on exercise date multiplied by the number of rights exercised during the year.
(4) The fair value as based on a valuation period from 18 October 2012 to grant date. The Bank's total shareholder return over this period was below the peer group, decreasing the vesting probability and reducing the fair value calculation.

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6.2 EQUITY HELD BY GROUP EXECUTIVES (CONTINUED)

TABLE 13 – VALUE OF RIGHTS HELD BY GROUP EXECUTIVES DURING THE FINANCIAL YEAR 2018 (CONTINUED)

Group Executive	Grant	Grant Date	Fair Value per Right at Grant Date $	Value at Grant Date (1) $	Exercise Date	Share Price at Exercise Date (2) $	Value at Exercise Date (3) $	Expiry / Lapsing Date
Current								
Matthew Baxby (continued)	2015 PARs	15/12/2015	7.67	338,968	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	239,334	15/12/2016	11.50	105,697	16/12/2025
					15/12/2017	12.61	115,899	16/12/2025
	2016 PARs	23/12/2016	6.80	369,913	–	–	–	16/12/2021
	Restricted Shares	23/12/2016	11.95	254,607	15/12/2017	12.61	134,334	16/12/2026
	2017 PARs	13/12/2017	7.14	357,014				13/12/2022
	Restricted Shares	13/12/2017	13.10	250,014				13/12/2027
Peter Deans	2012 PARs	10/05/2012	3.70	255,526	27/10/2015	13.76	950,279	16/12/2017
	2012 DARs	18/12/2012	6.20	38,273	30/10/2014	12.66	15,622	18/12/2017
					28/01/2015	12.37	22,909	18/12/2017
					18/12/2015	13.55	41,829	18/12/2017
	2012 PARs	18/12/2012	1.74 (4)	83,631	27/10/2015	13.76	661,361	18/12/2017
	2013 PARs	16/12/2013	7.63	393,639	24/10/2016	11.20	373,262	16/12/2018
	2013 DARs	16/12/2013	10.38	60,246	28/01/2015	12.37	14,349	16/12/2018
					18/12/2015	13.55	23,591	16/12/2018
					27/12/2016	11.95	34,691	16/12/2018
	2014 PARs	16/12/2014	6.13	330,622	28/10/2017	13.31	394,828	16/12/2019
	Restricted shares	16/12/2014	11.70	242,705	16/12/2015	13.31	138,051	16/12/2024
					16/12/2016	11.50	119,278	16/12/2024
	2015 PARs	15/12/2015	7.67	404,961	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	239,334	15/12/2016	11.50	105,697	16/12/2025
					15/12/2017	12.61	115,899	16/12/2025
	2016 PARs	23/12/2016	6.80	416,153	–	–	–	16/12/2021
	Restricted Shares	23/12/2016	11.95	203,150	15/12/2017	12.61	107,185	16/12/2026
	2017 PARs	13/12/2017	7.14	367,910				13/12/2022
	Restricted Shares	13/12/2017	13.10	210,006				13/12/2027
Anthony Rose	2012 PARs	29/02/2012	5.18	388,888	27/10/2015	13.76	1,033,032	16/12/2017
	2012 DARs	18/12/2012	6.20	38,800	15/01/2014	11.89	14,874	18/12/2017
					08/01/2015	11.94	22,423	18/12/2017
					26/02/2016	10.55	33,011	18/12/2017
	2012 PARs	18/12/2012	1.74 (4)	87,117	28/10/2015	13.51	676,405	18/12/2017
	2013 PARs	16/12/2013	7.63	410,036	21/10/2016	11.14	386,736	16/12/2018

(1) Represents rights held at 1 September 2017 or granted during FY18.
(2) Closing share price on exercise date of rights that have a nil exercise price.
(3) Closing share price on exercise date multiplied by the number of rights exercised during the year.
(4) The fair value as based on a valuation period from 18 October 2012 to grant date. The Bank's total shareholder return over this period was below the peer group, decreasing the vesting probability and reducing the fair value calculation.

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6.2 EQUITY HELD BY GROUP EXECUTIVES (CONTINUED)

TABLE 13 – VALUE OF RIGHTS HELD BY GROUP EXECUTIVES DURING THE FINANCIAL YEAR 2018 (CONTINUED)

Group Executive	Grant	Grant Date	Fair Value per Right at Grant Date $	Value at Grant Date (1) $	Exercise Date	Share Price at Exercise Date (2) $	Value at Exercise Date (3) $	Expiry / Lapsing Date
Current								
Anthony Rose	2013 DARs	16/12/2013	10.38	62,757	08/01/2015	11.94	14,435	16/12/2018
					26/02/2016	10.55	19,127	16/12/2018
					09/01/2017	12.40	37,498	16/12/2018
	2014 PARs	16/12/2014	6.13	317,902	27/10/2017	13.31	379,641	16/12/2019
	Restricted shares	16/12/2014	11.70	249,982	16/12/2015	13.31	142,191	16/12/2024
					16/12/2016	11.50	122,855	16/12/2024
	2015 PARs	15/12/2015	7.67	389,966	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	239,334	15/12/2016	11.50	105,697	16/12/2025
					15/12/2017	12.61	115,899	16/12/2025
	2016 PARs	23/12/2016	6.80	400,738	–	–	–	16/12/2021
	Restricted shares	23/12/2016	11.95	203,150	15/12/2017	12.61	107,185	16/12/2026
	2017 PARs	13/12/2017	7.14	386,988	–	–	–	13/12/2022
	Restricted Shares	13/12/2017	13.10	205,002	–	–	–	13/12/2027
Donna-Maree Vinci	2015 PARs	15/12/2015	7.67	341,967	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	163,961	6/12/2016	11.33	71,345	16/12/2025
					27/07/2017	12.20	76,811	16/12/2025
	2016 PARs	29/02/2016	7.67	399,423	–	–	–	16/12/2020
	2016 PARs	23/12/2016	6.80	351,417	–	–	–	16/12/2021
	Restricted shares	23/12/2016	11.95	184,185	15/12/2017	12.61	97,173	16/12/2026
	2017 PARs	13/12/2017	7.14	316,131	–	–	–	13/12/2022
	Restricted Shares	13/12/2017	13.10	182,509	–	–	–	13/12/2027
Brendan White	2012 PARs	10/02/2012	5.18	349,526	27/10/2015	13.76	928,470	16/12/2017
	2012 DARs	18/12/2012	6.20	38,800	23/12/2014	12.08	37,798	18/12/2017
					18/12/2015	13.55	42,398	18/12/2017
	2012 PARs	18/12/2012	1.74 (4)	87,117	27/10/2015	13.76	688,922	18/12/2017
	2013 PARs	16/12/2013	7.63	393,639	24/10/2016	11.20	373,262	16/12/2018
	2013 DARs	16/12/2013	10.38	60,246	23/12/2014	12.08	14,013	16/12/2018
					18/12/2015	13.55	23,591	16/12/2018
					05/04/2017	12.12	35,184	16/12/2018
	2014 PARs	16/12/2014	6.13	305,188	2/11/2017	12.49	341,864	16/12/2019

(1) Represents rights held at 1 September 2017 or granted during FY18.

(2) Closing share price on exercise date of rights that have a nil exercise price.

(3) Closing share price on exercise date multiplied by the number of rights exercised during the year.

(4) The fair value as based on a valuation period from 18 October 2012 to grant date. The Bank's total shareholder return over this period was below the peer group, decreasing the vesting probability and reducing the fair value calculation.

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6.2 EQUITY HELD BY GROUP EXECUTIVES (CONTINUED)

TABLE 13 – VALUE OF RIGHTS HELD BY GROUP EXECUTIVES DURING THE FINANCIAL YEAR 2018 (CONTINUED)

Group Executive	Grant	Grant Date	Fair Value per Right at Grant Date $	Value at Grant Date (1) $	Exercise Date	Share Price at Exercise Date (2) $	Value at Exercise Date (3) $	Expiry / Lapsing Date
Current								
Brendan White (continued)	Restricted shares	16/12/2014	11.70	330,080	16/12/2015	13.31	187,751	16/12/2024
					16/12/2016	11.50	162,219	16/12/2024
	2015 PARs	15/12/2015	7.67	383,968	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	310,618	15/12/2016	11.50	137,184	16/12/2025
					15/12/2017	12.61	150,412	16/12/2025
	2016 PARs	23/12/2016	6.80	394,577	–	–	–	16/12/2021
	Restricted shares	23/12/2016	11.95	257,319	15/12/2017	12.61	135,759	16/12/2026
	2017 PARs	13/12/2017	7.14	376,085	–	–	–	13/12/2022
	Restricted Shares	13/12/2017	13.10	270,004	–	–	–	13/12/2027
Former								
Belinda Jefferys	2016 PARs	29/02/2016	7.67	350,373	–	–	–	16/12/2020
	Restricted shares	29/02/2016	13.02	142,738	6/12/2016	11.33	41,411	16/12/2025
					4/4/2017	12.11	44,250	16/12/2025
					27/07/2017	12.20	44,579	16/12/2025
	2016 PARs	23/12/2016	6.80	323,673	–	–	–	16/12/2021
	Restricted Shares	23/12/2016	11.95	78,547	15/12/2017	12.61	41,436	16/12/2026
	2017 PARs	13/12/2017	7.14	286,157				13/12/2022
	Restricted Shares	13/12/2017	13.10	147,506				13/12/2027
Michelle Thomsen	2015 PARs	15/12/2015	7.67	236,980	–	–	–	16/12/2020
	Restricted shares	15/12/2015	13.02	94,200	15/12/2016	11.50	41,607	16/12/2025
					15/12/2017	12.61	45,610	16/12/2025
	2016 PARs	23/12/2016	6.80	243,528	–	–	–	16/12/2021
	Restricted shares	23/12/2016	11.95	92,099	15/12/2017	12.61	48,586	16/12/2026
	2017 PARs	13/12/2017	7.14	219,655	–	–	–	13/12/2022
	Restricted Shares	13/12/2017	13.10	102,508	–	–	–	13/12/2027

(1) Represents rights held at 1 September 2017 or granted during FY18.

(2) Closing share price on exercise date of rights that have a nil exercise price.

(3) Closing share price on exercise date multiplied by the number of rights exercised during the year.

(4) The fair value as based on a valuation period from 18 October 2012 to grant date. The Bank's total shareholder return over this period was below the peer group, decreasing the vesting probability and reducing the fair value calculation.

REMUNERATION REPORT

For the year ended 31 August 2018

6.3 EQUITY INSTRUMENTS - HOLDINGS AND MOVEMENTS

Movement in shares

The number of shares held directly, indirectly or beneficially by each Director, Group Executive or related party is as follows:

Ordinary shares [(1)]	Held at 1 September 2017	Purchases / (Sales)	Received on Exercise of Award Rights / Restricted Shares	Held at 31 August 2018
Executive Director				
Jon Sutton	194,438	(120,000)	103,178	177,616
Directors - Current				
Roger Davis	18,043	–	–	18,043
Bruce Carter	17,503	–	–	17,503
Richard Haire	7,347	9,256	–	16,603
John Lorimer	12,000	5,000	–	17,000
Warwick Negus	–	15,000	–	15,000
Karen Penrose	9,500	4,091	–	13,591
Michelle Tredenick	10,635	5,000	–	15,635
David Willis	2,132	9,800	–	11,932
Directors - Former				
Margaret Seale	11,043	–	–	n/a
Executives - Current				
Matthew Baxby	61,506	–	43,804	105,310
Peter Deans	67,143	(80,472)	47,355	34,026
Donna-Maree Vinci	12,593	–	7,706	20,299
Brendan White	3,330	(50,076)	50,076	3,330
Executives - Former				
Belinda Jefferys	10,963	–	–	n/a

(1) Directors and Group Executives with nil shareholding balances as at 31 August 2018 have been excluded from the table above.

REMUNERATION REPORT

For the year ended 31 August 2018

6.4 TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL (DIRECTORS AND GROUP EXECUTIVES)

Loan transactions

Loans to KMP and their related parties (including close family members of the KMP and entities over which the KMP and/or their close family members have control, joint control or significant influence) are provided in the ordinary course of business. Normal commercial terms and conditions are applied to all loans. Any discounts provided to KMP are the same as those available to all employees of the Consolidated Entity. There have been no write downs or amounts recorded as provisions during FY18.

Details of loans held by KMP and their related parties during the financial year, where the individual's aggregate loan balance exceeded $100,000 at any time in this period, are as follows:

	Balance at 1 September 2017 $	Interest charged during the year $	**Balance at 31 August 2018 $**	Highest balance during the year $
Executives				
Matthew Baxby	1,105,970	52,544	1,106,608	1,340,430
Brendan White	341,326	19,403	789,747	793,865
Other Related Parties				
Richard Haire related parties	191,000	8,194	191,000	191,696
Jon Sutton related parties	1,296,199	49,517	1,269,422	1,295,789
Executive-Former				
Michelle Thomsen [(1)]	323,410	68,215	–	–

(1) Michelle Thomsen resigned as an Executive on 29 June 2018. On this basis, loans and advances between the Consolidated Entity and Ms Thomsen are not included in the closing balance as at 31 August 2018.

Details regarding the aggregate of loans made, guaranteed or secured by any entity in the economic entity to all Group Executives and their related parties, and the number of individuals in each group are as follows:

	Balance at 1 September 2017 $	Interest charged during the year $	**Balance at 31 August 2018 $**	Number in group at 31 August 2018 #
Executives	1,788,768	140,768	1,928,903	3
Other Related Parties	1,487,199	57,711	1,460,422	2

Other transactions

Transactions with KMP and their related parties (other than loans and shares) during the financial year were related to personal banking, investment, finance leasing, insurance policy and deposit transactions. These transactions are on normal commercial terms and conditions, in the ordinary course of business and are considered trivial or domestic in nature.

On 26 May 2015, the Bank issued 15,000 Wholesale Capital Notes [(1)] at a price of $10,000 per note.

On 28 December 2017, the Bank issued 3,500,000 million Capital Notes [(1)] at a price of $100 per note.

Details of those notes issued to BOQ Directors are set out below:

		Balance at 31 August 2018 $	Interest earned for the year $
Roger Davis	Wholesale Capital Notes	200,000	8,798
David Willis	Wholesale Capital Notes	70,000	3,079
Roger Davis	Capital Notes	50,000	1,317
Roger Davis related parties	Capital Notes	50,000	1,317
Total		**370,000**	**14,511**

(1) Capital notes are classified as non-current.

DIRECTORS' REPORT

For the year ended 31 August 2018

Indemnification of officers

The Bank's Constitution supported by a deed of indemnity provides an indemnity in favour of all officers of the Bank against liabilities incurred by them in the capacity of officer to the full extent permitted by the *Corporations Act 2001* (Cth).

Insurance of officers

Since the end of the previous financial year the Bank has paid insurance premiums in respect of a Directors' and Officers' liability insurance contract. The contract insures each person who is or has been a Director or officer (as defined in the *Corporations Act 2001* (Cth)) of the Bank against certain liabilities arising in the course of their duties to the Bank and its controlled entities. The Directors have not included details of the nature of the liabilities covered or the amount of the premium paid in respect of the insurance contract as such disclosure is prohibited under the terms of the contract.

Directors' interests

Directors' interests as at the date of this report were as follows:

	Ordinary shares	Capital Notes	Wholesale Capital Notes
Roger Davis	18,043	1,000	20
Jon Sutton	177,616	–	–
Warwick Negus	15,000	–	–
Bruce Carter	17,503	–	–
Richard Haire	16,603	–	–
John Lorimer	17,000	–	–
Karen Penrose	13,591	–	–
Michelle Tredenick	15,635	–	–
David Willis	11,932	–	7

Audit and non-audit services

During the year, KPMG, the Bank's auditor, has performed certain other services in addition to their statutory duties. The Board has considered the non-audit services provided during the year by the auditor are compatible with, and did not compromise, the auditor's independence requirements of the *Corporations Act 2001* (Cth) for the following reasons:

- all non-audit services were subject to the corporate governance procedures adopted by the Bank and have been reviewed by the Audit Committee to ensure they do not impact the integrity and objectivity of the auditor; and
- the non-audit services provided do not undermine the general principles relating to auditor's independence as set out in APES 110 *Code of Ethics for Professional Accountants*, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision making capacity for the Bank or acting as an advocate for the Bank or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Bank, KPMG and its related practices for audit and non-audit services provided during the year are set out below and in the Section 6.7 Auditor Remuneration:

	Consolidated		Bank	
KPMG AUSTRALIA	2018 $000	2017 $000	2018 $000	2017 $000
Audit services				
– Audit and review of the financial reports	1,737	1,561	1,279	1,029
– Other regulatory and audit services	346	250	244	162
	2,083	1,811	1,523	1,191
Audit-related services				
– Other assurance services	532	744	399	533
– Regulatory assurance services	235	191	235	191
	767	935	634	724
Non-audit services				
– Taxation services	171	189	171	189
– Other	103	215	103	215
	274	404	274	404

DIRECTORS' REPORT

For the year ended 31 August 2018

Lead Auditor's Independence Declaration

The lead auditor's independence declaration is set out on page 90 and forms part of the Directors' report for the year ended 31 August 2018.

Director and management changes

On 3 January 2018, Ms Belinda Jefferys, tendered her resignation from her role as Group Executive People & Culture. Ms Jefferys' last day was 3 April 2018.

Debra Eckersley has been appointed to the role of Group Executive People & Culture and started on 3 September 2018.

On 18 January 2018, Ms Michelle Thomsen stepped down from her role as Company Secretary and on 29 June 2018, from her role as General Counsel.

On 10 May 2018, BOQ announced changes to the Group executive team aimed at broadening the expertise of the leadership team.

The changes to the Group executive team were:

- Anthony Rose moved from the Chief Financial Officer role to the newly created role of Chief Operating Officer effective 14 May 2018.
- Matt Baxby moved from the Group Executive Retail Banking role and was appointed Chief Financial Officer effective 14 May 2018.
- Lyn McGrath joined BOQ on 1 August 2018 as Group Executive Retail Banking.

Non-executive director Ms Seale resigned from the BOQ Board effective 28 June 2018.

Management attestation

The Board has been provided with a written statement from the Group's Managing Director & CEO and Chief Financial Officer, confirming the accompanying financial statements and notes are in accordance with the *Corporations Act 2001* (Cth) and they present a true and fair view in all material respects of the Group's financial position and performance as at and for the year ended 31 August 2018.

The Directors' Declaration can be found on page 162 of the financial statements.

Environmental regulation

The Group's operations are not subject to any significant environmental regulations under either Commonwealth or State legislation. The Board confirms that the Group is not aware of any breach of environmental requirements.

Subsequent events

Dividends have been determined after 31 August 2018. The financial effect of the dividends has not been brought to account in the financial statements for the year ended 31 August 2018. Further details with respect to the dividend amounts per share, payment date and dividend reinvestment plan can be obtained from Section 2.4 Dividends of the consolidated financial statements.

No matters or circumstances have arisen since the end of the financial year and up until the date of this report which significantly affect the operations of the Bank, the results of those operations, or the state of affairs of the Bank in subsequent years.

Rounding of amounts

The Bank is a company of a kind referred to in ASIC Corporations Instrument 2016/191 dated 24 March 2016 and in accordance with that Instrument, amounts in this financial report and Directors' report have been rounded off to the nearest million dollars, unless otherwise stated.

Signed in accordance with a resolution of the Directors:

Roger Davis
Chairman
3 October 2018

Jon Sutton
Managing Director and CEO
3 October 2018

LEAD AUDITOR'S INDEPENDENCE DECLARATION UNDER SECTION 307C OF THE CORPORATIONS ACT 2001

To the Directors of Bank of Queensland Limited

I declare that, to the best of my knowledge and belief, in relation to the audit of Bank of Queensland Limited for the financial year ended 31 August 2018 there have been:

(i) no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* (Cth) in relation to the audit; and

(ii) no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

Robert Warren
Partner, Sydney
3 October 2018

2018 FINANCIAL STATEMENTS

INCOME STATEMENTS

For the year ended 31 August 2018

	Section	Consolidated 2018 $m	Consolidated 2017 $m	Bank 2018 $m	Bank 2017 $m
Interest income	2.1	2,069	2,046	2,049	2,015
Interest expense	2.1	(1,104)	(1,120)	(1,311)	(1,280)
Net interest income	2.1	965	926	738	735
Other operating income	2.1	137	156	228	347
Net banking operating income		1,102	1,082	966	1,082
Premiums from insurance contracts		66	68	–	–
Investment revenue		2	2	–	–
Claims and policyholder liability expense from insurance contracts		(49)	(49)	–	–
Net insurance operating income	2.1	19	21	–	–
Total operating income before impairment and operating expenses	2.1	1,121	1,103	966	1,082
Expenses	2.2	(587)	(548)	(545)	(508)
Impairment on loans and advances	3.3	(41)	(48)	(23)	(32)
Profit before income tax		493	507	398	542
Income tax expense	2.3	(157)	(155)	(121)	(126)
Profit for the year		336	352	277	416
Profit attributable to:					
Equity holders of the parent		336	352	277	416
Earnings per share					
Basic earnings per share – Ordinary shares (cents)	2.6	85.5	90.9		
Diluted earnings per share – Ordinary shares (cents)	2.6	81.2	87.8		

The Income Statements should be read in conjunction with the accompanying notes.

STATEMENTS OF COMPREHENSIVE INCOME

For the year ended 31 August 2018

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Profit for the year	336	352	277	416
Other comprehensive income, net of income tax				
Items that may be reclassified subsequently to profit or loss				
Cash flow hedges:				
Net movement taken to equity	(11)	13	(12)	19
Net movement transferred to profit and loss	22	23	22	23
Net change in fair value of financial assets available-for-sale	6	3	6	3
Net movement transferred to profit and loss for financial assets available-for-sale	(14)	(14)	(14)	(14)
Other comprehensive expense, net of income tax	3	25	2	31
Total comprehensive income for the year	339	377	279	447
Total comprehensive income attributable to:				
Equity holders of the parent	339	377	279	447

The Statements of Comprehensive Income should be read in conjunction with the accompanying notes.

BALANCE SHEETS

As at 31 August 2018

	Section	Consolidated 2018 $m	Consolidated 2017 $m	Bank 2018 $m	Bank 2017 $m
ASSETS					
Cash and cash equivalents	3.1	1,212	914	840	537
Due from other financial institutions – term deposits		6	58	6	8
Financial assets available-for-sale	3.2	3,946	3,934	3,975	4,027
Financial assets held for trading	3.2	1,385	1,837	1,385	1,837
Derivative financial assets	3.8	135	109	80	107
Loans and advances at amortised cost	3.3	45,078	43,590	40,571	39,348
Other assets		169	214	940	501
Property, plant and equipment		57	60	51	53
Assets held for sale	6.5	57	–	–	–
Shares in controlled entities	6.5	–	–	522	867
Deferred tax assets	2.3	45	55	46	52
Intangible assets	4.1	875	872	798	793
Investments in joint arrangements	6.6	15	15	–	–
Amounts due from controlled entities		–	–	272	324
Total assets		52,980	51,658	49,486	48,454
LIABILITIES					
Due to other financial institutions – accounts payable at call		315	262	315	262
Deposits	3.4	38,017	37,169	38,266	37,501
Derivative financial liabilities	3.8	294	333	293	333
Accounts payable and other liabilities		360	390	304	327
Current tax liabilities		5	7	5	6
Liabilities held for sale	6.5	22	–	–	–
Provisions	4.2	34	42	30	33
Insurance policy liabilities	5.1	–	16	–	–
Borrowings	3.5	10,077	9,651	6,503	6,230
Total liabilities		49,124	47,870	45,716	44,692
Net assets		3,856	3,788	3,770	3,762
EQUITY					
Issued capital		3,418	3,360	3,425	3,367
Reserves		38	57	42	48
Retained profits		400	371	303	347
Total equity		3,856	3,788	3,770	3,762

The Balance Sheets should be read in conjunction with the accompanying notes.

STATEMENTS OF CHANGES IN EQUITY

For the year ended 31 August 2018

Consolidated	Ordinary shares $m	Employee benefits reserve $m	Equity reserve for credit losses $m	Cashflow hedge reserve $m	Available-for-sale reserve $m	Retained profits $m	Total equity $m
YEAR ENDED 31 AUGUST 2018							
Balance at beginning of the year	3,360	26	81	(117)	67	371	3,788
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	336	336
Other comprehensive income, net of income tax:							
Cash flow hedges:							
Net movement to equity	-	-	-	(11)	-	-	(11)
Net movement transferred to profit and loss	-	-	-	22	-	-	22
Net movement in fair value of financial assets available-for-sale	-	-	-	-	6	-	6
Net movement transferred to profit and loss for financial assets available-for-sale	-	-	-	-	(14)	-	(14)
Transfer from equity reserve for credit losses	-	-	(22)	-	-	22	-
Total other comprehensive income / (expense)	-	-	(22)	11	(8)	22	3
Total comprehensive income / (expense) for the year	-	-	(22)	11	(8)	358	339
Transactions with owners, recorded directly in equity / contributions by and distributions to owners							
Issues of ordinary shares (1)	11	-	-	-	-	-	11
Dividend reinvestment plan	47	-	-	-	-	-	47
Dividends to shareholders	-	-	-	-	-	(329)	(329)
Total contributions by and distributions to owners	58	-	-	-	-	(329)	(271)
Balance at the end of the year	3,418	26	59	(106)	59	400	3,856

(1) On 26 October 2017, 850,000 ordinary shares were issued at $13.28 and on 17 May 2018 2,809 ordinary shares were issued at $10.02 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

The Statements of Changes in Equity should be read in conjunction with the accompanying notes.

STATEMENTS OF CHANGES IN EQUITY

For the Year Ended 31 August 2018

Consolidated	Ordinary shares $m	Employee benefits reserve $m	Equity reserve for credit losses $m	Cashflow hedge reserve $m	Available-for-sale reserve $m	Retained profits $m	Total equity $m
YEAR ENDED 31 AUGUST 2017							
Balance at beginning of the year	3,243	27	81	(153)	78	311	3,587
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	352	352
Other comprehensive income, net of income tax:							
Cash flow hedges:							
Net movement to equity	-	-	-	13	-	-	13
Net movement transferred to profit and loss	-	-	-	23	-	-	23
Net movement in fair value of financial assets available-for-sale	-	-	-	-	3	-	3
Net movement transferred to profit and loss for financial assets available-for-sale	-	-	-	-	(14)	-	(14)
Total other comprehensive income / (expense)	-	-	-	36	(11)	-	25
Total comprehensive income / (expense) for the year	-	-	-	36	(11)	352	377
Transactions with owners, recorded directly in equity / contributions by and distributions to owners							
Issues of ordinary shares (1)	12	-	-	-	-	-	12
Dividend reinvestment plan	105	-	-	-	-	-	105
Dividends to shareholders	-	-	-	-	-	(292)	(292)
Equity settled transactions	-	(1)	-	-	-	-	(1)
Total contributions by and distributions to owners	117	(1)	-	-	-	(292)	(176)
Balance at the end of the year	3,360	26	81	(117)	67	371	3,788

(1) On 21 October 2016, 1,050,000 ordinary shares were issued at $11.15 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

The Statements of Changes in Equity should be read in conjunction with the accompanying notes.

STATEMENTS OF CHANGES IN EQUITY

For the year ended 31 August 2018

Bank	Ordinary shares $m	Employee benefits reserve $m	Equity reserve for credit losses $m	Cashflow hedge reserve $m	Available-for-sale reserve $m	Retained profits $m	Total equity $m
YEAR ENDED 31 AUGUST 2018							
Balance at beginning of the year	3,367	26	68	(113)	67	347	3,762
Total comprehensive income for the year							
Profit for the year	–	–	–	–	–	277	277
Other comprehensive income, net of income tax:							
Cash flow hedges:							
Net movement to equity	–	–	–	(12)	–	–	(12)
Net movement transferred to profit and loss	–	–	–	22	–	–	22
Net movement in fair value of financial assets available-for-sale	–	–	–	–	6	–	6
Net movement transferred to profit and loss for financial assets available-for-sale	–	–	–	–	(14)	–	(14)
Transfer from equity reserve for credit losses	–	–	(8)	–	–	8	–
Total other comprehensive income / (expense)	–	–	(8)	10	(8)	8	2
Total comprehensive income / (expense) for the year	–	–	(8)	10	(8)	285	279
Transactions with owners, recorded directly in equity / contributions by and distributions to owners							
Issues of ordinary shares (1)	11	–	–	–	–	–	11
Dividend reinvestment plan	47	–	–	–	–	–	47
Dividends to shareholders	–	–	–	–	–	(329)	(329)
Total contributions by and distributions to owners	58	–	–	–	–	(329)	(271)
Balance at the end of the year	3.425	26	60	(103)	59	303	3,770

(1) On 26 October 2017, 850,000 ordinary shares were issued at $13.28 and on 17 May 2018 2,809 ordinary shares were issued at $10.02 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

The Statements of Changes in Equity should be read in conjunction with the accompanying notes.

STATEMENTS OF CHANGES IN EQUITY

For the Year Ended 31 August 2018

Bank	Ordinary shares $m	Employee benefits reserve $m	Equity reserve for credit losses $m	Cashflow hedge reserve $m	Available-for-sale reserve $m	Retained profits $m	Total equity $m
YEAR ENDED 31 AUGUST 2017							
Balance at beginning of the year	3,250	27	68	(155)	78	223	3,491
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	416	416
Other comprehensive income, net of income tax:							
Cash flow hedges:							
Net movement to equity	-	-	-	19	-	-	19
Net movement transferred to profit and loss	-	-	-	23	-	-	23
Net movement in fair value of financial assets available-for-sale	-	-	-	-	3	-	3
Net movement transferred to profit and loss for financial assets available-for-sale	-	-	-	-	(14)	-	(14)
Total other comprehensive income / (expense)	-	-	-	42	(11)	-	31
Total comprehensive income / (expense) for the year	-	-	-	42	(11)	416	447
Transactions with owners, recorded directly in equity / contributions by and distributions to owners							
Issues of ordinary shares (1)	12	-	-	-	-	-	12
Dividend reinvestment plan	105	-	-	-	-	-	105
Dividends to shareholders	-	-	-	-	-	(292)	(292)
Equity settled transactions	-	(1)	-	-	-	-	(1)
Total contributions by and distributions to owners	117	(1)	-	-	-	(292)	(176)
Balance at the end of the year	3,367	26	68	(113)	67	347	3,762

(1) On 21 October 2016, 1,050,000 ordinary shares were issued at $11.15 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

The Statements of Changes in Equity should be read in conjunction with the accompanying notes.

STATEMENTS OF CASH FLOWS

For the year ended 31 August 2018

	Section	Consolidated 2018 $m	Consolidated 2017 $m	Bank 2018 $m	Bank 2017 $m
CASH FLOWS FROM OPERATING ACTIVITIES					
Interest received		2,085	1,990	1,958	1,846
Fees and other income received		160	137	192	176
Dividends received		-	1	-	1
Interest paid		(1,102)	(1,066)	(1,311)	(1,225)
Cash paid to suppliers and employees		(500)	(478)	(453)	(440)
Income tax paid		(147)	(143)	(143)	(141)
		496	441	243	217
Increase in operating assets:					
Loans and advances at amortised cost		(1,529)	(699)	(1,235)	(485)
Other financial assets		449	(484)	499	(390)
Increase / (decrease) in operating liabilities:					
Deposits		901	440	808	(217)
Net cash inflow / (outflow) from operating activities	3.1	317	(302)	315	(875)
CASH FLOWS FROM INVESTING ACTIVITIES					
Payments for property, plant and equipment		(14)	(18)	(10)	(17)
Proceeds from sale of property, plant and equipment		8	13	1	1
Payments for intangible assets		(73)	(46)	(71)	(40)
Acquisition of BOQF Cashflow Finance Pty Ltd		-	(14)	-	-
Disposal of vendor finance entity, net of cash		-	19	-	-
Receipt of third party loan repayment		-	95	-	-
Net cash inflow / (outflow) from investing activities		(79)	49	(80)	(56)
CASH FLOWS FROM FINANCING ACTIVITIES					
Proceeds from borrowings	3.5	3,308	4,090	2,022	2,734
Repayments of borrowings	3.5	(2,959)	(3,963)	(1,824)	(1,788)
Proceeds from foreign exchange instruments		(1)	-	(1)	10
Net movement in other financing activities		-	-	131	(57)
Proceeds from issue of ordinary shares		11	12	11	11
Payments for treasury shares		(11)	(12)	(11)	(12)
Dividends paid		(282)	(188)	(282)	(188)
Dividends received from controlled entities		-	-	22	55
Net cash inflow / (outflow) from financing activities		66	(61)	68	765
Net increase / (decrease) in cash and cash equivalents		304	(314)	303	(166)
Cash and cash equivalents at beginning of year		914	1,228	537	703
Cash and cash equivalents at end of year (1)	3.1	1,218	914	840	537

(1) The consolidated cash and cash equivalents at end of year includes assets held for sale as outlined in Note 6.5(d). The components of cash and cash equivalents are in Note 3.1.

The Statements of Cash Flows should be read in conjunction with the accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

SECTION 1. BASIS OF PREPARATION

1.1 REPORTING ENTITY

The Bank is a for-profit company domiciled in Australia. The address of the Bank's registered office is Level 6, 100 Skyring Terrace, Newstead QLD 4006.

The consolidated financial statements of the Bank for the financial year ended 31 August 2018 comprise the Consolidated Entity and the Consolidated Entity's interest in equity accounted investments. The principal activity of the Bank is the provision of financial services to the community.

1.2 BASIS OF PREPARATION

(a) Statement of compliance

These general purpose financial statements have been prepared in accordance with Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board (**AASB**) and the *Corporations Act 2001* (Cth). The consolidated financial statements and notes thereto also comply with International Financial Reporting Standards (**IFRS**) as issued by the International Accounting Standards Board (**IASB**). The consolidated financial statements were authorised for issue by the Directors on 3 October 2018.

(b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis, with the exception of the following assets and liabilities which are stated at their fair value:

- Derivative financial instruments;
- Financial assets held for trading; and
- Financial assets available-for-sale.

(c) Functional and presentation currency

The consolidated financial statements are presented in Australian dollars, which is the Bank's functional currency.

(d) Rounding

The Consolidated Entity is of a kind referred to in ASIC Corporations Instrument 2016/191 dated 24 March 2016 and in accordance with that instrument, amounts in this financial report and Directors' report have been rounded off to the nearest million dollars, unless otherwise stated.

1.3. USE OF ESTIMATES AND JUDGEMENTS

The preparation of a financial report in conformity with Australian Accounting Standards requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. These estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. These accounting policies have been consistently applied throughout the Consolidated Entity.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised if the revision only affects that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described below:

- Provision for impairment – Section 3.3;
- Financial instruments – Section 3.7;
- Carrying value of goodwill and other intangible assets – Section 4.1.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

SECTION 2. FINANCIAL PERFORMANCE

2.1 OPERATING INCOME

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
INTEREST INCOME				
Loans and advances	1,927	1,900	1,760	1,738
Securities at fair value	142	146	289	277
Total interest income	2,069	2,046	2,049	2,015
INTEREST EXPENSE				
Retail deposits	(578)	(611)	(580)	(612)
Wholesale deposits and borrowings	(526)	(509)	(731)	(668)
Total interest expense	(1,104)	(1,120)	(1,311)	(1,280)
Net interest income	965	926	738	735
INCOME FROM OPERATING ACTIVITIES				
Other customer fees and charges	85	90	110	118
Share of fee revenue paid to Owner Managed Branches	(7)	(8)	(7)	(8)
Securitisation income	–	–	56	42
Net (loss) from financial instruments and derivatives at fair value	(4)	(4)	(4)	(3)
Commissions	34	31	14	13
Dividend income	–	–	22	150
Management fee – controlled entities	–	–	23	19
Foreign exchange income – customer based	12	11	12	11
Net profit on sale of property, plant and equipment	7	12	–	–
Other income	10	24	2	5
Total income from operating activities	137	156	228	347
Net insurance operating income	19	21	–	–
Total operating income	1,121	1,103	966	1,082

Interest income and expense

Interest income and expense for all interest bearing financial instruments are recognised in the profit or loss using the effective interest rates of the financial assets or financial liabilities to which they relate.

Other operating income

Other operating income and expense that are considered an integral part of the effective interest rate on a financial instrument are included in the measurement of the effective interest rate.

Non-yield related application and activation lending fee revenue is recognised when the loan is disbursed or the commitment to lend expires. Service fees that represent the recoupment of the costs of providing the service are recognised on an accrual basis when the service is provided.

Dividends are recognised when control of a right to receive consideration is established.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.2 EXPENSES

		Consolidated		Bank	
	Section	2018 $m	2017 $m	2018 $m	2017 $m
OPERATING EXPENSES					
Advertising		22	23	14	16
Commissions to Owner Managed Branches		5	6	5	6
Communications and postage		17	20	17	19
Printing and stationery		3	4	3	4
Processing costs		15	10	15	10
Other		24	31	26	33
		86	94	80	88
ADMINISTRATIVE EXPENSES					
Professional fees		30	13	27	12
Directors fees		2	2	2	2
Other		5	6	9	9
		37	21	38	23
IT EXPENSES					
Data processing		77	71	72	67
Amortisation – computer software	4.1	60	38	57	36
Depreciation – IT equipment		1	1	1	1
		138	110	130	104
OCCUPANCY EXPENSES					
Lease rentals		32	33	31	30
Depreciation – plant, furniture, equipment and leasehold improvements		9	9	9	8
Other		4	3	3	3
		45	45	43	41
EMPLOYEE EXPENSES					
Salaries, wages and superannuation contributions		240	232	219	209
Payroll tax		13	12	12	11
Equity settled transactions		10	11	8	10
Other		10	9	9	9
		273	264	248	239
OTHER					
Amortisation – acquired intangibles	4.1	8	14	6	13
Total expenses		587	548	545	508

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.3 INCOME TAX EXPENSE AND DEFERRED TAX

Income tax expense

The major components of income tax expense along with a reconciliation between pre-tax profit and tax expense are detailed below:

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
CURRENT TAX EXPENSE				
Current year	147	136	113	112
Adjustments for prior years	(1)	–	(1)	1
	146	136	112	113
DEFERRED TAX EXPENSE				
Origination and reversal of temporary differences	11	19	9	13
Total income tax expense	157	155	121	126
DEFERRED TAX RECOGNISED IN EQUITY				
Cash flow hedge reserve	1	18	1	20
Other	(3)	(5)	(3)	(5)
	(2)	13	(2)	15
NUMERICAL RECONCILIATIONS BETWEEN TAX EXPENSE AND PRE-TAX PROFIT				
Profit before tax	493	507	398	542
Income tax using the domestic corporate tax rate of 30% (2017: 30%)	148	152	119	163
Increase in income tax expense due to:				
Non-deductible expenses	9	10	9	10
Decrease in income tax expense due to:				
Non-assessable income	–	(5)	–	–
Other [(1)]	–	(2)	(7)	(47)
Income tax expense on pre-tax net profit	157	155	121	126

(1) In the Bank, this includes the impact of dividends received from subsidiary members in the Group which are eliminated at a Group level, and the dilutionary impact to prima-facie tax expense relating to franking credits on external dividends received on investments.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.3 INCOME TAX EXPENSE AND DEFERRED TAX (CONTINUED)

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
CONSOLIDATED	2018 $m	2017 $m	2018 $m	2017 $m	2018 $m	2017 $m
Accruals	3	2	–	–	3	2
Capitalised expenditure	–	–	(8)	(6)	(8)	(6)
Provisions for impairment	60	68	–	–	60	68
Other provisions	16	19	–	–	16	19
Equity reserves	6	4	–	–	6	4
Leasing	–	–	(34)	(30)	(34)	(30)
Other	7	8	(5)	(10)	2	(2)
Total tax assets / (liabilities) [(1)]	92	101	(47)	(46)	45	55
BANK						
Accruals	1	1	–	–	1	1
Capitalised expenditure	–	–	(5)	(3)	(5)	(3)
Provisions for impairment	46	55	–	–	46	55
Other provisions	16	17	–	–	16	17
Equity reserves	4	2	–	–	4	2
Leasing	–	–	(21)	(19)	(21)	(19)
Other	7	8	(2)	(9)	5	(1)
Total tax assets / (liabilities)	74	83	(28)	(31)	46	52

(1) The St Andrew's Group is classified as held for sale at the reporting date of 31 August 2018, refer to Note 6.5(d) for further information. Net deferred tax assets of $1 million have been reclassified as held for sale. The above table excludes these net deferred tax assets.

Unrecognised deferred tax assets

Deferred tax assets have not been brought to account for the following items as realisation of the benefit is not regarded as probable:

	2018 $m	2017 $m
Gross income tax losses [(2)]	26	28
Gross capital gains tax losses	51	51

(2) Income tax losses are subject to utilisation over an expected 10–15 year period.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.3 INCOME TAX EXPENSE AND DEFERRED TAX (CONTINUED)

Accounting for income tax

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

Current tax is the expected tax payable / receivable on the taxable income / loss for the year and any adjustment to the tax payable / receivable in respect of previous years. It is measured using tax rates enacted or substantially enacted at the reporting date.

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

Deferred tax assets are recognised for unused tax losses and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantially enacted at the reporting date. The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Consolidated Entity expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Tax consolidation

The Bank is the head entity in the tax-consolidated group comprising all the Australian wholly-owned subsidiaries. The implementation date for the tax-consolidated group was 1 September 2003.

Current tax expense (income), deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using a 'group allocation' approach by reference to the carrying amounts in the separate financial statements of each entity and the tax values applying under tax consolidation.

Any current tax liabilities (or assets) and deferred tax assets arising from unused tax losses of the subsidiaries is assumed by the head entity in the tax-consolidated group and are recognised as amounts payable (receivable) to (from) other entities in the tax-consolidated group in conjunction with any Tax Funding Arrangement amounts. Any difference between these amounts is recognised by the Bank as an equity contribution, or distribution from the subsidiary.

Any subsequent period amendments to deferred tax assets arising from unused tax losses as a result of a revised assessment of the probability of recoverability is recognised by the head entity only.

Nature of tax funding and tax sharing arrangements

The Bank, in conjunction with other members of the tax-consolidated group, has entered into a tax funding agreement which sets out the funding obligations of members of the tax-consolidated group in respect of tax amounts. The tax funding agreement requires payments to (from) the head entity equal to the current tax liability (asset) assumed by the head entity and any tax-loss deferred tax asset assumed by the head entity, resulting in the Bank recognising an inter-entity payable (receivable) equal in amount to the tax liability (asset) assumed.

Contributions to fund the current tax liabilities are payable as per the Tax Funding Arrangement and reflect the timing of the head entity's obligation to make payments for tax liabilities to the relevant tax authorities.

The Bank, in conjunction with other members of the tax-consolidated group, has also entered into a Tax Sharing Agreement (**TSA**). The TSA provides for the determination of the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement as payment of any amounts under the TSA is considered remote.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.4 DIVIDENDS

	Bank			
	2018		2017	
	Cents per share	$m	Cents per share	$m
ORDINARY SHARES				
Final 2017 dividend paid 23 November 2017 (2016: 22 November 2016)	38	149	38	145
Special 2017 dividend paid 23 November 2017 (2016: nil)	8	31	–	–
Interim 2018 dividend paid 17 May 2018 (2017: 17 May 2017)	38	149	38	147
		329		292
CONVERTIBLE PREFERENCE SHARES (CPS)				
Second half CPS dividend paid on 16 October 2017 (2016: 17 October 2016)	245	7	268	8
Pro-rata CPS dividend paid on 28 December 2017 (2016: nil)	98	2	–	–
First half CPS dividend paid (2017: 18 April 2017)	–	–	249	8
Final 2018 CPS dividend paid on 16 April 2018 (1)	244	3	–	–
		12		16

(1) In accordance with the ASX announcement dated 5 March 2018, BOQ confirmed the redemption of all outstanding CPS on the optional conversion/redemption date of 16 April 2018 with the redemption price of $102.44 per CPS, comprising the face value of $100 per CPS and a final dividend of $2.44 per CPS for the period from (and including) 16 October 2017 to (but excluding) the redemption date of 16 April 2018. The ASX announcement on 16 April 2018 confirmed the removal of CPS from official quotation at close of trading on 16 April 2018.

All dividends paid on ordinary and preference shares have been fully franked at 100%. Since the end of the financial year, the Directors have determined the following dividends:

	Cents per share	$m
Final ordinary share dividend	38	151

The final dividend payment will be fully franked and paid on 14 November 2018 to owners of ordinary shares at the close of business on 25 October 2018 (record date). Shares will be quoted ex-dividend on 24 October 2018.

	Bank	
	2018 $m	2017 $m
30% franking credits available to shareholders of the Bank for subsequent financial years	105	101

The ability to utilise the franking credits is dependent upon there being sufficient available profits to declare dividends. All franked dividends paid or declared by the Bank since the end of the previous financial year were franked at the tax rate of 30%.

The balance of the Bank's dividend franking account at the date of this report, after adjusting for franking credits and debits that will arise on payment of income tax and dividends relating to the year ended 31 August 2018, is $105 million credit calculated at the 30% tax rate (2017: $101 million credit). It is anticipated, based on these franking account balances that the Bank will continue to pay fully franked dividends in the foreseeable future.

Dividend reinvestment plan

The dividend reinvestment plan (**DRP**) provides ordinary shareholders with the opportunity to reinvest all or part of their entitlement to a dividend into new ordinary shares. The price for shares issued or transferred under the DRP is an amount 1.5 per cent (2017: 1.5 per cent) less than the arithmetic average, rounded to four decimal places, of the daily volume weighted average price of:

- all shares sold in the ordinary course of trading on the ASX automated trading system; and
- where shares are sold on trading platforms of Australian licensed financial markets operated by persons other than ASX, all shares sold in the ordinary course of trading on such of those trading platforms determined by the Board from time to time,

during the 10 trading day period commencing on the second trading day after the Record Date in respect of the relevant dividend.

Shares issued or transferred under the DRP will be fully-paid and rank equally in all respects with existing shares.

The calculation of the daily volume weighted average price shall not include certain transactions, as outlined in the DRP terms and conditions.

If, after this calculation there is a residual balance, that balance will be carried forward (without interest) and added to the next dividend for the purpose of calculating the number of shares secured under the DRP at that time.

The last date for election to participate in the DRP for the 2018 final dividend is 26 October 2018.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.5 OPERATING SEGMENTS

Segment information

The Consolidated Entity determines and presents operating segments based on the information that is provided internally to the Managing Director & CEO, the Bank's chief operating decision maker.

An operating segment is a component of the Consolidated Entity that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Consolidated Entity's other components. All operating segments' operating results are regularly reviewed by the Consolidated Entity's Managing Director & CEO to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the Managing Director & CEO include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

During the year ended 31 August 2018, the Consolidated Entity changed its operating segment model. Specifically, the Consolidated Entity has split its previously reported Banking segment into two segments: Retail Banking and BOQ Business. The insurance segment, previously presented on its own, has now been included in the Other segment.

The Bank's operating segments comprise the following:

Retail Banking – retail banking solutions to customers managed through our Owner Managed and Corporate branch network, third party intermediaries' and Virgin Money Australia distribution channels;

BOQ Business – BOQ Business includes the BOQ branded commercial lending activity, BOQ Finance and BOQ Specialist businesses. The division provides tailored business banking solutions including commercial lending, equipment finance and leasing, cashflow finance, foreign exchange, interest rate hedging, transaction banking and deposit solutions for commercial customers; and

Other – Group Treasury, St Andrews Insurance and Group Head Office.

The St Andrew's Insurance Group which forms part of the Other segment is classified as held for sale in the current financial year (refer Section 6.5(d) for more detail),

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss which in certain respects is measured differently from operating profit or loss in the consolidated financial statements. Income taxes are managed within the individual operating segments and thus disclosed this way.

Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

Major customers

No revenue from transactions with a single external customer or counter party amounted to 10% or more of the Consolidated Entity's total revenue in 2018 or 2017.

Geographic information

While the Consolidated Entity does have some operations in New Zealand, the business segments operate principally in Australia.

Goodwill

For goodwill allocation between segments, refer to Section 4.1.

Presentation

The following table presents income, profit and certain asset and liability information regarding the Consolidated Entity's operating segments.

Prior year comparatives have been restated to align with the current year presentation.

Inter-segment revenue and expenses and transfer pricing adjustments are reflected in the performance of each operating segment.

All inter-segment profits are eliminated on consolidation.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.5 OPERATING SEGMENTS (CONTINUED)

	Retail Banking		BOQ Business		Other		Segment Total	
	2018 $m	2017 $m	2018 $m	2017 $m	2018 $m	2017 $m	2018 $m	2017 $m
INCOME								
Net interest income [(1)]	458	446	514	482	(7)	(2)	965	926
Non interest income	67	69	59	78	19	28	145	175
Total income	525	515	573	560	12	26	1,110	1,101
Operating expenses	(281)	(274)	(228)	(220)	(18)	(19)	(527)	(513)
Underlying Profit	244	241	345	340	(6)	7	583	588
Loan impairment expense	(15)	(14)	(26)	(34)	–	–	(41)	(48)
Cash profit before tax	229	227	319	306	(6)	7	542	540
Income tax expense	(72)	(70)	(100)	(90)	2	(2)	(170)	(162)
Segment cash profit / (loss) after tax [(2)]	157	157	219	216	(4)	5	372	378
Statutory basis adjustments:								
Amortisation of acquisition of fair value adjustments	–	–	–	–	(7)	(13)	(7)	(13)
Hedge ineffectiveness	–	–	–	–	(3)	(9)	(3)	(9)
Integration / transaction costs	–	–	–	–	(1)	(1)	(1)	(1)
Regulatory / compliance	–	–	–	–	(9)	–	(9)	–
Software changes [(3)]	(7)	–	(4)	–	–	–	(11)	–
Legacy items	–	–	–	–	(5)	(3)	(5)	(3)
Statutory net profit / (loss) after tax	150	157	215	216	(29)	(21)	336	352
INCLUDED IN THE RESULTS:								
Depreciation and amortisation	49	43	26	18	2	1	77	62
Loan impairment expense	(15)	(14)	(26)	(34)	–	–	(41)	(48)
Segment assets	25,826	25,847	20,588	19,104	6,566	6,708	52,980	51,658
Segment liabilities	15,226	14,527	8,105	7,464	25,793	25,879	49,124	47,870

(1) Interest income and interest expenses are disclosed in this note on a net interest income basis. This is in line with the information provided internally to the Managing Director & CEO.
(2) This excludes a number of items that introduce volatility and / or one-off distortions of the Group's performance.
(3) Software changes include a non-recurring adjustment due to a reassessment of useful lives of existing assets aligned with the Group investment roadmap and a change to the capitalisation policy.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

2.6 EARNINGS PER SHARE

Basic earnings per share (EPS) is calculated by dividing the relevant earnings attributable to ordinary shareholders by the average weighted number of shares on issue. Diluted EPS takes into account the dilutive effect of all outstanding share rights vesting as ordinary shares.

	Consolidated	
	2018 $m	2017 $m
EARNINGS RECONCILIATION		
Profit for the year	336	352
Basic earnings	336	352
Effect of CPS	7	15
Effect of wholesale capital notes	7	7
Effect of capital notes	9	–
Diluted earnings	359	374

Weighted average number of shares used as the denominator	2018 Number	2017 Number
Number for basic earnings per share		
Ordinary shares	393,417,739	386,861,957
Number for diluted earnings per share		
Ordinary shares	393,417,739	386,861,957
Effect of award rights	1,523,277	1,797,630
Effect of CPS	12,129,338	24,505,955
Effect of wholesale capital notes	13,750,181	12,169,313
Effect of capital notes	21,408,589	–
	442,229,124	425,334,855
EARNINGS PER SHARE		
Basic earnings per share – Ordinary shares (cents)	85.5	90.9
Diluted earnings per share – Ordinary shares (cents)	81.2	87.8

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

SECTION 3. CAPITAL AND BALANCE SHEET MANAGEMENT

3.1 CASH AND CASH EQUIVALENTS

Components of cash and cash equivalents

Cash and cash equivalents comprise cash at branches, cash on deposit and balances with the Reserve Bank of Australia. Cash flows from the following activities are presented on a net basis in the statements of cash flows:

- Sales and purchases of trading securities;
- Customer deposits and withdrawals from deposit accounts; and
- Loan drawdowns and repayments.

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Notes, coins and cash at bank	815	705	443	328
Remittances in transit	297	209	297	209
Reverse repurchase agreements maturing in less than three months	100	-	100	-
Cash and cash equivalents as presented in the Balance Sheets	1,212	914	840	537
Cash and cash equivalents included in assets held for sale	6	-	-	-
Total	1,218	914	840	537

Notes to the statements of cash flows

Reconciliation of profit for the year to net cash provided by operating activities:

	Consolidated 2018 $m	Consolidated 2017 $m	Bank 2018 $m	Bank 2017 $m
Profit from ordinary activities after income tax	336	352	277	416
Add / (less) non-cash items or items classified as investing / financing:				
Depreciation	11	9	11	9
Amortisation	6	14	5	13
Software amortisation and impairment	62	38	59	37
(Profit) / loss on sale of property, plant and equipment	(1)	(4)	-	5
Equity settled transactions	10	11	8	11
Dividends received from controlled entities	-	-	(22)	(55)
Investments equity accounted	-	7	-	7
Profit on disposal of vendor finance entity	-	(16)	-	-
Decrease in due from other financial institutions	6	10	2	2
(Increase) / decrease in financial assets	443	(495)	506	(396)
Increase in loans and advances at amortised cost	(1,461)	(624)	(1,195)	(442)
Decrease in provision for impairment	(26)	(28)	(28)	(23)
Decrease in derivatives	35	4	26	4
Decrease in deferred tax asset	9	11	9	8
(Increase) / decrease in amounts due from controlled entities	-	-	322	(226)
(Increase) / decrease in other assets	41	(88)	(426)	(286)
Increase in due to other financial institutions	54	53	54	53
Increase / (decrease) in deposits	824	449	740	(22)
Increase / (decrease) in accounts payable and other liabilities	(29)	6	(27)	16
Decrease in current tax liabilities	(1)	(7)	(1)	(8)
Increase / (decrease) in provisions	3	(5)	(2)	(3)
Increase / (decrease) in deferred tax liabilities	1	9	(3)	5
Decrease in insurance policy liabilities	(6)	(8)	-	-
Net cash (inflow) / outflow from operating activities	317	(302)	315	(875)

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.2 FINANCIAL ASSETS

Refer to Section 3.7 for the accounting policy on financial assets.

Financial assets available-for-sale

Financial assets that are intended to be held for an indefinite period of time, but which may be sold in response to changes in interest rates, exchange rates and liquidity needs, are classified as available-for-sale. These assets are initially measured at fair value, plus any directly attributable transaction costs. Any changes in fair value other than impairment losses are recognised in other comprehensive income and accumulated in reserves in equity until the asset is sold. Interest income received on these assets is recorded as net interest income and any realised gains or losses recorded in other income in the Income Statement.

Financial assets held for trading

Financial assets that are held as part of the trading book are designated at fair value through the profit or loss in the Income Statement. The Consolidated Entity manages such financial assets and makes purchase and sale decisions based on their fair value in accordance with the documented risk management or investment strategy. Upon initial recognition, attributable transaction costs are recognised in profit or loss in the Income Statement when incurred. Financial instruments at fair value through the profit and loss are measured at fair value, and changes therein are recognised in profit or loss in the Income Statement.

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Available-for-sale				
Debt instruments	3,943	3,931	3,972	4,024
Unlisted equity instruments	3	3	3	3
Total available-for-sale	3,946	3,934	3,975	4,027
Current	817	1,019	846	1,052
Non-current	3,129	2,915	3,129	2,975
	3,946	3,934	3,975	4,027
Held for trading				
Floating rate notes and bonds	430	720	430	720
Negotiable certificates of deposit	955	1,117	955	1,117
Total held for trading	1,385	1,837	1,385	1,837
Current	1,385	1,837	1,385	1,837

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.3 LOANS AND ADVANCES AT AMORTISED COST

Loans and advances are originated by the Bank and are recognised upon cash being advanced to the borrower. Loans and advances are initially recognised at fair value, plus incremental directly attributable transaction costs. They are subsequently measured at each reporting date at amortised cost using the effective interest method.

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Residential property loans – secured by mortgages	30,506	29,853	30,506	29,853
Personal loans	222	232	222	232
Overdrafts	223	248	223	248
Commercial loans	9,626	9,001	9,466	8,856
Credit cards	75	75	75	75
Leasing finance	5,020	4,780	263	299
Gross loans and advances at amortised cost	45,672	44,189	40,755	39,563
Less:				
Unearned lease finance income	(393)	(372)	(28)	(33)
Specific provision for impairment	(86)	(106)	(74)	(90)
Collective provision for impairment	(115)	(121)	(82)	(92)
Total loans and advances at amortised cost	45,078	43,590	40,571	39,348

Loans and advances at amortised cost – impairment

If there is evidence of impairment for any of the Consolidated Entity's financial assets carried at amortised cost, the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, excluding future credit losses that have not been incurred. The cash flows are discounted at the financial asset's original effective interest rate. The loss is recognised in the profit or loss in the Income Statement.

(i) Specific impairment provisions

Impairment losses on individually assessed loans and advances are assessed on a case-by-case basis. If there is objective evidence that an individual loan or advance is impaired, a specific provision for impairment is raised. The amount of the specific provision is based on the carrying amount of the loan or advance, including the security held against the loan or advance and the present value of expected future cash flows. Any subsequent write-offs for bad debts are then made against the specific provision for impairment.

(ii) Collective impairment provisions

Where no evidence of impairment has been identified for loans and advances, these loans and advances are grouped together on the basis of similar credit characteristics for the purpose of calculating a collective impairment loss. Collective impairment provisions are based on historical loss experience applied to current observable data. The amount required to bring the collective provision for impairment to its required level is charged to profit or loss in the Income Statement.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.3 LOANS AND ADVANCES AT AMORTISED COST (CONTINUED)

Provision for impairment

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Specific provision:				
Balance at the beginning of the year	106	116	90	96
Add: Expensed during the year	44	67	31	45
Less: Bad debts written off	(61)	(74)	(44)	(49)
Transfers from collective provision	–	2	–	2
Unwind of discount	(3)	(5)	(3)	(4)
Balance at the end of the year	86	106	74	90
Collective provision:				
Balance at the beginning of the year	121	140	92	111
Add: Released during the year	(6)	(17)	(10)	(17)
Transfers to specific provision	–	(2)	–	(2)
Balance at the end of the year	115	121	82	92
Total provisions for impairment	201	227	156	182

Lease receivables

Loans and advances at amortised cost include the following finance lease receivables for leases of certain property and equipment where the Consolidated Entity is the lessor.

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Gross investment in finance lease receivables:				
Less than one year	1,909	1,807	23	24
Between one and five years	3,015	2,858	192	220
More than five years	96	115	48	55
	5,020	4,780	263	299
Unearned lease finance income	(393)	(372)	(28)	(33)
Net investment in finance leases	4,627	4,408	235	266
The net investment in finance leases comprise:				
Less than one year	1,740	1,647	22	23
Between one and five years	2,805	2,661	173	197
More than five years	82	100	40	46
	4,627	4,408	235	266

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.3 LOANS AND ADVANCES AT AMORTISED COST (CONTINUED)

Transfer of financial assets

Securitisation program

Through its REDS Securitisation and Warehouse Trusts (**RMBS Trusts**), REDS EHP Securitisation Trusts (**REDS EHP Trusts**) and Impala Securitisation programs, the Consolidated Entity packages loans and advances through a series of securitisation vehicles from which debt securities are issued to investors. The Consolidated Entity is entitled to any residual income from the vehicles after all payments to investors and costs of the programs have been met. The securitisation vehicles are consolidated and included in the 'Loans and advances' section of the Consolidated Entity's Balance Sheet. The note holders have recourse only to the loan pool of assets. Refer to Section 6.9 (a)(ii) for further information.

Covered bond program

The Bank issues covered bonds for funding and liquidity purposes. The bonds are issued to external investors and are secured against a pool of the Bank's housing loans. Housing loans are assigned to a bankruptcy remote structured entity to provide security for all obligations payable on the covered bonds issued by the Bank. The covered bond holders have dual recourse to the Bank and the cover pool of assets. The Bank is required to maintain the cover pool at a level sufficient to cover the obligations of the bonds. The Bank is entitled to any residual income of the covered bond structured entity after all payments due to the covered bond holders and any costs related to the program have been met. The housing loans are included in 'Loans and advances' and the covered bonds issued are included in 'Borrowings' on the Bank's Balance Sheet.

The following table sets out the transferred financial assets and associated liabilities of the securitisation and covered bond programs that did not qualify for derecognition under AASB 139 *Financial Instruments: Recognition and Measurement* (**AASB 139**).

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
TRANSFERRED FINANCIAL ASSETS				
Securitisation – loans and advances at amortised cost	3,291	2,836	3,291	2,921
Covered bonds – loans and advances at amortised cost	1,382	926	1,382	926
Securitisation – lease receivables	109	425	–	–
	4,782	4,187	4,673	3,847
ASSOCIATED FINANCIAL LIABILITIES				
Securitisation liabilities – external investors	3,580	3,429	–	–
Covered bonds liabilities – external investors	806	752	806	752
Amounts due to controlled entities	–	–	3,459	3,055
	4,386	4,181	4,265	3,807
FOR THOSE LIABILITIES THAT HAVE RECOURSE ONLY TO TRANSFERRED ASSETS (1)				
Fair value of transferred assets	4,785	4,201	4,675	3,855
Fair value of associated liabilities	(4,386)	(4,181)	(4,265)	(3,807)
Net position	399	20	410	48

(1) The fair values of transferred assets and liabilities that reprice within 6 months are assumed to equate to the amortised cost. All other fair values are calculated using a discounted cashflow model.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.4 DEPOSITS

Deposits are initially recognised at fair value, net of any directly attributable transaction costs. Subsequent to initial measurement, they are measured at amortised cost using the effective interest method.

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Deposits at call	14,786	13,512	14,991	13,802
Term deposits	18,747	18,646	18,791	18,688
Certificates of deposit	4,484	5,011	4,484	5,011
Total deposits	38,017	37,169	38,266	37,501
Concentration of deposits:				
Customer deposits	31,325	30,190	31,530	30,480
Wholesale deposits	6,692	6,979	6,736	7,021
	38,017	37,169	38,266	37,501

3.5 BORROWINGS

(a) Borrowings

Borrowings are initially recognised at fair value, net of any directly attributable transaction costs. Subsequent to initial measurement, they are measured at amortised cost using the effective interest method.

The Consolidated Entity recorded the following movements on borrowings:

	Securitisation liabilities [1] $m	Covered bonds liabilities [2] $m	EMTN program $m	ECP program $m	Subordinated notes $m	Senior unsecured notes $m	CPS and Capital Notes [3] $m	Total $m
YEAR ENDED 31 AUGUST 2018								
Balance at beginning of year	3,424	749	172	321	200	4,338	447	9,651
Proceeds from issues	1,288	–	93	88	200	1,459	191	3,319
Repayments	(1,135)	–	–	(322)	(50)	(1,311)	(141)	(2,959)
Deferred establishment costs	(2)	–	–	–	(1)	(1)	(7)	(11)
Amortisation of deferred costs	1	1	–	–	–	1	3	6
Foreign exchange translation [4]	–	54	11	6	–	–	–	71
Balance at end of the year	3,576	804	276	93	349	4,486	493	10,077

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.5 BORROWINGS (CONTINUED)

(a) Borrowings (continued)

	Securitisation liabilities [1] $m	Covered bonds liabilities [2] $m	EMTN program $m	ECP program $m	Subordinated notes $m	Senior unsecured notes $m	CPS and Capital Notes [3] $m	Total $m
YEAR ENDED 31 AUGUST 2017								
Balance at beginning of year	4,117	–	160	341	252	4,083	445	9,398
Acquired during the year	–	–	–	–	–	125	–	125
Proceeds from issues	1,356	743	48	512	–	1,431	–	4,090
Repayments	(2,050)	–	(33)	(529)	(50)	(1,301)	–	(3,963)
Deferred establishment costs	(3)	(3)	–	–	–	(1)	–	(7)
Amortisation of deferred costs	4	–	–	–	(2)	1	2	5
Foreign exchange translation [4]	–	9	(3)	(3)	–	–	–	3
Balance at end of the year	3,424	749	172	321	200	4,338	447	9,651

(1) Securitisation liabilities are secured by a floating charge over securitised assets for amounts owing to note holders and any other secured creditors of the securitisation vehicles.

(2) Covered bonds liabilities are secured by a charge over a pool of loans and advances and guaranteed by the covered bond guarantor.

(3) *CPS*

On 24 December 2012, the Bank issued 3,000,000 CPS. CPS were fully paid, perpetual and convertible preference shares with preferred, discretionary, non-cumulative dividends. They were not guaranteed or secured. In accordance with the ASX announcement dated 5 March 2018, BOQ confirmed the redemption of all outstanding CPS on the optional conversion/redemption date of 16 April 2018 with the redemption price of $102.44 per CPS, comprising the face value of $100 per CPS and a final dividend of $2.44 per CPS for the period from (and including) 16 October 2017 to (but excluding) the redemption date of 16 April 2018. The ASX announcement on 16 April 2018 confirmed the removal of CPS from official quotation at close of trading on 16 April 2018.

Wholesale Capital Notes

On 26 May 2015, the Bank issued 15,000 Wholesale Capital Notes (**WCN**) at a price of $10,000 per note. WCN are non-cumulative, fully paid and are issued by the Bank on a perpetual and subordinated basis. They are not guaranteed or secured. As at 31 August 2018, 15,000 WCN were outstanding with accrued distributions of $2 million. WCN must convert to ordinary shares on a mandatory conversion date of 26 May 2022 if certain mandatory conversion conditions are satisfied. Upon conversion, WCN holders will receive a number of ordinary shares based on the value weighted average price during a specified period. The WCN must also convert to ordinary shares of the Bank with the occurrence of a non-viability event, a capital trigger event or an acquisition event. BOQ may elect to redeem or resell the WCN on 26 May 2020 or following a regulatory or tax event. These options are subject to APRA's prior written approval and certain conditions being satisfied. In a winding up of the Bank, if the WCN have not been converted or written off on account of a non-viability trigger event or capital trigger event, the WCN will rank for payment of capital ahead of ordinary shareholders, equally with other securities or instruments ranking equally with WCN, but behind all other securities or instruments ranking ahead of WCN, and behind all senior creditors.

Capital Notes

On 28 December 2017, the Bank issued 3,500,000 Capital Notes at a price of $100 per note. Capital Notes are perpetual and convertible notes issued by BOQ, with preferred, discretionary, non-cumulative distributions. They are not guaranteed or secured. As at 31 August 2018, 3,500,000 Capital Notes were outstanding with accrued distributions of $1 million. Capital Notes must convert into ordinary shares on 15 August 2026 if certain mandatory conversion conditions are satisfied, unless they are converted or redeemed earlier. Where the mandatory conversion conditions are satisfied, a holder will receive a number of ordinary shares per Capital Note based on the value weighted average price of ordinary shares during a specified period. The Capital Notes must also convert to ordinary shares of the Bank with the occurrence of a loss absorption event or an acquisition event. BOQ may elect to convert, redeem or resell Capital Notes on 15 August 2024 or following a regulatory or tax event. BOQ may also elect to convert all Capital Notes following a potential acquisition event. These options are subject to APRA's prior written approval and certain conditions being satisfied. In a winding up of the Bank, Capital Notes will rank for payment of capital ahead of ordinary shares, equally with CPS, WCN and other equal ranking instruments, but behind the claims of all senior ranking creditors, including depositors and unsubordinated and subordinated creditors.

(4) Foreign exchange translation is a non-cash movement which is 100% hedged.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.5 BORROWINGS (CONTINUED)

(a) Borrowings (continued)

The Bank recorded the following movements on borrowings:

	Covered bonds liabilities[1] $m	EMTN program $m	ECP program $m	Subordinated notes $m	Senior unsecured notes $m	CPS and Capital Notes [2] $m	Total $m
YEAR ENDED 31 AUGUST 2018							
Balance at beginning of year	752	172	321	200	4,338	447	6,230
Proceeds from issues	–	93	88	200	1,459	191	2,031
Repayments	–	–	(322)	(50)	(1,311)	(141)	(1,824)
Deferred establishment costs	–	–	–	(1)	(1)	(7)	(9)
Amortisation of deferred costs	–	–	–	–	1	3	4
Foreign exchange translation [3]	54	11	6	–	–	–	71
Balance at end of the year	**806**	**276**	**93**	**349**	**4,486**	**493**	**6,503**

	Covered bonds liabilities[1] $m	EMTN program $m	ECP program $m	Subordinated notes $m	Senior unsecured notes $m	CPS and Capital Notes [2] $m	Total $m
YEAR ENDED 31 AUGUST 2017							
Balance at beginning of year	–	160	341	252	4,083	445	5,281
Proceeds from issues	743	48	512	–	1,431	–	2,734
Repayments	–	(33)	(529)	(50)	(1,176)	–	(1,788)
Deferred establishment costs	–	–	–	–	(1)	–	(1)
Amortisation of deferred costs	–	–	–	(2)	1	2	1
Foreign exchange translation [3]	9	(3)	(3)	–	–	–	3
Balance at end of the year	752	172	321	200	4,338	447	6,230

(1) Covered bonds liabilities are secured by a charge over covered pool of loans and advances and guaranteed by the covered bond guarantor.

(2) *CPS*

On 24 December 2012, the Bank issued 3,000,000 CPS. CPS were fully paid, perpetual and convertible preference shares with preferred, discretionary, non-cumulative dividends. They were not guaranteed or secured. In accordance with the ASX announcement dated 5 March 2018, BOQ confirmed the redemption of all outstanding CPS on the optional conversion/redemption date of 16 April 2018 with the redemption price of $102.44 per CPS, comprising the face value of $100 per CPS and a final dividend of $2.44 per CPS for the period from (and including) 16 October 2017 to (but excluding) the redemption date of 16 April 2018. The ASX announcement on 16 April 2018 confirmed the removal of CPS from official quotation at close of trading on 16 April 2018.

Wholesale Capital Notes

On 26 May 2015, the Bank issued 15,000 WCN at a price of $10,000 per note. WCN are non-cumulative, fully paid and are issued by the Bank on a perpetual and subordinated basis. They are not guaranteed or secured. As at 31 August 2018, 15,000 WCN were outstanding with accrued distributions of $2 million. WCN must convert to ordinary shares on a mandatory conversion date of 26 May 2022 if certain mandatory conversion conditions are satisfied. Upon conversion, WCN holders will receive a number of ordinary shares based on the value weighted average price during a specified period. The WCN must also convert to ordinary shares of the Bank with the occurrence of a non-viability event, a capital trigger event or an acquisition event. BOQ may elect to redeem or resell the WCN on 26 May 2020 or following a regulatory or tax event. These options are subject to APRA's prior written approval and certain conditions being satisfied. In a winding up of the Bank, if the WCN have not been converted or written off on account of a non-viability trigger event or capital trigger event, the WCN will rank for payment of capital ahead of ordinary shareholders, equally with other securities or instruments ranking equally with WCN, but behind all other securities or instruments ranking ahead of WCN, and behind all senior creditors.

Capital Notes

On 28 December 2017, the Bank issued 3,500,000 Capital Notes at a price of $100 per note. Capital Notes are perpetual and convertible notes issued by BOQ, with preferred, discretionary, non-cumulative distributions. They are not guaranteed or secured. As at 31 August 2018, 3,500,000 Capital Notes were outstanding with accrued distributions of $1 million. Capital Notes must convert into ordinary shares on 15 August 2026 if certain mandatory conversion conditions are satisfied, unless they are converted or redeemed earlier. Where the mandatory conversion conditions are satisfied, a holder will receive a number of ordinary shares per Capital Note based on the value weighted average price of ordinary shares during a specified period. The Capital Notes must also convert to ordinary shares of the Bank with the occurrence of a loss absorption event or an acquisition event. BOQ may elect to convert, redeem or resell Capital Notes on 15 August 2024 or following a regulatory or tax event. BOQ may also elect to convert all Capital Notes following a potential acquisition event. These options are subject to APRA's prior written approval and certain conditions being satisfied. In a winding up of the Bank, Capital Notes will rank for payment of capital ahead of ordinary shares, equally with CPS, WCN and other equal ranking instruments, but behind the claims of all senior ranking creditors, including depositors and unsubordinated and subordinated creditors.

(3) Foreign exchange translation is a non-cash movement which is 100% hedged.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT

The Consolidated Entity adopts a "managed risk" approach to its banking and insurance activities. As such, the articulation of a risk aware culture is prevalent throughout the Consolidated Entity's credit, market, liquidity, insurance, operational risk and compliance policies and procedures. The Board has adopted policies in relation to the assessment, management and monitoring of these risks and ownership of the frameworks within which these risks are managed reside with the Chief Risk Officer.

The Chief Risk Officer contributes towards the achievement of the Consolidated Entity's corporate objectives through the operationalisation and progressive development of the Consolidated Entity's risk management function. The continued improvement of the Consolidated Entity's risk management function focuses on a number of key areas, with particular emphasis on:

1. the efficiency and effectiveness of the Consolidated Entity's credit, market, liquidity, operational risk and compliance management process controls and policies to support the Bank's customer proposition in line with its risk appetite;
2. to provide management and the Board with risk reporting that contributes to the further development of sound corporate governance standards;
3. to maintain regulatory compliance in line with regulators' expectations;
4. to provide a sound basis from which the Bank can progress to the required compliance level under the Basel II accord; and
5. to contribute to the Consolidated Entity achieving risk based performance management.

Group Risk is an independent function and is responsible for providing the framework, policies and procedures needed for managing credit, liquidity, market, operational risk and compliance throughout the Group. Policies are set in line with the governing strategy and risk guidelines set by the Board.

Monitoring

The Consolidated Entity's enterprise risk management framework incorporates active management and monitoring of a range of risks including (but not limited to):

1. Market;
2. Credit;
3. Liquidity; and
4. Insurance.

(a) Market risk

Market risk is the risk that movements in market rates and prices will result in profits or losses to the Bank. The objective of market risk management is to manage and control market risk and to minimise its impact on the Consolidated Entity.

(i) Interest rate risk management

The operations of the Consolidated Entity are subject to the risk of interest rate fluctuations as a result of mismatches in the timing of the repricing of interest rates on the Consolidated Entity's assets and liabilities.

The figures in the table below indicate the potential increase / (decrease) in net interest income for an ensuing 12 month period of a 1% parallel shock increase to the yield curve. A 1% decrease in the yield curve has a materially equal but opposite impact.

Consolidated	2018 $m	2017 $m
Exposure at the end of the year	15	5
Average monthly exposure during the year	2	1
High month exposure during the year	15	12
Low month exposure during the year	(8)	(15)

(ii) Foreign exchange risk

It is the Bank's policy not to carry material foreign exchange rate exposures, net of associated hedging instruments. At balance date, there are no net material foreign exchange rate exposures.

The Bank uses cross currency swaps and foreign exchange forwards to hedge its exchange rate exposures arising from borrowing off-shore in foreign currencies. The Bank uses forward foreign exchange contracts to hedge potential exchange rate exposures created by customer-originated foreign currency transactions.

The Bank's investment in its New Zealand subsidiary is hedged by forward foreign exchange contracts which mitigate the currency risk arising from the subsidiary's net assets.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(a) Market risk (continued)

(iii) Traded market risk

Market risks attributable to trading activities are primarily measured using a parametric Value-at-Risk (**VaR**) model based on historical data. VaR is a statistical technique used to quantify the potential loss in earnings from adverse market movements and is calculated over a 1-day time horizon to a 99% confidence level using 2 years of historical data. As an additional overlay to VaR, the individual market risks of interest rate, foreign exchange, credit and equity are managed using a framework that includes stress testing, scenario analysis, sensitivity analysis and stop losses. Risks are monitored and measured against limits delegated by the Asset-Liability Committee (**ALCO**) and approved by the Board's Risk Committee.

The portfolio (interest rate, foreign exchange, credit and equity) VaR for the Bank's trading portfolio for the year was as follows:

Trading VaR	2018 $m	2017 $m
Average	0.21	0.43
Maximum	0.82	1.03
Minimum	0.10	0.15

(b) Credit risk

Credit risk arises in the business from lending activities, the provision of guarantees including letters of credit and commitments to lend, investment in bonds and notes, financial market transactions and other associated activities. Credit risk is the potential loss arising from the possibility that customers or counter parties fail to meet contractual payment obligations to the Bank as they fall due.

The Board have implemented a structured framework of systems and controls to monitor and manage credit risk comprising:

- documented credit risk management principles which are disseminated to all staff involved with the lending process;
- documented policies;
- a process for approving risk, based on tiered delegated approval authorities, whereby the largest exposures are assessed by the Executive Credit Committee consisting of Group Executives and senior risk managers, chaired by the Chief Risk Officer;
- risk grading the Bank's commercial exposures for facilities greater than $100,000 based on items inclusive of financial performance and stability, organisational structure, industry segment and security support. Exposures within this segment of the portfolio are generally subject to annual review including reassessment of the assigned risk grade;
- an automated scorecard approval model for the Bank's retail portfolio inclusive of home loans, personal loans, and lines of credit. This model is supported by experienced risk assessment managers; and
- a series of management reports detailing industry concentrations, counter party concentrations, loan grades and security strength ratings.

The Consolidated Entity uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operating, financing and investing activities. In accordance with its treasury risk policies, the Consolidated Entity can hold derivative financial instruments for trading purposes. Credit risk on derivative contracts used for these purposes is minimised as counter parties are recognised financial intermediaries with acceptable credit ratings determined by a recognised rating agency.

(i) Maximum exposure to credit risk

The amounts disclosed are the maximum exposure to credit risk, before taking account of any collateral held or other credit enhancements. For financial assets recognised on the Balance Sheet, the exposure to credit risk equals their carrying amount. For customer commitments, the maximum exposure to credit risk is the full amount of the committed facilities as at reporting date.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(b) Credit risk (continued)

(i) Maximum exposure to credit risk (continued)

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Cash and cash equivalents	1,212	914	840	537
Due from other financial institutions	6	58	6	8
Other financial assets (including accrued interest)	5,395	5,829	5,420	5,920
Derivative financial instruments	135	109	80	107
Financial assets other than loans and advances	6,748	6,910	6,346	6,572
Gross loans and advances at amortised cost	45,672	44,189	40,755	39,563
Total financial assets	52,420	51,099	47,101	46,135
Customer commitments (1)	1,753	1,733	995	959
Total potential exposure to credit risk	54,173	52,832	48,096	47,094

(1) Refer to Section 6.2 for details of customer commitments.

The distribution of financial assets by credit quality at the reporting date was:

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Neither past due or impaired				
Gross loans and advances at amortised cost	44,653	43,068	39,851	38,567
Financial assets other than loans and advances	6,748	6,910	6,346	6,572
Past due but not impaired				
Gross loans and advances at amortised cost	855	929	756	826
Impaired				
Gross loans and advances at amortised cost	164	192	148	170
Total financial assets	52,420	51,099	47,101	46,135

There is no individual exposure included in impaired assets which exceeds 5% of shareholders' equity (2017: 5%).

The Bank holds collateral against loans and advances to customers in the form of mortgage interest over property, other registered securities over assets and guarantees and mortgage insurance. To mitigate credit risk, the Bank can take possession of the collateral held against the loans and advances as a result of customer default. To ensure reduced exposure to losses, the collateral held by the Bank as mortgagee in possession is realised promptly.

Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. An estimate of the collateral held against past due but not impaired and impaired loans and advances at amortised cost is outlined below. It is not practical to determine the fair value of collateral held against performing loans.

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Held against past due but not impaired assets	1,397	1,436	1,335	1,384
Held against impaired assets	105	116	98	107

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(b) Credit risk (continued)

(ii) Credit quality

The credit quality categories of financial assets have been determined based on Standard & Poor's credit ratings, APRA risk weightings and the Bank's standard risk grading. The categories are classified as below:

- High grade – generally corresponds to Standard & Poor's credit ratings AAA+ to BBB–.
- Satisfactory – generally corresponds to Standard & Poor's credit rating BB+ to B.
- Weak – generally corresponds to Standard & Poor's credit ratings up to B.
- Unrated – Loans and advances which have been classified as unrated are not secured, however these are not deemed to be weak.

The table below presents an analysis of the credit quality of financial assets:

Consolidated								
	2018 $m				2017 $m			
	Gross loans & advances				Gross loans & advances			
	Retail	Commercial	Total loans & advances	Financial assets other than loans & advances	Retail	Commercial	Total loans & advances	Financial assets other than loans & advances
High Grade	25,294	4,388	29,682	6,745	24,643	4,257	28,900	6,907
Satisfactory	5,114	8,967	14,081	–	5,128	8,299	13,427	–
Weak	330	1,327	1,657	3	313	1,277	1,590	3
Unrated	65	187	252	–	76	196	272	–
	30,803	14,869	45,672	6,748	30,160	14,029	44,189	6,910

Bank								
	2018 $m				2017 $m			
	Gross loans & advances				Gross loans & advances			
	Retail	Commercial	Total loans & advances	Financial assets other than loans & advances	Retail	Commercial	Total loans & advances	Financial assets other than loans & advances
High Grade	25,294	3,640	28,934	6,313	24,643	3,370	28,013	6,476
Satisfactory	5,114	5,637	10,751	19	5,128	5,285	10,413	60
Weak	330	488	818	14	313	552	865	36
Unrated	65	187	252	–	76	196	272	–
	30,803	9,952	40,755	6,346	30,160	9,403	39,563	6,572

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(b) Credit risk (continued)

(iii) Loans and advances which were past due but not impaired

Loans which are 90 or more days past due are not classified as impaired assets where the estimated net realisable value of the security is sufficient to cover the repayment of all principal and interest amounts due.

		Consolidated		Bank	
		2018 $m	2017 $m	2018 $m	2017 $m
Less than 30 days	– Retail	224	276	224	276
	– Commercial	162	183	85	101
30 to 89 days	– Retail	161	164	161	164
	– Commercial	48	49	30	34
90 days or more	– Retail	150	170	150	170
	– Commercial	110	87	106	81
		855	929	756	826

(iv) Concentration of exposure for gross loans and advances at amortised cost

Concentration of credit risk exists when a number of counter parties are engaged in similar activities, operate in the same geographical areas or industry sectors and have similar economic characteristics, so that their ability to meet contractual obligations is similarly affected by changes in economic, political or other conditions. The Bank monitors concentrations of credit risk by geographical location for loans and advances. An analysis of these concentrations of credit risk at the reporting date is shown below:

	Consolidated		Bank	
Geographical concentration of credit risk for loans and advances at amortised cost (before provisions and unearned income):	2018 $m	2017 $m	2018 $m	2017 $m
Queensland	20,221	20,613	18,526	19,029
New South Wales	12,026	10,412	10,687	9,143
Victoria	7,044	6,867	6,012	5,909
Northern Territory	287	302	277	294
Australian Capital Territory	323	311	300	293
Western Australia	4,463	4,510	4,143	4,155
South Australia	771	705	611	548
Tasmania	230	215	199	192
International (New Zealand)	307	254	–	–
	45,672	44,189	40,755	39,563

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For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(c) Liquidity risk

Liquidity risk arises from the possibility that the Bank is unable to meet its financial obligations as they fall due. Liquidity risk is managed through a series of detailed policies. This includes the management of cash flow mismatches, the maintenance of a stable, core retail deposits base, the diversification of the funding base and the retention of adequate levels of high quality liquid assets.

The Consolidated Entity manages liquidity risk by maintaining adequate reserves and facilities by continuously monitoring forecast and actual cash flows, matching maturity profiles of financial assets and liabilities and monitoring liquidity scenario analysis.

Consolidated 2018	Carrying amount $m	At Call $m	3 months or less $m	3 to 12 months $m	1 to 5 years $m	Over 5 years $m	Policy holder $m	Total contractual cash flows $m
FINANCIAL LIABILITIES								
Due to other financial institutions	315	315	–	–	–	–	–	315
Deposits	38,017	14,786	13,340	9,389	893	–	–	38,408
Derivative financial instruments (1)	8	–	2	2	6	1	–	11
Accounts payable and other liabilities	360	–	360	–	–	–	–	360
Securitisation liabilities (2)	3,576	–	260	611	2,117	659	–	3,647
Borrowings	6,501	–	66	1,055	5,901	–	–	7,022
Liabilities Held for Sale	22	–	–	–	–	–	22	22
Total financial liabilities	**48,799**	**15,101**	**14,028**	**11,057**	**8,917**	**660**	**22**	**49,785**
DERIVATIVE FINANCIAL INSTRUMENTS (HEDGING RELATIONSHIP)								
Contractual amounts payable		–	853	452	1,664	211	–	3,180
Contractual amounts receivable		–	(846)	(404)	(1,457)	(118)	–	(2,825)
	176	–	7	48	207	93	–	355
OFF BALANCE SHEET POSITIONS								
Guarantees, indemnities and letters of credit		304	–	–	–	–	–	304
Customer funding commitments		1,449	–	–	–	–	–	1,449
	–	1,753	–	–	–	–	–	1,753

(1) Derivative financial instruments other than those designated in hedge relationships.

(2) Repayment of securitisation bonds is forecast based on the expected repayment profile of the underlying assets of the Trusts.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(c) Liquidity risk (continued)

Consolidated 2017	Carrying amount $m	At Call $m	3 months or less $m	3 to 12 months $m	1 to 5 years $m	Over 5 years $m	Policy holder $m	Total contractual cash flows $m
FINANCIAL LIABILITIES								
Due to other financial institutions	262	262	–	–	–	–	–	262
Deposits	37,169	13,152	11,952	11,498	971	–	–	37,573
Derivative financial instruments [(1)]	13	–	6	–	2	1	–	9
Accounts payable and other liabilities	390	–	390	–	–	–	–	390
Securitisation liabilities [(2)]	3,424	–	261	609	2,077	659	–	3,606
Borrowings	6,227	–	221	1,917	4,474	–	–	6,612
Insurance policy liabilities	16	–	–	–	–	–	16	16
Total financial liabilities	47,501	13,414	12,830	14,024	7,524	660	16	48,468
DERIVATIVE FINANCIAL INSTRUMENTS (HEDGING RELATIONSHIP)								
Contractual amounts payable		–	784	525	1,683	220	–	3,212
Contractual amounts receivable		–	(757)	(467)	(1,375)	(95)	–	(2,694)
	239	–	27	58	308	125	–	518
OFF BALANCE SHEET POSITIONS								
Guarantees, indemnities and letters of credit		321	–	–	–	–	–	321
Customer funding commitments		1,412	–	–	–	–	–	1,412
	–	1,733	–	–	–	–	–	1,733

(1) Derivative financial instruments other than those designated in hedge relationships.

(2) Repayment of securitisation bonds is forecast based on the expected repayment profile of the underlying assets of the Trusts.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(c) Liquidity risk (continued)

Bank 2018	Carrying amount $m	At Call $m	3 months or less $m	3 to 12 months $m	1 to 5 years $m	Over 5 years $m	Total contractual cash flows $m
FINANCIAL LIABILITIES							
Due to other financial institutions	315	315	–	–	–	–	315
Deposits	38,266	14,991	13,384	9,389	893	–	38,657
Derivative financial instruments (1)	8	–	2	2	6	1	11
Accounts payable and other liabilities	304	–	304	–	–	–	304
Borrowings	6,503	–	66	1,055	5,901	–	7,022
Total financial liabilities	45,396	15,306	13,756	10,446	6,800	1	46,309
DERIVATIVE FINANCIAL INSTRUMENTS (HEDGING RELATIONSHIP)							
Contractual amounts payable		–	849	433	852	211	2,345
Contractual amounts receivable		–	(848)	(399)	(640)	(118)	(2,005)
	230	–	1	34	212	93	340
OFF BALANCE SHEET POSITIONS							
Guarantees, indemnities and letters of credit		304	–	–	–	–	304
Customer funding commitments		691	–	–	–	–	691
	–	995	–	–	–	–	995

(1) Derivative financial instruments other than those designated in a hedge relationships.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(c) Liquidity risk (continued)

Bank 2017	Carrying amount $m	At Call $m	3 months or less $m	3 to 12 months $m	1 to 5 years $m	Over 5 years $m	Total contractual cash flows $m
FINANCIAL LIABILITIES							
Due to other financial institutions	262	262	–	–	–	–	262
Deposits	37,501	13,802	11,634	11,498	971	–	37,905
Derivative financial instruments (1)	13	–	6	–	2	1	9
Accounts payable and other liabilities	327	–	327	–	–	–	327
Borrowings	6,230	–	221	1,917	4,474	–	6,612
Total financial liabilities	44,333	14,064	12,188	13,415	5,447	1	45,115
DERIVATIVE FINANCIAL INSTRUMENTS (HEDGING RELATIONSHIP)							
Contractual amounts payable		–	784	516	859	220	2,379
Contractual amounts receivable		–	(763)	(472)	(613)	(95)	(1,943)
	242	–	21	44	246	125	436
OFF BALANCE SHEET POSITIONS							
Guarantees, indemnities and letters of credit		321	–	–	–	–	321
Customer funding commitments		638	–	–	–	–	638
	–	959	–	–	–	–	959

(1) Derivative financial instruments other than those designated in hedge relationships.

(d) Insurance risk

(i) Risk management objectives and policies for risk mitigation

Insurance risks are controlled through the use of underwriting procedures, adequate premium rates and policy charges and sufficient reinsurance arrangements, all of which are approved through a Board approved governance structure. Controls are also maintained over claims management practices to assure the correct and timely payment of insurance claims.

(ii) Strategy for managing insurance risk

Portfolio of risks

During the financial year, the Bank's insurance subsidiaries issued a range of consumer credit insurance, life and general insurance products. The performance of the Bank's insurance subsidiaries and its continuing ability to write business depends on its ability to pre-empt and control risks. The Bank's insurance subsidiaries have a risk management strategy which has been approved by their respective Boards. It summarises the approach to risk and risk management.

Risk strategy

In compliance with contractual and regulatory requirements, a strategy is in place to ensure that the risks underwritten satisfy objectives whilst not adversely affecting the Consolidated Entity's ability to pay benefits and claims when due. The strategy involves the identification of risks by type, impact and likelihood, the implementation of processes and controls to mitigate the risks, and continuous monitoring and improvement of the procedures in place to minimise the chance of an adverse compliance or operational risk event occurring. Included in this strategy is the process for underwriting and product pricing to ensure products are appropriately priced. Capital management is also a key aspect of the Consolidated Entity's risk management strategy. Capital requirements take account of all of the various regulatory requirements to which the Consolidated Entity is subject.

Prudential capital requirements

Prudential capital requirements established by APRA are in place to safeguard policyholders' interests, which are primarily the ability to meet future claim payments to policyholders. These require the Consolidated Entity's capital base to exceed the Prudential Capital Requirement throughout the year, not just at year end. The level of capital requirements also take into account specific risks faced by the Bank's insurance subsidiaries.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.6 RISK MANAGEMENT (CONTINUED)

(d) Insurance risk (continued)

(iii) Methods to limit or transfer insurance risk exposures

Reinsurance

The insurance subsidiaries use reinsurance arrangements to pass on or cede to reinsurers risks that are outside of the subsidiaries' risk appetite.

Underwriting procedures

Strategic underwriting decisions are put into effect using the underwriting procedures detailed in the Bank's insurance subsidiaries' Underwriting Policy. Such procedures include limits to delegated authorities and signing powers.

Claims management

Strict claims management procedures ensure timely and correct payment of claims in accordance with policy conditions.

Asset and liability management techniques

Assets are allocated to different classes of business using a risk based approach. The Bank's insurance subsidiaries have a mix of short and long term business and invest accordingly. Market risk is managed through investing in cash, deposits and bank issued commercial bills. No more than 35% of shareholder funds and funds backing insurance policy liabilities can be invested with any one counterparty, subject to counterparty credit ratings.

(e) Concentration of insurance risk

(i) Insurance risks associated with human life events

The Bank aims to maintain a diversified profile of ages, genders, health statuses and geographic location within its portfolio of policyholders. This policy maintains a balance between the current and future profitability of the life business, and exposure to any significant external events. The distribution channels and subsequent demographic mix of the population of policyholders is sufficiently spread so that the risk concentration in relation to any particular group is small. Specific processes for monitoring identified key concentrations include monitoring sales by product type, cover type and corporate partner type.

3.7 FINANCIAL INSTRUMENTS

(a) Financial instrument classifications

Financial assets

The Consolidated Entity classifies its financial assets into the following categories:

- Financial assets available-for-sale: Refer to Section 3.2;
- Financial assets at fair value through profit and loss: Refer to Section 3.2 for further information on financial assets held for trading;
- Loans and receivables: Refer to Section 3.3 for further information on loan and advances at amortised cost. Receivables due from other financial institutions are recognised and measured at amortised cost and include settlement account balances and nostro balances (an account held with a foreign bank usually in a foreign currency); and
- Derivative financial assets: Refer to Section 3.8.

Financial liabilities

The Consolidated Entity classifies its financial liabilities into the following categories:

- Financial liabilities at amortised cost: Refer to Section 3.4 for further information on deposits and Section 3.5 for further information on borrowings; and
- Derivative financial liabilities: Refer to Section 3.8.

(b) Fair value of financial instruments

The financial assets and liabilities listed below are recognised and measured at fair value and therefore their carrying value equates to their fair value:

- Financial assets available-for-sale;
- Financial assets and liabilities designated at fair value through the profit and loss (held for trading); and
- Derivatives.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.7 FINANCIAL INSTRUMENTS (CONTINUED)

The fair value estimates for instruments carried at amortised cost are based on the following methodologies and assumptions:

Cash and cash equivalents, due from and to other financial institutions, accounts payable and other liabilities
The fair value approximates their carrying value as they are short term in nature or are receivable or payable on demand.

Loans and advances
Loans and advances are net of specific and collective provisions for impairment and unearned income. The fair values of loans and advances that reprice within six months of year end are assumed to equate to the carrying value. The fair values of all other loans and advances are calculated using discounted cash flow models based on the maturity of the loans and advances.

The discount rates applied are based on the current interest rates at the reporting date for similar types of loans and advances, if the loans and advances were performing at the reporting date. The differences between estimated fair values and carrying values reflect changes in interest rates and creditworthiness of borrowers since loan or advance origination.

Deposits
The fair value of non-interest bearing, at call and variable rate deposits and fixed rate deposits repricing within six months is the carrying value. The fair value of other term deposits is calculated using discounted cash flow models based on the deposit type and its related maturity.

Borrowings
The fair values are calculated based on a discounted cash flow model using a yield curve appropriate to the remaining maturity of the instruments.

(c) Comparison of fair value to carrying amounts

The tables below disclose the fair value of financial instruments where their carrying value is not a reasonable approximation of their fair value:

		Consolidated Entity			
		Carrying value		Fair value	
	Section	2018 $m	2017 $m	2018 $m	2017 $m
ASSETS CARRIED AT AMORTISED COST					
Loans and advances at amortised cost	3.3	45,078	43,590	45,105	43,623
		45,078	43,590	45,105	43,623
LIABILITIES CARRIED AT AMORTISED COST					
Deposits	3.4	(38,017)	(37,169)	(38,020)	(37,174)
Borrowings	3.5	(10,077)	(9,651)	(10,074)	(9,650)
		(48,094)	(46,820)	(48,094)	(46,824)

		Bank			
		Carrying value		Fair value	
	Section	2018 $m	2017 $m	2018 $m	2017 $m
ASSETS CARRIED AT AMORTISED COST					
Loans and advances at amortised cost	3.3	40,571	39,348	40,585	39,369
		40,571	39,348	40,585	39,369
LIABILITIES CARRIED AT AMORTISED COST					
Deposits	3.4	(38,266)	(37,501)	(38,269)	(37,506)
Borrowings	3.5	(6,503)	(6,230)	(6,504)	(6,231)
		(44,769)	(43,731)	(44,773)	(43,737)

The estimated fair values disclosed do not include the assets and liabilities that are not financial instruments.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.7 FINANCIAL INSTRUMENTS (CONTINUED)

(d) Fair value hierarchy

The Consolidated Entity measures fair values using the following fair value hierarchy and valuation techniques, which reflect the significance of the inputs used in making the measurements:

- Level 1: This category includes assets and liabilities for which the valuation is determined from inputs based on unadjusted quoted market prices in active markets for identical instruments.
- Level 2: This category includes assets and liabilities for which the valuation is determined from inputs other than quoted prices included within level 1, which are observable either directly or indirectly. This includes the use of discounted cash flow analysis, option pricing models and other market accepted valuation models.
- Level 3: This category includes assets and liabilities for which the valuation includes inputs that are not based on observable market data. This includes equity instruments and as there are no quoted market prices and fair value cannot be measured reliably, these are held at cost.

The fair value hierarchy classification of instruments in Section 3.7 (c):

- Loans and advances at amortised cost – Level 3
- Deposits and borrowings – Level 2

There was no movement between levels during the year.

The table below analyses financial instruments carried at fair value, by valuation method:

	2018			
Consolidated Entity	Level 1 $m	Level 2 $m	Level 3 $m	Total $m
Instruments carried at fair value				
Financial assets available-for-sale	2,580	1,363	3	3,946
Financial assets at fair value through profit and loss	–	1,385	–	1,385
Derivative financial assets	–	135	–	135
	2,580	2,883	3	5,466
Derivative financial liabilities	–	(294)	–	(294)
	2,580	2,589	3	5,172

	2017			
Consolidated Entity	Level 1 $m	Level 2 $m	Level 3 $m	Total $m
Instruments carried at fair value				
Financial assets available-for-sale	2,261	1,670	3	3,934
Financial assets at fair value through profit and loss	53	1,784	–	1,837
Derivative financial assets	–	109	–	109
	2,314	3,563	3	5,880
Derivative financial liabilities	–	(333)	–	(333)
	2,314	3,230	3	5,547

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.7 FINANCIAL INSTRUMENTS (CONTINUED)

(d) Fair value hierarchy (continued)

	2018			
Bank	Level 1 $m	Level 2 $m	Level 3 $m	Total $m
Instruments carried at fair value				
Financial assets available-for-sale	2,580	1,392	3	3,975
Financial assets at fair value through profit and loss	–	1,385	–	1,385
Derivative financial assets	–	80	–	80
	2,580	2,857	3	5,440
Derivative financial liabilities	–	(293)	–	(293)
	2,580	2,564	3	5,147

	2017			
Bank	Level 1 $m	Level 2 $m	Level 3 $m	Total $m
Instruments carried at fair value				
Financial assets available-for-sale	2,261	1,763	3	4,027
Financial assets at fair value through profit and loss	53	1,784	–	1,837
Derivative financial assets	–	107	–	107
	2,314	3,654	3	5,971
Derivative financial liabilities	–	(333)	–	(333)
	2,314	3,321	3	5,638

(e) Master netting or similar arrangements

There have been no financial assets or financial liabilities offset in the Balance Sheets. The Consolidated Entity has netting arrangements in place with counter parties on derivative financial instruments and the effects of these netting arrangements if they were to be applied in the Balance Sheets has been disclosed at Section 3.8 (c).

(f) Impairment of financial instruments policy

Financial assets other than loans and advances at amortised cost

The Consolidated Entity assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets, not carried at fair value through profit and loss, is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset and the loss event had a negative effect on the estimated future cash flow of that asset that can be estimated reliably.

In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of a security below its cost is considered as an indicator that the securities are impaired.

If any such evidence exists for financial assets available-for-sale the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss in the Income Statement) is reclassified from equity and recognised in profit or loss in the Income Statement as a reclassification adjustment. Impairment losses recognised in profit or loss in the Income Statement on equity instruments classified as available-for-sale are not reversed through the profit or loss in the Income Statement. For available-for-sale debt instruments, if an increase in the fair value can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed through profit of loss in the Income Statement.

(g) Derecognition of financial assets and liabilities

Financial assets are derecognised when the contractual rights to receive cash flows from the assets have expired, or where the Bank has transferred its contractual rights to receive the cash flows of the financial assets and substantially all the risks and rewards of ownership. Financial liabilities are derecognised when they are extinguished, i.e. when the obligation is discharged, cancelled or expired.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.8 DERIVATIVE FINANCIAL INSTRUMENTS

(a) Fair value of derivatives

The following tables summarise the notional and fair value of the Consolidated Entity's and Bank's commitments to derivative financial instruments at reporting date. Fair value in relation to derivative financial instruments is estimated using net present value techniques. The tables below set out the fair values of the derivative financial instruments.

	Consolidated					
	2018			2017		
	Notional Amount	Fair Value		Notional Amount	Fair Value	
	$m	Asset $m	Liability $m	$m	Asset $m	Liability $m
DERIVATIVES AT FAIR VALUE THROUGH INCOME STATEMENT						
Interest rate swaps	14,729	21	(7)	22,744	18	(12)
Foreign exchange forwards	120	1	(1)	139	2	(1)
Futures	2,364	3	–	8,775	8	–
	17,213	25	(8)	31,658	28	(13)
DERIVATIVES HELD AS CASH FLOW HEDGES						
Interest rate swaps	29,731	32	(33)	31,196	71	(50)
Cross currency swaps	1,163	65	(2)	993	8	(5)
Foreign exchange forwards	730	13	(1)	683	1	(17)
	31,624	110	(36)	32,872	80	(72)
DERIVATIVES DESIGNATED AS FAIR VALUE HEDGES						
Interest rate swaps	2,267	–	(250)	1,937	–	(248)
DERIVATIVES DESIGNATED AS NET INVESTMENT HEDGES						
Foreign exchange forwards	23	–	–	22	1	–
	51,127	135	(294)	66,489	109	(333)

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.8 DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

(a) Fair value of derivatives (continued)

	Bank					
	2018			2017		
	Notional Amount	Fair Value		Notional Amount	Fair Value	
	$m	Asset $m	Liability $m	$m	Asset $m	Liability $m
DERIVATIVES AT FAIR VALUE THROUGH INCOME STATEMENT						
Interest rate swaps	14,729	21	(7)	22,744	18	(12)
Foreign exchange forwards	144	1	(1)	161	3	(1)
Futures	2,364	3	-	8,775	8	-
	17,237	25	(8)	31,680	29	(13)
DERIVATIVES HELD AS CASH FLOW HEDGES						
Interest rate swaps	29,864	33	(32)	31,136	73	(50)
Cross currency swaps	357	9	(2)	241	4	(5)
Foreign exchange forwards	730	13	(1)	683	1	(17)
	30,951	55	(35)	32,060	78	(72)
DERIVATIVES DESIGNATED AS FAIR VALUE HEDGES						
Interest rate swaps	2,267	-	(250)	1,937	-	(248)
	50,455	80	(293)	65,677	107	(333)

(b) Accounting for derivatives

The Consolidated Entity and Bank used derivative financial instruments for both hedging and trading purposes in the current year. Refer to Section 3.6 (a) for an explanation of the Consolidated Entity's and Bank's risk management framework. The Consolidated Entity uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operating, financing and investing activities. In accordance with its treasury risk policies, the Consolidated Entity can hold derivative financial instruments for trading purposes. Derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are initially measured at fair value. Subsequent to initial recognition, gains or losses on derivatives are recognised in the Income Statement, unless they are entered into for hedging purposes.

The fair value of interest rate swaps is the estimated amount that the Consolidated Entity would receive or pay to terminate the swap at the reporting date, taking into account current interest rates and current creditworthiness of the swap counter parties. The fair value of forward exchange contracts is their quoted market price at the reporting date, being the present value of the quoted forward price. The fair value of futures contracts is their quoted market price.

Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability of the cash flows of a recognised asset or liability, or a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in other comprehensive income and accumulated in reserves in equity. The ineffective portion of any gain or loss is recognised immediately in profit or loss in the Income Statement. If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, then the associated gains and losses previously recognised directly in other comprehensive income are reclassified to profit or loss in the Income Statement in the same period or periods in which the asset acquired or liability assumed affects the Income Statement (i.e. when interest income or expense is recognised).

When a hedging instrument expires or is sold, terminated or exercised, or the Consolidated Entity revokes designation of the hedge relationship, and the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in other comprehensive income and is recognised in profit or loss in the Income Statement when the transaction occurs. If the hedged transaction is no longer expected to take place, then the cumulative unrealised gain or loss is recognised immediately in profit or loss in the Income Statement.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.8 DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

(b) Accounting for derivatives (continued)

Fair value hedges

Fair value hedges are used by the Group to manage exposure to changes in the fair value of an asset. Changes in fair values arise from fluctuations in interest rates. The Group principally uses interest rate swaps to protect against such fluctuations.

Changes in the value of fair value hedges are recognised in the Income Statement, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. All gains and losses associated with the ineffective portion of fair value hedge relationships are recognised immediately in the Income Statement.

If the hedge relationship no longer meets the criteria for hedge accounting, it is discontinued. The fair value adjustment to the hedged item is amortised to the Income Statement from the date of discontinuation over the period to maturity of the previously designated hedge relationship using the effective interest method. If the hedged item is sold or repaid, the unamortised fair value adjustment is recognised immediately in the Income Statement.

Net investment hedge

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any foreign currency gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in other comprehensive income . To the extent the hedge is ineffective, a portion is recognised immediately in the Income Statement within other income or other expenses.

Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the Income Statement and are included in other income.

(c) Master netting or similar arrangements

The Consolidated Entity enters into derivative transactions under International Swaps and Derivatives Association (ISDA) master netting agreements. Amounts owed by each counter party are aggregated into a single net amount that is payable by one party to another. The Consolidated Entity receives and gives collateral in the form of cash in respect of derivatives and such collateral is subject to standard industry terms. The Consolidated Entity has not offset these amounts in the Balance Sheet as their ISDA agreements do not meet the criteria to do so. The Consolidated Entity has no current legally enforceable right to offset recognised amounts as the right to offset is only enforceable on the occurrence of future events. The Consolidated Entity normally settles on a net basis or realises the derivative assets and liabilities simultaneously.

The following tables set out the effect of netting arrangements on derivative financial assets and derivative financial liabilities if they were to be applied.

2018

Consolidated	Gross amounts as presented in the Balance Sheet $m	Net amounts of recognised assets and liabilities available for offset $m	Cash collateral $m	Net amounts if offsetting applied in the Balance Sheet $m
Derivative financial assets	135	(39)	(8)	88
Derivative financial liabilities	(294)	39	250	(5)

2017

Consolidated	Gross amounts as presented in the Balance Sheet $m	Net amounts of recognised assets and liabilities available for offset $m	Cash collateral $m	Net amounts if offsetting applied in the Balance Sheet $m
Derivative financial assets	109	(69)	(22)	18
Derivative financial liabilities	(333)	69	276	12

2018

Bank	Gross amounts as presented in the Balance Sheet $m	Net amounts of recognised assets and liabilities available for offset $m	Cash collateral $m	Net amounts if offsetting applied in the Balance Sheet $m
Derivative financial assets	80	(39)	(8)	33
Derivative financial liabilities	(293)	39	250	(4)

2017

Bank	Gross amounts as presented in the Balance Sheet $m	Net amounts of recognised assets and liabilities available for offset $m	Cash collateral $m	Net amounts if offsetting applied in the Balance Sheet $m
Derivative financial assets	107	(69)	(22)	16
Derivative financial liabilities	(333)	69	276	12

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.9 CAPITAL MANAGEMENT

The Bank and Consolidated Entity's capital management strategy aims to ensure adequate capital levels are maintained to protect deposit holders. The Bank's capital is measured and managed in line with Prudential Standards issued by APRA. The capital management plan is updated annually and submitted to the Board for approval. The approval process is designed to ensure the plan is consistent with the overall business plan and for managing capital levels on an ongoing basis.

The Board has set the CET1 capital target range to be between 8% and 9.5% of risk weighted assets and the total capital range to be between 11.5% and 13.5% of risk weighted assets.

Qualifying capital for Level 2 entities(1)	2018 $m	2017 $m
Common Equity Tier 1 Capital		
Paid-up ordinary share capital	3,418	3,360
Reserves	4	1
Retained profits, including current year profits	394	365
Total Common Equity Tier 1 Capital	3,816	3,726
Regulatory adjustments		
Goodwill and intangibles	(875)	(870)
Deferred expenditure	(178)	(168)
Other deductions	(1)	2
Total regulatory adjustments	(1,054)	(1,036)
Net Common Equity Tier 1 Capital	2,762	2,690
Additional Tier 1 Capital	500	450
Net Tier 1 Capital	3,262	3,140
Tier 2 Capital		
Tier 2 Capital	350	200
General reserve for credit losses	174	202
Net Tier 2 Capital	524	402
Capital base	3,786	3,542
Risk Weighted Assets	29,669	28,644
Common Equity Tier 1 Capital	9.31%	9.39%
Net Tier 1 Capital ratio	10.99%	10.96%
Total Capital Adequacy Ratio	12.76%	12.37%

(1) APRA Prudential Standard APS 001 *Definitions* defines Level 2 as the ADI and all of its subsidiary entities other than non-consolidated subsidiaries. The non-consolidated subsidiaries excluded from Level 2 are:

- Bank of Queensland Limited Employee Share Plans Trust;
- Home Credit Management Pty Ltd;
- St Andrew's Australia Services Pty Ltd;
- St Andrew's Life Insurance Pty Ltd;
- St Andrew's Insurance (Australia) Pty Limited;
- Series 2012-1E REDS Trust;
- Series 2013-1 REDS Trust;
- Series 2015-1 REDS Trust;
- Series 2017-1 REDS Trust; and
- Series 2018-1 REDS Trust.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

3.10 CAPITAL AND RESERVES

(a) Ordinary shares

Ordinary shares

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

Treasury shares

Ordinary shares of the Bank may be purchased from time to time by a controlled entity of the Bank, pursuant to the Awards Right, Restricted Share and Employee Share Plans. Where these shares remain unvested to employees they are treated as treasury shares and deducted from capital as required by AASB 132 *Financial Instruments: Presentation*. No profit or loss is recorded on purchase, sale, issue or cancellation of these shares.

	Consolidated		Bank	
	2018 No of shares	2017 No of shares	**2018 No of shares**	2017 No of shares
MOVEMENTS DURING THE YEAR				
Balance at the beginning of the year – fully paid	**391,739,729**	380,995,702	**391,739,729**	380,995,702
Dividend reinvestment plan	**4,719,312**	9,694,027	**4,719,312**	9,694,027
Issues of ordinary shares (1) (2)	**852,809**	1,050,000	**852,809**	1,050,000
Balance at the end of the year – fully paid	**397,311,850**	391,739,729	**397,311,850**	391,739,729
Treasury shares (included in ordinary shares above):				
Balance at the beginning of the year	**565,308**	537,337	**–**	–
Net acquisitions and disposals during the year	**22,207**	27,971	**–**	–
Balance at the end of the year	**587,515**	565,308	**–**	–

(1) On 26 October 2017, 850,000 ordinary shares were issued at $13.28 and on 17 May 2018, 2,809 ordinary shares were issued at $10.02 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

(2) On 21 October 2016, 1,050,000 ordinary shares were issued at $11.15 to the trustee of the Bank of Queensland Limited Employee Share Plans Trust to satisfy the exercise of award rights and issue of shares under the Award Rights Plan and issue of shares under the BOQ Restricted Share Plan and BOQ Employee Share Plan.

Terms and conditions

Holders of ordinary shares are entitled to receive dividends as determined by the Bank and are entitled to one vote per share at shareholders' meetings. In the event of winding up of the Bank, ordinary shareholders rank after preference shareholders, wholesale capital note holders and creditors and are fully entitled to any residual proceeds of liquidation.

(b) Nature and purpose of reserves

Employee benefits reserve

The employee benefits reserve is used to record the value of share based payments provided to employees, including key management personnel, as part of their remuneration. Refer to Section 6.1 for further details of these plans.

Equity reserve for credit losses

The Bank is required by APRA to maintain a general reserve for credit losses. As the Bank is unable to hold a general provision under current accounting standards, the Bank has created an equity reserve for credit losses. The equity reserve for credit losses and the eligible component of the collective provision for impairment are aggregated for the purpose of satisfying the APRA requirement for a general reserve for credit losses.

Available-for-sale reserve

Changes in the fair value of investments classified as financial assets available-for-sale are recognised in other comprehensive income as described in Section 3.2 and accumulated in a separate reserve within equity. Amounts are reclassified to profit or loss in the Income Statement when the associated assets are sold or impaired.

Cash flow hedge reserve

The hedging reserve is used to record gains or losses on a hedging instrument in a cash flow hedge that are recognised in other comprehensive income, as described in Section 3.8 (b). Amounts are reclassified to profit or loss when the associated hedged transaction affects profit or loss.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

SECTION 4. OTHER ASSETS AND LIABILITIES

4.1 INTANGIBLE ASSETS

	Consolidated					Bank				
	Goodwill $m	Customer related intangibles and brands $m	Computer software $m	Other $m	Total $m	Goodwill $m	Customer contracts $m	Computer software $m	Other $m	Total $m
COST										
Balance as at 1 September 2016	675	130	365	19	1,189	619	89	352	14	1,074
Additions	7	–	46	3	56	–	–	37	3	40
Balance as at 31 August 2017	682	130	411	22	1,245	619	89	389	17	1,114
Balance as at 1 September 2017	682	130	411	22	1,245	619	89	389	17	1,114
Additions	–	–	71	3	74	–	–	68	3	71
Disposals	–	–	(1)	–	(1)	–	–	(1)	–	(1)
Reclassified to held for sale	–	(32)	–	–	(32)	–	–	–	–	–
Balance as at 31 August 2018	**682**	**98**	**481**	**25**	**1,286**	**619**	**89**	**456**	**20**	**1,184**
AMORTISATION AND IMPAIRMENT LOSSES										
Balance as at 1 September 2016	–	105	199	16	320	–	67	193	12	272
Amortisation for the year	–	9	38	5	52	–	8	36	5	49
Impairment	–	–	1	–	1	–	–	–	–	–
Balance as at 31 August 2017	–	114	238	21	373	–	75	229	17	321
Balance as at 1 September 2017	–	114	238	21	373	–	75	229	17	321
Amortisation for the year	–	6	60	2	68	–	5	57	1	63
Impairment	–	–	2	–	2	–	–	2	–	2
Reclassified to held for sale	–	(32)	–	–	(32)	–	–	–	–	–
Balance as at 31 August 2018	**–**	**88**	**300**	**23**	**411**	**–**	**80**	**288**	**18**	**386**
CARRYING AMOUNTS										
Carrying amount as at 1 September 2016	675	25	166	3	869	619	22	159	2	802
Carrying amount as at 31 August 2017	682	16	173	1	872	619	14	160	–	793
Carrying amount as at 31 August 2018	**682**	**10**	**181**	**2**	**875**	**619**	**9**	**168**	**2**	**798**

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

4.1 INTANGIBLE ASSETS (CONTINUED)

Initial recognition and measurement

Intangible assets are stated at cost less any accumulated amortisation and any impairment losses. Expenditure on internally generated goodwill, research costs and brands is recognised in the Income Statement as an expense as incurred.

Subsequent expenditure

Subsequent expenditure on intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Impairment

As part of the Bank's periodic assessment of the carrying value of intangible assets, no material impairment indicators were identified.

Amortisation

Except for goodwill, amortisation is charged to profit and loss in the Income Statement on a straight-line basis over the estimated useful life of the intangible asset unless the life of the intangible asset is indefinite. Where applicable, intangible assets are amortised from the date they are available for use. The amortisation period and method are reviewed on an annual basis. The amortisation rates used in the current and comparative periods are as follows:

	Years
Computer software	3-15
Customer related intangibles and brands	3-12

Impairment testing of the cash generating units containing goodwill

For the purpose of the annual impairment test, goodwill is allocated to groups of cash-generating units (**CGUs**) which represent the Controlled Entity's operating segments - Retail Banking and BOQ Business (refer Section 2.5). The carrying amount of each CGU is compared to its recoverable amount. The recoverable amount is based on the CGU's value in use.

Value in use was determined by discounting the future cash flows generated from the continued use of the CGU. The values assigned to the key assumptions represent management's assessments of future trends in retail banking and are based on both external and internal sources. Below are the key assumptions used in determining value in use:

- Cash flows were initially based on the segment's three year projections as per the Group's Board approved strategic business plan (2017: three years);
- Subsequent cash flows were extrapolated for a further seven years beyond the three year projections incorporating key growth rate assumptions (average cash earnings growth rate of 4.5% driven by an average loan growth of 4%); and
- A post-tax discount rate of 10.0% (2017: 10.0%) and a pre-tax discount rate of 14.3% (2017: 14.3%) was used.

The key assumptions described above may change as economic and market conditions change. The Group estimates that reasonably possible changes in these assumptions would not cause the recoverable amount of either CGU to decline below the carrying amount.

The aggregate carrying amounts of goodwill for each CGU are:

	2018 $m	2017 $m
Retail Banking	288	288
BOQ Business	394	394
Total	682	682

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

4.2 PROVISIONS

A provision is recognised in the Balance Sheet when the Consolidated Entity has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, when appropriate, the risks specific to the liability. The carrying amounts of the provisions recognised are:

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
Employee benefits (1)	24	24	22	21
Leases	1	1	1	1
Provision for non-lending loss (2)	7	10	6	9
Other (3)	2	7	1	2
Total provisions	34	42	30	33

(1) Employee benefits provision consist of annual leave (represents present obligations resulting from employees' services provided up to the reporting date, calculated at discounted amounts based on remuneration wage and salary rates that the Consolidated Entity expects to pay as at reporting date including related on-costs) and long service leave entitlements for employees (represents the present value of the estimated future cash outflows to be made resulting from employees' services provided to reporting date). The provision is calculated using expected future increases in wage and salary rates including related on-costs, and expected settlement dates based on turnover history and is discounted using the rates attached to Australian 10 year corporate bonds at reporting date which most closely match the terms of maturity of the related liabilities. $20 million (2017: $ 20 million) of this provision balance is classified as current.

(2) Included within the non-lending loss provision is $6 million (2017: $6 million) in respect of the Storm Financial settlement, which is classified as non-current.

(3) Other provisions relate to restructuring costs.

Movements in provisions

Movements in each class of provision during the year, other than employee benefits, are as follows:

	Consolidated			Bank		
2018	Leases $m	Non-lending loss $m	Other $m	Leases $m	Non-lending loss $m	Other $m
Carrying amount at beginning of year	1	10	7	1	9	2
Additional provision recognised	-	-	4	-	-	3
Amounts utilised during the year	-	(2)	(3)	-	(2)	(4)
Release of provision	-	(1)	-	-	(1)	-
Reclassification to liabilities held for sale	-	-	(6)	-	-	-
Carrying amount at end of year	1	7	2	1	6	1
Current	1	1	2	1	-	1
Non-current	-	6	-	-	6	-
	1	7	2	1	6	1

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

SECTION 5. INSURANCE BUSINESS

5.1 INSURANCE BUSINESS

On 17 April 2018, the Bank announced it had entered into an agreement to sell the Group's controlled entities, St Andrew's Australia Services Pty Ltd, St Andrew's Insurance (Australia) Pty Ltd and St Andrew's Life Insurance Pty Ltd (**St Andrew's Group**), to Freedom Insurance Group Limited for total consideration of $65 million. The transaction remains subject to certain conditions including receipt of regulatory approvals. The profit on sale will be determined at completion and will be impacted by transaction costs and completion adjustments.

The St Andrew's Group is classified as held for sale at the reporting date of 31 August 2018, refer to Note 6.5(d) for further information.

(a) Basis of preparation

The effective date of the actuarial report on life insurance policy liabilities and regulatory capital requirements is 31 August 2018. The actuarial report was prepared by Mr Stephen Jones, Fellow of the Institute of Actuaries of Australia. This report indicates that Mr Jones is satisfied as to the accuracy of the data upon which life insurance policy liabilities have been determined.

The amount of life insurance and general insurance policy liabilities have been determined in accordance with methods and assumptions disclosed in this financial report and the requirements of applicable accounting standards. Specifically, policy liabilities for life insurance contracts and general insurance contracts are determined in accordance with AASB 1038 *Life Insurance Contracts* and AASB 1023 *General Insurance Contracts* respectively, and LPS 340 *Valuation of Policy Liabilities*. These require policy liabilities to be calculated in a way which allows for the systematic release of planned margins as services are provided to policyholders and premiums are received.

At the reporting date, the projection method was used to determine the life insurance policy liabilities of the level premium funeral cover business. Policy liabilities for all other business were determined using the accumulation method.

The accumulation method values policy liabilities as the provision for unearned premium reserve less a deferred acquisition cost component.

The projection method values life insurance policy liabilities as the net present value of projected policy cash flows (premiums, benefits, expenses and profit margins to be released in future periods), using best estimate assumptions about the future. Future cash flows are discounted at a risk-free discount rate derived from Government bond yields at the reporting date.

Outstanding claims liabilities and Incurred But Not Reported (**IBNR**) liabilities are included in provisions.

(b) Processes used to determine actuarial assumptions

Premium earning pattern

For single premium products, the Unearned Premium Reserve (**UPR**) is based on a premium earning pattern that is similar to the pattern of expected future claim payments. The future claim payments are based on an assessment of the future sum insured (e.g. outstanding loan balances for mortgage and loan protection) and future claims frequencies.

Past experience is used to set these assumptions. This earning pattern is also used to recognise commissions incurred. For regular premium products, the UPR is based on the unearned proportion of premium for the given premium payment frequency.

Mortality and morbidity

Mortality and morbidity assumptions have been based on recent St Andrew's Life Insurance Pty Ltd (**insurance company**) experience, or where data was limited, on the experience of similar products issued by the insurance company. The disputed claims provision is based on individual claim estimates and an assumed 50% probability of disputed claims being incurred.

Future maintenance expenses

For life insurance contracts valued using the projection method, maintenance unit costs are based on budgeted expenses in the year following the reporting date.

Voluntary discontinuances

For life insurance contracts valued using the projection method, voluntary discontinuance assumptions have been based on recent insurance company experience. These rates are derived from the overall discontinuance rate for the individual product group and then further adjusted for duration and premium structure.

Variable	Impact of movement in underlying variable
Mortality rates	For contracts providing death benefits, greater mortality rates would lead to higher levels of claims occurring sooner than anticipated, increasing associated claims cost and therefore reducing profit and shareholder's equity.
Morbidity rates	The cost of disability related claims depends on both the incidence of policyholders becoming disabled and the duration which they remain so. Higher than expected incidence and duration would be likely to increase claim costs, reducing profit and shareholder equity.
Discontinuance rates	Higher than expected policy discontinuance rates reduces future premium income, however this is offset by reduced future claims costs, commissions and maintenance expenses. The likely impact would be to reduce future profit and shareholder equity.
Maintenance expenses	Higher than expected maintenance expenses would reduce future profit and shareholder equity.
Risk-free discount rate	For life insurance contracts valued using the projection method, changes in the risk-free discount rate, such as changes in market yields caused by changes in investment markets and economic conditions, impact both life insurance policy liabilities and asset values at the reporting date.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

5.1 INSURANCE BUSINESS (CONTINUED)

(b) Processes used to determine actuarial assumptions (continued)

Risk-free discount rates

For life insurance contracts valued using the projection method, a risk-free discount rate based on Government bond yields at the reporting date is used. Risk-free rates are term-dependent and as at 31 August 2018 varied from 1.966 to 2.519 per cent.

(c) Sensitivity analysis

Under Margin on Services (**MoS**) reporting, changes in assumptions for life insurance contracts valued using the projection method are generally recognised by adjusting the value of future profit margins in the life insurance policy liabilities. Therefore, where a change in assumptions does not result in loss recognition, there is no impact on the policy liabilities in the current period. As at 31 August 2018, no related product groups were in loss recognition. Changes in assumptions will however give rise to a difference in the emergence of profit margins in future periods. Changes in assumptions will not affect policy liabilities determined using the accumulation method, however, claims provisions would be affected in the current period.

(d) Reconciliation of movements

	2018 $m	2017 $m
RECONCILIATION OF MOVEMENTS IN INSURANCE POLICY LIABILITIES		
Life insurance contract policy liabilities		
Gross life insurance contract liabilities at the beginning of the financial year	11	17
Decrease in life insurance contract policy liabilities (i)	(5)	(6)
Gross life insurance contract liabilities at the end of the financial year	6	11
Liabilities ceded under reinsurance		
Opening balance at the beginning of the financial year	(1)	(1)
Increase in life reinsurance assets (ii)	(1)	-
Closing balance at the end of the financial year	(2)	(1)
Net life policy liabilities at the end of the financial year	4	10
(i) plus (ii) = change in life insurance contract liabilities reflected in the profit for the year	(6)	(6)
Components of net life insurance contract liabilities		
Future policy benefits	28	34
Future charges for acquisition costs	(24)	(24)
Total net life insurance contract policy liabilities	4	10
Components of general insurance liabilities		
Unearned premium liability	4	5
Outstanding claims liability	1	1
	5	6
Total insurance policy liabilities	9	16

Future policy benefits include the unearned premium components of the liability. The accumulation method has been used to calculate policy liabilities and components relating to expenses and profits are not separately calculated.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

5.1 INSURANCE BUSINESS (CONTINUED)

(e) Life insurance regulatory capital requirements

The regulatory capital requirement of each fund and for the subsidiary in total is the amount required to be held in accordance with LPS 110 *Capital Adequacy*. These are amounts required to meet the prudential standards prescribed by the *Life Insurance Act 1995* to provide protection against the impact of fluctuations and unexpected adverse circumstances on the Insurance Company.

The methodology and basis for determining the capital base and regulatory capital requirements are in accordance with relevant prudential requirements.

	2018		2017	
	Statutory Fund No. 1 $m	Shareholders' Fund $m	Statutory Fund No. 1 $m	Shareholders' Fund $m
CAPITAL BASE				
Net assets	34	1	33	1
Add / (subtract) regulatory adjustments to net assets	(15)	–	(16)	–
Total capital base	19	1	17	1
Asset risk charge	1	–	1	–
Operational risk charge	2	–	2	–
Total prescribed capital amount	3	–	3	–
Assets in excess of prescribed capital amount	16	1	14	1
Capital adequacy multiple	7	72	6	58

	2018 $m	2017 $m
COMPOSITION OF CAPITAL BASE		
Common Equity Tier 1 Capital	35	34
Subtract regulatory adjustments to Common Equity Tier 1 Capital	(15)	(16)
Total capital base	20	18
PRESCRIBED CAPITAL AMOUNT		
Statutory Fund No. 1	3	3
Additional amount to meet Insurance company minimum	7	7
Total prescribed capital amount	10	10
Assets in excess of prescribed capital amount	10	8
Capital adequacy multiple	2	2

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

5.1 INSURANCE BUSINESS (CONTINUED)

(e) Life insurance regulatory capital requirements (continued)

Disaggregated information life insurance (before consolidation adjustments)

SUMMARISED INCOME STATEMENT	2018 $m	2017 $m
Revenue		
Life insurance premium revenue	52	51
Investment income	1	1
Net life insurance revenue	53	52
Expenses		
Net claims and other liability expense from insurance contracts	37	35
Other expenses	7	7
	44	42
Profit before income tax	9	10
Income tax expense	(3)	(3)
Profit after income tax	6	7
Statement of sources of profit for statutory funds		
Operating profit after income tax arose from:		
Components of profit related to movement in life insurance liabilities:		
Planned margins of revenues over expenses released	7	9
Difference between actual and assumed experience	(2)	(3)
Investment earnings on assets in excess of life insurance policy liabilities and provision	1	1
SUMMARISED BALANCE SHEET		
Assets		
Investment assets	50	54
Other assets	4	4
	54	58
Liabilities		
Net life insurance liabilities	4	9
Liabilities other than life insurance liabilities	14	15
	18	24
Issued capital, reserves and retained profits		
Directly attributable to shareholders	36	34
	36	34

The life insurance business has no life investment contracts.

(f) Accounting policy

The life insurance operations of the Consolidated Entity are conducted within separate funds as required by the *Life Insurance Act 1995* and is reported in aggregate with the shareholders' fund in the Income Statement, Balance Sheet and Statement of Cash Flows of the Consolidated Entity. The life insurance operations of the Consolidated Entity comprise the selling and administration of life insurance contracts.

Life insurance contracts involve the acceptance of significant insurance risk. Insurance risk is defined as significant if, and only if, an insured event could cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance (i.e. have no discernible effect on the economics of the transaction).

Insurance contracts include those where the insured benefit is payable on the occurrence of a specified event such as death, injury or disability caused by accident or illness.

The insured benefit is either not linked or only partly linked to the market value of the investments held by the Consolidated Entity. Financial risks are substantially borne by the Consolidated Entity.

Monies held in the statutory fund are subject to distribution and transfer restrictions and other requirements of the *Life Insurance Act 1995*.

Under AASB 1038 *Life Insurance Contracts*, the financial statements must include all assets, liabilities, revenues, expenses and equity, irrespective of whether they are designated as relating to shareholders or policy owners. Therefore, the Consolidated Entity's financial statements comprise the total of all statutory funds and the shareholders' fund.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

5.1 INSURANCE BUSINESS (CONTINUED)

(f) Accounting policy (continued)

Insurance contract liability

Profits of the insurance contract business are brought to account on a MoS basis in accordance with guidance provided by LPS 340 *Valuation of Policy Liabilities* as determined by APRA. Under MoS, profit is recognised as fees are received and services are provided to policyholders. When fees are received but the service has not been provided, the profit is deferred. Losses are expensed when identified.

Consistent with the principle of deferring unearned profit is the requirement to defer expenditure associated with the deferred profit. MoS permits costs associated with the acquisition of policies to be charged to profit or loss in the Income Statement over the period that the policy will generate profits. Costs may only be deferred to the extent that a policy is expected to be profitable.

Profit arising from life insurance is based on actuarial assumptions, and calculated as the excess of premiums and investment earnings less claims, operating expenses and the amortisation of acquisition costs that will be incurred over the estimated life of the policies. The profit is systematically recognised over the estimated time period the policy will remain in force.

Under MoS, insurance contract liabilities may be valued using a projection approach or an accumulation approach where this does not result in a material difference to the projection approach. The Insurance Company's Directors and the appointed actuary have deemed the projection approach appropriate for the level premium funeral cover portion of the business, and the accumulation approach appropriate for the remainder of the business. Under the accumulation approach, premiums received are deferred and earned in accordance with the underlying incidence of risk. Costs of acquiring insurance contracts, both direct and indirect, are deferred to the extent that related product groups are expected to be profitable. Under the projection approach, insurance contract liabilities are valued as the net present value of projected policy cash flows (premiums, benefits, expenses and profit margins to be released in future periods), using best estimate assumptions about the future. Future cash flows are discounted at a risk-free discount rate.

Where a related product group is not expected to be profitable, the insurance contract liability is increased by the excess of the present value of future expenses over future revenues.

Revenue recognition

Premiums in respect of life insurance contracts are recognised as revenue in the Income Statement from the date of attachment of risk. Premiums with no due date are recognised as revenue on a cash basis. Premiums with a regular due date are recognised as revenue on an accruals basis. Unpaid premiums are only recognised as revenue during the days of grace or where secured by the surrender value of the policy and are included in the intergroup balance in the Balance Sheet.

Investment income is recognised on an accruals basis. Realised and unrealised gains and losses are included in the Income Statement as investment income.

Claims expense – insurance contracts

Claims incurred all relate to the provision of services, including the bearing of risks, and are treated as expenses.

Claims are recognised when the liability to the policyholder under the policy contract has been established. Claims recognition is based upon:

- cost estimates for losses reported to the close of the financial year; and
- estimated incurred but not reported losses, based upon past experience.

Deferred acquisition costs – life insurance contracts

The fixed and variable costs of acquiring new life insurance business are deferred to the extent that such costs are deemed recoverable from future premiums or policy charges. These costs include commission, policy issue and underwriting costs, certain advertising costs and other sales costs. Acquisition costs deferred are limited to the lesser of the actual costs incurred and the allowance for the recovery of such costs in the premium or policy charges. The actual acquisition costs incurred are recorded in profit or loss in the Income Statement. The value and future recovery of these costs are assessed in determining policy liabilities. This has the effect that acquisition costs are deferred within the policy liability balance and amortised over the period that they will be recovered from premiums or policy charges.

Critical accounting judgements and estimates

The Consolidated Entity's insurance subsidiaries make estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The areas where critical accounting judgements and estimates are applied are noted as:

Policy liabilities

Policy liabilities for life insurance contracts are computed using statistical or mathematical methods, which are expected to give approximately the same results as if an individual liability was calculated for each contract. The computations are made by suitably qualified personnel on the basis of recognised actuarial methods, with due regard to relevant actuarial principles.

The methodology takes into account the risks and uncertainties of the particular classes of life insurance business written. The key factors that affect the estimation of these liabilities and related assets are:

- The cost of providing benefits and administering these insurance contracts;
- Mortality and morbidity experience on life insurance products, including enhancements to policyholder benefits; and
- Discontinuance experience, which affects the Bank's ability to recover the cost of acquiring new business over the lives of the contracts.

In addition, factors such as regulation, competition, interest rates, taxes, securities market conditions and general economic conditions affect the level of these liabilities.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

SECTION 6. OTHER NOTES

6.1 EMPLOYEE BENEFITS

(a) Superannuation commitments

Superannuation plan

The Bank contributes to a number of superannuation plans which comply with the *Superannuation Industry (Supervision) Act 1993*. Contributions are charged to profit or loss in the Income Statement as they are made.

Basis of contributions

Employee superannuation contributions are based on various percentages of employees' gross salaries. The Consolidated Entity's contributions are also based on various percentages of employees' gross salaries.

The Consolidated Entity is under no legal obligation to make superannuation contributions except for the minimum contributions required under the relevant superannuation guarantee legislation.

(b) Share based payments

The Consolidated Entity currently operates an Award Rights Plan for equity-settled compensation. The plan allows the Consolidated Entity's employees to acquire shares in the Bank. The fair value of rights granted is recognised as an employee expense with a corresponding increase to the Employee Benefits Reserve. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the rights. The fair value of the rights granted is measured using industry accepted pricing methodologies, taking into account the terms and conditions upon which the rights are granted. The fair value of the rights is expensed over the vesting period. Where rights do not vest due to failure to meet a non market condition (e.g. employee service period) the expense is reversed. Where rights do not vest due to failure to meet a market condition (e.g. Total shareholder return test) the expense is not reversed.

(i) Description of share based payments

Long-term incentives - Award Rights

The Award Rights Plan was first introduced and approved by shareholders on 11 December 2008, the current Award Rights Plan was approved by shareholders on 30 November 2017. It is an equity based program under which Award Rights are granted as long-term incentives. The two types of award rights currently granted to employees under the plan are Performance Award Rights (**PARs**) and Deferred Award Rights (**DARs**). No amount is payable by employees for the grant or exercise of these award rights.

PARs

The vesting framework for PARs will depend upon when the issue has been granted. For PARs granted prior to December 2015 the vesting framework will be based on the Total Shareholder Return (**TSR**) of the Bank measured against a peer group over a 2 to 3 year period. That peer group consists of the S&P / ASX 200 from time to time, excluding selected entities in resources, real estate investment trusts, telecommunications (offshore headquartered), energy and utilities and such other inclusions and exclusions the Board considers appropriate. TSR is a measure of the entire return a shareholder would obtain from holding an entity's securities over a period, taking into account factors such as changes in the market value of the securities and dividends paid over the period.

One half of an employee's PARs will vest if the Bank's TSR performance over the three year period is in the top 50% of the peer group. All of the PARs vest if the Bank's TSR performance is in the top 25%. For TSR performance between those targets, a relative proportion of the PARs between 50% and 100% would vest. If the Bank's TSR performance is below 50% of the Peer Group, no PARs vest.

For issues granted from December 2015, the vesting framework will also contain an EPS component, with 80% of the employee's PARs to vest based on the Bank's TSR performance measured against a peer group over a three year period. The remaining 20% of PARs vest based on the Bank's EPS performance, measured against a financial services peer group over a three year period.

PARs may be exercised by the employee once they have vested.

DARs

There are no market performance hurdles or vesting conditions for DARs but the holder must remain an employee of the Bank. DARs vest proportionately over three years in the ratio of 20% at the end of year one, 30% at the end of year two and 50% at the end of year three. DARs may be exercised by the employee once they have vested.

Restricted shares

The Consolidated Entity has used shares with restrictions on disposal as a non-cash, share based component of both short term and long term incentive awards.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.1 EMPLOYEE BENEFITS (CONTINUED)

(b) Share based payments (continued)

(ii) Award rights on issue

The number of award rights and restricted shares on issue for the Bank is as follows:

	Deferred Award Rights		Performance Award Rights		Restricted shares	
	2018 '000	2017 '000	2018 '000	2017 '000	2018 '000	2017 '000
Balance at beginning of the year	1,045	1,034	2,377	2,061	228	239
Granted	480	568	822	1,046	156	160
Forfeited / expired	(159)	(164)	(610)	(335)	–	–
Exercised	(367)	(393)	(311)	(395)	(150)	(171)
Outstanding at the end of the year	999	1,045	2,278	2,377	234	228

(iii) Measurement of fair values

The fair value of the PARs and DARs has been measured using the trinomial pricing methodology.

Restricted shares have been valued based on the volume weighted average price of ordinary shares in the Bank sold on the ASX during a 5 day trading period. The shares vest on the respective expiry dates and meeting certain service conditions.

The weighted average of the inputs used in the measurement of the long term incentive award rights grants during the year were as follows:

	Deferred award rights		Performance award rights		Restricted shares	
	2018	2017	2018	2017	2018	2017
Fair value at grant date ($)	11.05	11.45	7.14	6.80	13.03	11.03
Share price at grant date ($)	12.63	11.94	12.66	11.94	12.68	11.95
Expected volatility (%)	22.5	22.9	22.5	22.9	22.5	22.9
Risk free interest rate (%)	1.9	2.0	1.9	2.0	1.9	2.0
Dividend yield (%)	6.6	6.3	6.6	6.3	6.6	6.3

6.2 COMMITMENTS

	Consolidated		Bank	
	2018 $m	2017 $m	2018 $m	2017 $m
(A) LEASE COMMITMENTS				
Future rentals in respect of operating leases (principally in respect of premises) not provided for in these financial statements comprise amounts payable:				
Within 1 year	39	34	39	34
Between 1 year and 5 years	118	104	118	104
Later than 5 years	43	60	43	60
	200	198	200	198
(B) CUSTOMER FUNDING COMMITMENTS				
Guarantees, indemnities and letters of credit	304	321	304	321
Customer funding commitments	1,449	1,412	691	638
	1,753	1,733	995	959

In the normal course of business the Bank makes commitments to extend credit to its customers. Most commitments either expire if not taken up within a specified time or can be cancelled by the Bank within one year. Credit risk is significantly less than the notional amount and does not crystallise until a commitment is funded. Guarantees are provided to third parties on behalf of customers. The credit risks of such facilities are similar to the credit risks of loans and advances.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.3 CONTINGENT LIABILITIES

As at 31 August 2018, the Group does not have any contingent liabilities.

6.4 RELATED PARTIES INFORMATION

(a) Controlled entities

Details of interests in material controlled entities are set out in Section 6.5.

During the year there have been transactions between the Bank and all of its controlled entities. The Bank conducted normal banking business with its operating controlled entities. Amounts owing to or from controlled entities generally attract interest on normal terms and conditions, except in respect of B.Q.L. Management Pty Ltd, BOQ Specialist Pty Ltd, BOQ Share Plans Nominee Pty Ltd, BOQ Home Pty Limited and dormant entities as set out in Section 6.5(a).

The Bank receives management fees from its operating controlled entities except BOQ Home Pty Limited, BOQ Share Plans Nominee Pty Ltd and dormant entities as set out in Section 6.5(a).

The Bank has a related party relationship with equity accounted joint ventures, refer to Section 6.6.

(b) Key management personnel compensation

KMP have authority and responsibility for planning, directing and controlling the activities of the Bank and the Consolidated Entity, including Directors and other Group Executives.

KMP compensation included in 'administrative expenses' and 'employee expenses' (refer to Section 2.2) is as follows:

	Consolidated and Bank	
	2018 $	2017 $
Short term employee benefits	8,893,945	10,201,793
Long term employee benefits	86,018	106,201
Post employment benefits	311,532	353,928
Share based employment benefits	4,754,422	4,853,858
Termination benefits	-	381,167
	14,045,917	15,896,947

Individual Directors and Group Executives compensation disclosures

Information regarding individual Directors and Group Executives compensation and some equity instruments disclosures as permitted by Regulation 2M.3.03 of the *Corporations Regulation 2001* is provided in the Remuneration Report section of the Directors' Report.

Apart from the details disclosed in the Remuneration Report, no Director has entered into a material contract with the Bank since the end of the previous financial year and there were no material contracts involving Directors' interest existing at year end.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.4 RELATED PARTIES INFORMATION (CONTINUED)

(c) Other financial instrument transactions with key management personnel and personally-related entities

A number of the KMP and their close family members hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities. These entities, as well as the KMP and their close family members, are related parties to the Consolidated Entity. Financial instrument transactions with KMP and their related parties during the financial year arise out of the provision of banking services, the acceptance of funds on deposit, the granting of loans and other associated financial activities. The terms and conditions of the transactions entered into with KMP and their related parties were no more favourable than those available, or which might reasonably be expected to be available on similar transactions to non-related entities, on an arm's length basis. No amounts have been written down or recorded as impaired during the year (2017: nil).

The transactions undertaken between the Consolidated Entity and KMP or their related parties up to 31 August 2018 are:

	Balance as at		For the period (1)		
	1 September 2017 $	31 August 2018 $	Total loan drawdowns / (repayments) $	Total loan / overdraft interest $	Total fees on loans / overdraft $
Term products (loans / advances)					
KMP	1,788,768	1,928,903	2,004,249	140,768	600
Other related parties	1,487,199	1,460,422	(84,727)	57,711	240
Total	**3,275,967**	**3,389,325**	**1,919,522**	**198,479**	**840**

(1) Amounts are included only for the period that the Director / Executive is classified as a member of KMP. Michelle Thomsen resigned as an Executive on 29 June 2018. On this basis, loans and advances between the Consolidated Entity and Ms Thomsen are not included in the closing balance as at 31 August 2018.

	Balance as at		For the period (2)		
	1 September 2016 $	31 August 2017 $	Total loan drawdowns / (repayments) $	Total loan / overdraft interest $	Total fees on loans / overdraft $
Term products (loans / advances)					
KMP	1,690,202	1,788,768	19,791	78,415	360
Other related parties	953,899	1,487,199	(2,371,886)	121,065	2,761
Total	2,644,101	3,275,967	(2,352,095)	199,480	3,121

(2) Amounts are included only for the period that the Director / Executive is classified as a member of KMP. Warwick Negus was appointed a Director of the Bank on 22 September 2016. On this basis, existing loans and advances between the Consolidated Entity and related parties of Mr Negus were not included in the opening balances as at 1 September 2016. Related parties of Mr Negus repaid all loans and advances with the Consolidated Entity during the year and these repayments are reflected in the Total Loan Drawdowns / (Repayments) column in the table above.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.4 RELATED PARTIES INFORMATION (CONTINUED)

(c) Other financial instrument transactions with key management personnel and personally-related entities (continued)

Other transactions

Transactions with KMP and their related parties (other than loans and shares) during the financial year were related to personal banking, investment, finance leasing, insurance policy and deposit transactions. These transactions are on normal commercial terms and conditions, in the ordinary course of business and are considered trivial or domestic in nature.

On 26 May 2015, the Bank issued 15,000 Wholesale Capital Notes at a price of $10,000 per note. Details of those notes issued to Directors are set out below:

	2018		2017	
	Balance $	Interest earned $	Balance $	Interest earned $
Roger Davis	200,000	8,798	200,000	8,884
David Willis	70,000	3,079	70,000	3,109
Total	270,000	11,877	270,000	11,993

On 28 December 2017, the Bank issued 3,500,000 Capital Notes at a price of $100 per note. Details of those notes issued to Directors are set out below:

	2018		2017	
	Balance $	Interest earned $	Balance $	Interest earned $
Roger Davis	50,000	1,317	–	–
Roger Davis's related parties	50,000	1,317		
Total	100,000	2,634	–	–

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.5 CONTROLLED ENTITIES

(a) Particulars in relation to material controlled entities

The Group's controlled entities at 31 August 2018 are set out below. Unless otherwise stated, they have share capital consisting solely of ordinary shares that are held directly by the Group. The Bank owns 100% of all controlled entities with nil ownership interest held by non-controlling interests. The country of incorporation or registration is also their principal place of business.

Controlled entities:	Place of business/ country of incorporation	Parent entity's interest 2018 %	Parent entity's interest 2017 %	Amount of investment 2018 $m	Amount of investment 2017 $m	Principal activities
Alliance Premium Funding Pty Ltd	New Zealand	100%	100%	–	–	Dormant
Bank of Queensland Limited Employee Share Plans Trust	Australia	100%	100%	–	–	Trust
BOQ Asset Finance and Leasing Pty Ltd	Australia	100%	100%	–	–	Asset finance & leasing
BOQ Covered Bond Trust	Australia	100%	100%	–	–	Issue of covered bonds
BOQ Credit Pty Limited	Australia	100%	100%	–	–	Asset finance & leasing
BOQ Equipment Finance Limited	Australia	100%	100%	15	15	Asset finance & leasing
BOQF Cashflow Finance Pty Ltd	Australia	100%	100%	–	–	Professional finance
BOQ Finance (Aust) Limited	Australia	100%	100%	230	230	Asset finance & leasing
BOQ Finance (NZ) Limited	New Zealand	100%	100%	22	22	Asset finance & leasing
BOQ Funding Pty Limited	Australia	100%	100%	–	–	Asset finance & leasing
BOQ Home Pty Ltd	Australia	100%	100%	157	157	Investment holding entity
BOQ Share Plans Nominee Pty Ltd	Australia	100%	100%	–	–	Trust management
BOQ Specialist (Aust) Limited (1)	Australia	100%	100%	13	358	Professional finance and asset finance & leasing
BOQ Specialist Pty Ltd	Australia	100%	100%	–	–	Professional finance
B.Q.L. Management Pty Ltd	Australia	100%	100%	–	–	Trust management
B.Q.L. Nominees Pty Ltd	Australia	100%	100%	–	–	Dormant
B.Q.L. Properties Pty Ltd	Australia	–	100%	–	–	Dormant
Home Credit Management Pty Ltd	Australia	100%	100%	–	–	Investment holding entity
Home Financial Planning Pty Ltd	Australia	100%	100%	–	–	Dormant
Hunter Leasing Pty Ltd	Australia	–	100%	–	–	Dormant
Impala Trust No. 1 – Sub-Series 2	Australia	100%	100%	–	–	Securitisation
Newcourt Financial (Australia) Pty Limited	Australia	–	100%	–	–	Dormant
Pioneer Permanent Pty Ltd	Australia	100%	100%	32	32	Dormant
Queensland Electronic Switching Pty Ltd	Australia	–	100%	–	–	Dormant
Series 2007-2 REDS Trust	Australia	–	100%	–	–	Securitisation
Series 2008-1 REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2008-2 REDS Trust	Australia	–	100%	–	–	Securitisation
Series 2009-1 REDS Trust	Australia	100%	100%	–	–	Securitisation

(1) BOQ completed a share capital reduction of $345 million in BOQ Specialist (Aust) Limited during the year, resulting in a decrease in investment of $345 million.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.5 CONTROLLED ENTITIES (CONTINUED)

(a) Particulars in relation to material controlled entities (continued)

Controlled entities:	Place of business/ country of incorporation	Parent entity's interest 2018 %	Parent entity's interest 2017 %	Amount of investment 2018 $m	Amount of investment 2017 $m	Principal activities
Series 2010-1 REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2010-2 REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2012-1E REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2013-1 REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2014-1 EHP REDS Trust	Australia	–	100%	–	–	Securitisation
Series 2015-1 REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2015-1 EHP REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2017-1 REDS Trust	Australia	100%	100%	–	–	Securitisation
Series 2018-1 REDS Trust	Australia	100%	–	–	–	Securitisation
St Andrew's Australia Services Pty Ltd	Australia	100%	100%	–	–	Insurance
St Andrew's Insurance (Australia) Pty Ltd	Australia	100%	100%	–	–	General insurance
St Andrew's Life Insurance Pty Ltd	Australia	100%	100%	–	–	Life insurance
Statewest Financial Planning Pty Ltd	Australia	100%	100%	–	–	Dormant
Statewest Financial Services Pty Ltd	Australia	–	100%	–	–	Dormant
Virgin Money (Australia) Pty Limited	Australia	100%	100%	53	53	Financial services
Virgin Money Financial Services Pty Ltd	Australia	100%	100%	–	–	Financial services
Virgin Money Home Loans Pty Limited	Australia	100%	100%	–	–	Dormant
				522	867	

(b) Significant restrictions

In accordance with APS 222 *Associations with related entities*, the Bank and its subsidiaries that form part of the Extended Licensed Entity have various restrictions. This includes not having unlimited exposures to related entities, including general guarantees.

(c) Acquisition of controlled entities

(i) Accounting for business combinations

Acquisitions on or after 1 July 2009

The Consolidated Entity has adopted revised AASB 3 *Business Combinations* for business combinations occurring in the financial year starting 1 July 2009. All business combinations occurring on or after 1 July 2009 are accounted for by applying the acquisition method. The Consolidated Entity has also adopted AASB 10 *Consolidated Financial Statements* which has superseded AASB 127 *Consolidated and Separate Financial Statements* (as amended in 2008). For every business combination, the Group identifies the acquirer, which is the combining entity that obtains control of the other combining entities or businesses. The Group controls an entity if it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the investee.

Contingent Liabilities

A contingent liability of the acquiree is assumed in a business combination only if such a liability represents a present obligation and arises from a past event, and its fair value can be measured reliably.

Transactions Costs

Transactions costs that the Group incurs in connection with a business combination, such as a finders fee, legal fees, due diligence fees and other professional and consulting fees are expensed as incurred.

(ii) Entities established during the year

The following entities were established during the financial year:

- Series 2018-1 REDS Trust was opened on 24 May 2018.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.5 CONTROLLED ENTITIES (CONTINUED)

(d) Operations classified as held for sale

On 17 April 2018, the Bank announced it had entered into an agreement to sell the Group's controlled entities, St Andrew's Australia Services Pty Ltd, St Andrew's Insurance (Australia) Pty Ltd and St Andrew's Life Insurance Pty Ltd (**St Andrew's Group**), to Freedom Insurance Group Limited for total consideration of $65 million. The transaction remains subject to certain conditions including receipt of regulatory approvals. The profit on sale will be determined at completion and will be impacted by transaction costs and completion adjustments.

The accounting profit on sale will not be material to the Group. The sale of the St Andrew's Group would impact the operating segment, Other. The St Andrew's Group is reported as held for sale in the current financial year. Financial information in relation to the St Andrews Group assets and liabilities held for sale for the period to 31 August 2018 is set out below.

At 31 August 2018, assets and liabilities of the disposal group held for sale are measured at the lower of their carrying amount and fair value less costs of disposal, except for assets such as deferred tax assets, financial assets and contractual rights under insurance contracts, which are specifically exempt from this requirement.

	2018 (1) $m
Cash and cash equivalents	6
Due from other financial institutions – term deposits	46
Other assets	5
Total assets	**57**
Insurance policy liabilities (2)	9
Other liabilities	13
Total liabilities	**22**

(1) Intragroup balances have been eliminated, however, will impact on the final profit on sale on completion.

(2) Refer to section 5 for further information on insurance business disclosures.

(e) Disposal of controlled entities

The following entities were closed during the financial year:

- Series 2007-2 REDS Trust was closed on 4 December 2017;
- Series 2014-1 EHP REDS Trust was closed on 19 March 2018; and
- Series 2008-2 REDS Trust was closed on 6 April 2018.

The following entities were deregistered during the year, effective 2 May 2018:

- B.Q.L. Properties Pty Ltd;
- Hunter Leasing Pty Ltd;
- Newcourt Financial (Australia) Pty Limited;
- Queensland Electronic Switching Pty Ltd; and
- Statewest Financial Services Pty Ltd.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.6 INVESTMENTS IN JOINT ARRANGEMENTS

The Consolidated Entity holds interests in a number of collectively and individually immaterial joint ventures that are accounted for using the equity method. The principal activity of the joint venture entities is land subdivision, development and sale.

(a) Accounting for joint arrangements

The Consolidated Entity's investments in joint venture entities are accounted for under the equity method of accounting in the consolidated financial statements. These are entities in which the Consolidated Entity has joint control over all operational decisions and activities.

(b) Joint venture details

Set out below are the joint ventures of the Consolidated Entity as at 31 August 2018 which, in the opinion of the directors, are immaterial to the Consolidated Entity. Australia is the place of business and also the country of incorporation for all joint ventures. The proportion of ownership interest is the same as the proportion of voting rights held.

	Ownership Interest		Carrying amount	
	2018 (%)	2017 (%)	2018 $m	2017 $m
Ocean Springs Pty Ltd (Brighton)	9.31	9.31	6	6
Dalyellup Beach Pty Ltd (Dalyellup)	17.08	17.08	8	8
East Busselton Estate Pty Ltd (Provence)	25.00	25.00	1	1
Coastview Nominees Pty Ltd (Margaret River)	5.81	5.81	-	-
Provence 2 Pty Ltd (Provence 2)	25.00	25.00	-	-
Total equity accounted investments			15	15

Summary financial information for equity accounted joint ventures, not adjusted for the percentage of ownership held by the Consolidated Entity and fair value adjustments on acquisition, is contained below:

	2018 $m	2017 $m
Profit from continuing operations	3	5
Total comprehensive income	3	5

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.7 AUDITOR'S REMUNERATION

	Consolidated		Bank	
KPMG AUSTRALIA	2018 $000	2017 $000	2018 $000	2017 $000
Audit services				
– Audit and review of the financial reports	1,737	1,561	1,279	1,029
– Other regulatory and audit services	346	250	244	162
	2,083	1,811	1,523	1,191
Audit related services				
– Other assurance services	532	744	399	533
– Regulatory assurance services	235	191	235	191
	767	935	634	724
Non-audit services				
– Taxation services	171	189	171	189
– Other	103	215	103	215
	274	404	274	404

6.8 EVENTS SUBSEQUENT TO BALANCE DATE

The Directors are not aware of any matters or circumstance that have arisen in the interval between the end of the financial year and the date of this report, or any item, event or transaction which significantly affects, or may significantly affect the operations of the Consolidated Entity in future financial years.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.9 SIGNIFICANT ACCOUNTING POLICIES & NEW ACCOUNTING STANDARDS

The accounting policies set out below have been applied consistently to all periods presented in the consolidated financial statements, and have been applied consistently across the Consolidated Entity.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to benefit from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. In the Bank's financial statements, investments in subsidiaries are carried at cost.

(ii) Securitisation

The Consolidated Entity conducts a loan securitisation program whereby mortgage loans are packaged and sold to the RMBS Trusts. The Consolidated Entity also securitises hire purchase, chattel mortgages and finance leases which are packaged and sold to the REDS EHP Trusts. The Bank acquired Impala Trust No. 1 – Sub-Series 2 (**Impala Trust**) through the acquisition of Investec Bank (Australia) Limited. Assets securitised to the Impala Trust are financed by the Bank through the BOQ Specialist channel and consist of medical finance equipment.

Consolidated Entity

The Consolidated Entity receives the residual income distributed by the RMBS and Impala Trust (**Trusts**) after all payments due to investors and associated costs of the program have been met. As a result, the Consolidated Entity is considered to retain the risks and rewards of the Trusts and they do not meet the derecognition criteria of AASB 139.

The Trusts fund their purchase of the loans by issuing floating-rate debt securities. The securities are issued by the Trusts. These are represented as borrowings of the Consolidated Entity, however, the Consolidated Entity does not stand behind the capital value or the performance of the securities or the assets of the Trusts. The Consolidated Entity does not guarantee the payment of interest or the repayment of principal due on the securities. The loans subject to the securitisation program have been pledged as security for the securities issued by the Trusts. The Consolidated Entity is not obliged to support any losses that may be suffered by investors and does not intend to provide such support.

The Bank provides the securitisation programs with arm's length services and facilities, including the management and servicing of the leases securitised.

The Bank has no right to repurchase any of the securitised assets and no obligation to do so, other than in certain circumstances where there is a breach of warranty within 120 days of the sale or when certain criteria are met under the clean up provision per the Trust Deed Supplement.

The transferred assets are equitably assigned to the Trusts. The investors in the securities issued by the Trusts have full recourse to the assets transferred to the Trusts.

Bank

Interest rate risk from the Trusts is transferred back to the Bank by way of interest rate and basis swaps. Accordingly, under AASB 139 the original sale of the mortgages from the Bank to the Trusts does not meet the de-recognition criteria set out in AASB 139. The Bank continues to reflect the securitised loans in their entirety and also recognises a financial liability to the Trusts. The interest payable on the intercompany financial asset / liability represents the return on an imputed loan between the Bank and the Trusts and is based on the interest income under the mortgages, the fees payable by the Trusts and the interest income or expense not separately recognised under the interest rate and basis swaps transactions between the Bank and the Trusts.

All transactions between the Bank and the Trusts are eliminated on consolidation.

(iii) Transactions eliminated on consolidation

Intra-group balances, and any unrealised gains and losses or income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.9 SIGNIFICANT ACCOUNTING POLICIES & NEW ACCOUNTING STANDARDS (CONTINUED)

(b) New accounting standards

New accounting standards applicable this financial year

The following are the amendments to standards and interpretations applicable for the first time in the current year:

- AASB 2016-1 *Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses;*
- AASB 2016-2 *Amendments to Australian Accounting Standards - Disclosure Initiative: Amendments to AASB 107;*
- AASB 2017-2 *Amendments to Australian Accounting Standards – Further Annual Improvements 2014-2016 Cycle; and*
- AASB 1048 *Interpretation of Standards.*

The Consolidated Entity has reviewed the impact of the aforementioned standards and determined there to be no material impact.

New accounting standards applicable in future financial years

The following standards and amendments have been identified as those which may impact the Consolidated Entity in future financial years:

- AASB 9 *Financial Instruments* (**AASB 9**) - The standard introduces changes in the classification and measurement of financial assets and liabilities, a new expected credit loss model for impairment and simplifications to hedge accounting. The standard became mandatory for the Group in the financial year commencing 1 September 2018 and will replace the guidance under AASB 139.

  Impairment

  The Group has developed AASB 9 expected credit loss (**ECL**) models which replaces the previous incurred loss approach under AASB 139. The new models are forward looking, resulting in an acceleration of impairment recognition.

  The Group applies a three-stage approach to measuring the ECL based on credit risk since origination as they transition between the three stages. The Group estimates ECL through modelling the probability of default, loss given default and exposure at default.

  - Stage 1 - Performing - This includes financial assets that have not experienced a significant increase in credit risk since their origination. For these financial assets an allowance equivalent to 12 month's ECL is recognised. This represents the credit losses expected to arise from defaults occurring over the next 12 months.
  - Stage 2 - Under-performing - This includes financial assets that have experienced a significant increase in credit risk since their origination and are not credit impaired. For these financial assets an allowance equivalent to lifetime ECL is recognised. Lifetime ECL is the credit losses expected to arise from defaults occurring over the remaining life of financial assets.
  - Stage 3 - Non-performing (impaired) - This includes financial assets that are credit impaired. The provision is also equivalent to the lifetime ECL. Financial instruments in Stage 3 are subject to either collective or individual impairment assessment.

Key management judgements and assumptions are as follows.

Significant increase in credit risk (SICR)

Significant increase in credit risk for financial assets are assessed by comparing the risk of a default occurring over the expected life of a financial asset at the reporting date compared to the corresponding risk of default at origination. In determining what constitutes a significant increase in credit risk, the Group considers qualitative and quantitative information. For the majority of the Group's Retail portfolio, a mathematical model has been developed to identify a facility's recent behaviour that deteriorates significantly from its origination behaviour. For most of the Group's Commercial portfolio the primary indicator of a significant increase in credit risk is a change in the internal customer risk grade between origination and reporting date. For all loan portfolios, the primary indicator is in addition to the secondary SICR indicator, which is based on 30 days past due arrears information.

ECL measurement and forward-looking information

ECL is a probability weighted credit loss estimated by evaluating a range of possible outcomes and taking into account the time value of money, past events, current conditions and forecasts of future economic conditions.

To calculate ECL, the models multiply the following credit risk factors:

- Probability of default (**PD**): The likelihood that a debtor fails to meet an obligation or contractual commitment;
- Exposure at default (**EAD**): Expected balance sheet exposure at default; and
- Loss given default (**LGD**): The percentage that is not expected to be recovered following default.

These credit risk factors are at a point in time estimates based on the probability weighted forward looking economic scenarios.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.9 SIGNIFICANT ACCOUNTING POLICIES & NEW ACCOUNTING STANDARDS (CONTINUED)

(b) New accounting standards (continued)

The Group considers four macroeconomic scenarios (boom, recovery, slow down and recession) to ensure a sufficient unbiased representative sample is included in estimating ECL.

The inclusion of a forward looking component in the model anticipates changes in the economic outlook, which will likely increase the volatility of the provision. Where applicable, management adjustments may be made to account for situations where known or expected risks and information have not been considered in the modelling process.

Governance

The Executive Credit Committee (**ECC**) has the delegation for reviewing and approving the methodology, and any judgements and assumptions.

The Group holds a Quarterly Economic Forum to discuss and approve future economic forecasts, and the associated probability weights and economic scenarios.

The Group's provision for impairment, impairment on loans and advances and any areas of judgement are reported to the Group's Audit Committee and Board at each reporting period.

Classification and measurement

AASB 9 introduces new classification requirements, which determine how financial assets are categorised and measured. Financial assets are classified according to the Group's business model in place for managing the financial assets and the contractual cash flow characteristics of the financial assets.

Three principle classification categories of financial assets replace the previous AASB 139 classifications and are as follows:

- Amortised cost – financial assets held within a business model where the objective is to hold them in order to collect contractual cash flows. These contractual cash flows represent solely payments of principle and interest (**SPPI**);
- Fair value through other comprehensive income (**FVOCI**) – financial assets held within a business model where the objective is achieved by collecting contractual cash flows and selling financial assets. Contractual cash flows represent SPPI; and
- Fair value through profit or loss (**FVTPL**) – All other financial assets. AASB 9 requires equity instruments to be classified as FVTPL, but there is an option to make an irrevocable election to designate non-traded equity investments as FVOCI.

AASB 9 largely retains the existing classification and measurement requirements of AASB 139 for financial liabilities.

Hedging

The new accounting standard requirements allow for broader application of hedge accounting and to align it more closely with risk management. While the new model does not fundamentally change the types of hedging relationships, it simplifies the effectiveness testing by removing the 80 – 125 per cent thresholds. Adoption of the hedge accounting requirements under AASB 9 is currently optional. The Group has elected to continue applying the hedge accounting requirements under AASB 139.

Transition to AASB 9 and impacts

The classification and measurement, and impairment requirements are applied retrospectively by adjusting opening retained earnings at 1 September 2018. BOQ does not intend to restate comparatives. Transitional and additional disclosures will be included in the Group's 2019 Consolidated Interim Financial Report and the 2019 Annual Report.

BOQ has reported anticipated material movements based on assessment reported to date. The impacts listed below do not constitute a full list of adjustments applicable in the financial year ending 31 August 2019.

Impairment

Based on the financial assets held as at 31 August 2018, economic conditions prevailing at the time and management's judgements and estimates, transition to the AASB 9 impairment requirements has resulted in an increase in the collective provision. The following AASB 9 impacts have been reflected in Group's provision, deferred tax asset and opening retained profits as at 1 September 2018, as follows:

	31 August 2018 $m	AASB 9 impairment impact $m	1 September 2018 $m
Assets			
Loans and advances at amortised cost	45,078	(10)	45,068
Net deferred tax asset	45	3	48
Equity			
Retained profits	400	(7)	393

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.9 SIGNIFICANT ACCOUNTING POLICIES & NEW ACCOUNTING STANDARDS (CONTINUED)

(b) New accounting standards (continued)

Classification and measurement

Available-for-sale and held for trading financial assets are no longer classification categories under AASB 9. As at 31 August 2018, the Group has $5,331 million in these categories, which will be required to be classified as FVOCI or FVTPL.

The Group holds an immaterial amount of unlisted equity instruments which were previously held as an available-for-sale financial asset measured at cost under AASB 139. These instruments are required to be measured at fair value under AASB 9.

From assessment undertaken to date, no other material impacts on the classification and measurement of the Group's financial assets have been identified.

There are no expected material changes to the classification and measurement of financial liabilities as a result of the adoption of AASB 9.

- AASB 15 *Revenue from contracts with customers* (**AASB 15**) – The standard introduces a single model for revenue recognition from contracts with customers and replaces current guidance under AASB 118 *Revenue*, AASB 111 *Construction Contracts* and related interpretations. The standard became mandatory for the Group in the financial year commencing 1 September 2018.

  The core principle of AASB 15 is for an entity to recognise revenue to depict the transfer of promised goods or services to customers. The revenue amount should reflect the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this, the model in AASB 15 features a contract based five-step analysis of transactions to determine the revenue recognition and measurement elements. AASB 15 applies to contracts with customers except for revenue arising from items such as financial instruments, insurance contracts and leases.

  A significant proportion of the Group's revenue is outside the scope of AASB 15, however, certain revenue streams such as commissions, services fees, interchange fees and some others are within the scope of the standard.

  From assessment undertaken to date, no material impacts on the Group's financial statements have been identified. Transitional disclosures will be included in the Group's 2019 Consolidated Interim Financial Report and the 2019 Annual Report.

- AASB 16 *Leases* (**AASB 16**) – The standard will replace AASB 117 *Leases*. It will become mandatory for the Group in the financial year commencing 1 September 2019.

  Lessees are required to recognise a right-of-use (**ROU**) asset and a lease liability for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee measures ROU assets similarly to other non-financial assets and lease liabilities similarly to other financial liabilities. Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments, including inflation-linked payments. It also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease. A depreciation charge will be recognised on ROU assets, while interest expense will be recognised on lease liabilities.

  AASB 16 substantially carries forward the lessor accounting requirements in AASB 117. Accordingly, a lessor continues to classify leases as operating leases or finance leases, accounting for the two types of leases differently.

  The Group is in the process of identifying leases currently held, reviewing existing service contracts for embedded leases and evaluating the quantitative impact of AASB 16. Transition options have been evaluated and the Group will finalise the transition option to adopt in due course. The Group is currently reviewing processes and considering control changes, system requirements and future disclosure requirements.

The following standard is applicable to the Consolidated Entity in future periods but is not expected to have an impact:

- AASB 17 *Insurance Contracts* (**AASB 17**) – The standard will replace AASB 4 *Insurance Contracts*, AASB 1023 *General Insurance Contracts* and AASB 1038 *Life Insurance Contracts*. It will become mandatory for the Group in the financial year beginning 1 September 2021. AASB 17 introduces new measurement approaches to be used in valuing insurance contract liabilities. Under the new model, insurance contract liabilities will represent the present value of future cash flows including a provision for risk. St Andrew's Group is reported as held for sale in the current financial year. Following the sale of the St Andrew's Group, AASB 17 is expected to have no impact on the Group.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.9 SIGNIFICANT ACCOUNTING POLICIES & NEW ACCOUNTING STANDARDS (CONTINUED)

(c) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into Australian dollars at the foreign exchange rate ruling at that date. Non-monetary items in a foreign currency that are measured at historical cost are translated using the exchange rate at the date of the transaction. Foreign exchange differences arising on translation are recognised in the profit and loss. Where a foreign currency transaction is part of a hedge relationship it is accounted for as above, subject to the hedge accounting rules set out in Section 3.8.

(ii) Foreign operations

The Consolidated Entity carries out its foreign operations in New Zealand through the wholly controlled subsidiary, BOQ Finance (NZ) Limited, and through the non-incorporated branch of BOQ Equipment Finance Limited.

(d) Leases

(i) Finance leases

Finance leases in which the Consolidated Entity is the lessor, are recorded in the Balance Sheet as loans and advances at amortised cost. They are recorded on the commencement of the lease as the net investment in the lease, being the present value of the minimum lease payments.

(ii) Operating leases

Operating leases, in which the Consolidated Entity is the lessor, are measured at cost less accumulated depreciation and accumulated impairment losses. Depreciation is calculated to write off the cost of operating lease assets less their estimated residual values using the straight-line basis over the term of the lease. This is generally recognised in profit or loss. Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

Operating leases, in which the Consolidated Entity is the lessee, are expensed on a straight-line basis over the term of the lease, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased property. When an operating lease terminates before the lease period expires, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

(e) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (**GST**), except where the amount of GST incurred is not recoverable from the Australian Tax Office (**ATO**). In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from or payable to the ATO is included as a current asset or current liability in the Balance Sheet.

Cash flows are included in the Statements of Cash Flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from or payable to the ATO are classified as operating cash flows.

(f) Property, plant & equipment

(i) Recognition and initial measurement

Items of property, plant and equipment are stated at cost or deemed cost less accumulated depreciation and accumulated impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads.

(ii) Subsequent costs

Subsequent additional costs are only capitalised when it is probable that future economic benefits in excess of the originally assessed performance of the assets will flow to the Bank in future years. Where these costs represent separate components, they are accounted for as separate assets and are separately depreciated over their useful lives. Costs that do not meet the criteria for subsequent capitalisation are expensed as incurred.

(iii) Subsequent measurement

The Bank has elected to use the cost model to measure property, plant and equipment after recognition. The carrying value is the initial cost less accumulated depreciation and any accumulated impairment losses.

(iv) Depreciation

Depreciation is charged to the profit or loss in the Income Statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment.

The estimated useful lives are as follows:

	Years
IT equipment	3-10
Plant, furniture and equipment	3-20
Leasehold improvements [1]	6-12

(1) Or term of lease if less.

The useful lives are reassessed annually.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 August 2018

6.9 SIGNIFICANT ACCOUNTING POLICIES & NEW ACCOUNTING STANDARDS (CONTINUED)

(g) Impairment of non-financial assets

Non-financial assets, other than deferred tax assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. For goodwill and intangible assets with an indefinite life, the recoverable amount is estimated at the same time each year.

The Bank conducts an annual internal review of non-financial asset values to assess for any indicators of impairment. If any indication of impairment exists, an estimate of the asset's recoverable amount is calculated.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows that are largely independent of the cash inflows from other assets or groups of assets – a CGU. An impairment loss is recognised in profit or loss in the Income Statement for the amount by which the asset's carrying amount exceeds its recoverable amount. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of goodwill allocated to the units, and then to reduce the carrying amounts of the other assets in the unit on a pro-rata basis.

This grouping is subject to an operating segment ceiling test. Non-financial assets, other than goodwill, that suffered impairment are tested for possible reversal of the impairment whenever events or changes in circumstances indicate that the impairment may have reversed. An impairment loss in respect of goodwill is not reversed.

(i) Calculation of recoverable amount

The recoverable amount of a non-financial asset or CGU is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

DIRECTORS' DECLARATION

1. In the opinion of the Directors of Bank of Queensland Limited:

   (a) the consolidated financial statements and notes and the remuneration report included within the Directors' Report set out on pages 60 to 161, are in accordance with the Corporations Act 2001 (Cth), including:

      (i) giving a true and fair view of the financial position of the Bank and Consolidated Entity as at 31 August 2018 and of their performance, for the year ended on that date; and

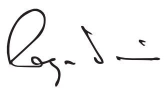
      (ii) complying with Australian Accounting Standards and the Corporations Regulations 2001; and

   (b) there are reasonable grounds to believe that the Bank and Consolidated Entity will be able to pay its debts as and when they become due and payable.

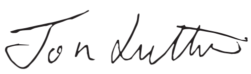
2. The Directors have been given the declarations required by Section 295A of the *Corporations Act 2001* (Cth) from the Managing Director and CEO and Chief Financial Officer for the financial year ended 31 August 2018.

3. The Directors draw attention to Section 1.2 (a) to the financial statements, which includes a statement of compliance with International Financial Reporting Standards.

Signed in accordance with a resolution of the Directors:



Roger Davis
Chairman
3 October 2018



Jon Sutton
Managing Director and CEO
3 October 2018

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

Report on the audits of the Financial Reports

Opinions

We have audited the consolidated **Financial Report** of Bank of Queensland Limited (the Consolidated Entity Financial Report). We have also audited the **Financial Report** of Bank of Queensland Limited (the Bank Financial Report).

In our opinion, each of the accompanying Consolidated Entity Financial Report and Bank Financial Report are in accordance with the *Corporations Act 2001,* including: :

- giving a true and fair view of the **Consolidated Entity 's** and of the **Bank's** financial positions as at 31 August 2018 and of their financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001.*

The respective **Financial Reports** of the Consolidated Entity and the Bank comprise:

- the Balance Sheets as at 31 August 2018
- Income Statements, Statements of comprehensive income, Statements of changes in equity, and Statements of cash flows for the year then ended
- Notes including a summary of significant accounting policies
- Directors' Declaration.

The **Consolidated Entity** consists of Bank of Queensland Limited (the **Bank**) and the entities it controlled at the year-end or from time to time during the financial year.

Basis for opinions

We conducted our audits in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinions.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audits of the Financial Reports* section of our report.

We are independent of the Consolidated Entity and Bank in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audits of the Financial Reports in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

The **Key Audit Matters** we identified for the Consolidated Entity and Bank are:

- Specific and collective impairment provisions for loans and advances at amortised cost
- Valuation of goodwill
- Valuation of intangible computer software
- Fair value measurement of financial instruments
- Information Technology (IT) systems and the control environment.

Key Audit Matters are those matters that, in our professional judgment, were of most significance in our respective audits of the Financial Reports of the current period.

These matters were addressed in the context of our audits of each of the Financial Reports as a whole, and in forming our opinions thereon, and we do not provide a separate opinion on these matters.

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

<table>
<tr><th colspan="2">Specific and collective provisions for impairment of loans and advances at amortised cost (Consolidated Entity: AUD $201m and Bank: AUD $156m)</th></tr>
<tr><td colspan="2">Refer to Section 3.3 Loans and advances at amortised cost and Section 3.6 Risk Management to the Financial Reports</td></tr>
<tr><th>The Key Audit Matter</th><th>How the matter was addressed in our audits</th></tr>
<tr><td>
Impairment provisions are considered to be a Key Audit Matter owing to the significance of loans and advances, the high degree of complexity and judgement applied by the Consolidated Entity and Bank in determining the provisions and the judgement required by us in challenging these estimates.

Specific impairment provisions:
We focused on the significant assumptions the Consolidated Entity and Bank applied in estimating specific impairment provisions, including:
• Expected future cash flows – the Consolidated Entity and Bank forecast future cash flows based on the assessment of an impaired loan and advance specific circumstances. This assessment is complex and will vary according to the individual circumstances of the underlying loan and advance; and
• Estimated recoverable amount of assets held as security – in estimating the specific provision, the Consolidated Entity and Bank will estimate the value of the security through use of external valuation experts and/or various valuation techniques.

Collectively assessed provisions:
An enhanced new collective impairment provision model has been implemented during the year to support the calculation of the collective provision. We focused on the key assumptions used in estimating the collective provision in the model including assessing the Probability of Default (PD) and, were a default to occur, what the loss would be (Loss Given Default (LGD)). The Consolidated Entity and Bank determine these assumptions based on historical loss experience and expert knowledge of the risk characteristics of their portfolios of loans and advances. This estimation is challenging due to use of complex models based on historical loss experience to predict probability of default and loss given default estimates.

Significant judgement is applied in determining the nature and level of model adjustments, which are used where the underlying models may not represent emerging risks or trends in the respective loan portfolios.

AASB 9 Financial Instruments - expected credit loss (ECL) provisions disclosures:
AASB 9 has been implemented from 1 September 2018. This is a new and complex accounting standard which requires considerable judgement and interpretation in its implementation to measure the expected credit loss provisions on loans and advances. Given the complexity in estimating the ECL provision, judgement was required in assessing the accuracy of the disclosure included in the notes to the financial statements.

We involved our senior team members with the assessment of key assumptions applied in the collective provision models given their highly specialised nature.
</td><td>
Our audit procedures included:
• Testing a sample of key credit risk monitoring controls, including controls over loan risk ratings, annual assessments of loans, security valuations, model monitoring and governance and PD and LGD ratios for significant portfolios;
• Testing of a sample of IT system controls, including certain controls over the integrity of the IT systems that are relevant to loans and advances and the calculation inputs into the specific and collective provisions;
• Testing, on a sample basis, specific impairment provisions held against individual loans and advances. This included:
› Comparing the security values used in the formulation of impairment provisions to reports from external valuation experts used by the Consolidated Entity and Bank;
› Comparing the consistency of methods applied in estimating the expected future cash flows and estimated sale proceeds;
› Evaluating the accuracy of previous impairment estimates; and
› Considering current economic conditions and specific areas of credit risk concentration (industries and geographies), which may impact on security values, and challenging the Consolidated Entity's and Bank's judgment with respect to estimated recoverable values;
• Assessing of the adequacy of collectively assessed provisions. Together with the assistance of our credit risk specialists, this included:
› Performing analytical procedures to independently derive an estimate and compared this estimate to the Consolidated Entity's and Bank's collective provisions;
› Testing the completeness and accuracy of key assumptions and data flows into to the collective provision model; and
› Testing governance and control over the application of collective provision model adjustments. This included assessing the components of model adjustments, trends, in the credit risk concentration of specific portfolios, and our understanding of economic conditions in higher–risk geographies; and
• Assessing the adequacy of expected credit loss provisions disclosures including:
› Independently assessing the disclosure of the impact of adopting AASB 9 as it pertains to expected credit losses;
› Testing the completeness and accuracy of key data being transferred to the ECL model, including key data reconciliation controls;
› Testing the controls over the selection and approval of key accounting policy determinations, for example, definition of significant increase in credit risk; and
› Using our credit specialists to assess model methodology and assumptions for a sample of models to determine compliance with AASB 9 and perform an independent recalculation of the provision for all loan portfolios.
</td></tr>
</table>

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

Valuation of goodwill (Consolidated Entity: AUD $682m and Bank: AUD $619m)	
Refer to Section 4.1 Intangible assets to the Financial Reports	
The Key Audit Matter	**How the matter was addressed in our audits**
The assessment of goodwill is considered a Key Audit Matter due to the subjectivity of forward-looking assumptions used in the value-in-use model. In addition, following the adoption of more granular operating segment during the financial year, Management applied the relative fair value approach which required making significant assumptions related to past and forecast financial performance of the newly identified cash generating (**CGUs**). We focused on the significant forward-looking assumptions applied in their value-in-use model, including: • Forecast operating cash-flows, forecast growth rates and the terminal value earnings multiple. The sector in which the Consolidated Entity and Bank operates in is highly competitive and experiencing slower growth and regulatory change making it inherently subjective to estimate the projected cash flow forecast into the future. As the model is sensitive to changes in these assumptions, this drives additional audit effort specific to their feasibility and consistency of the application to the Consolidated Entity and Bank's strategy; and • Discount rate – which is subjective in nature and varies according to the specific conditions and environment of the relevant cash generating unit (**CGU**). We involved our valuation specialists and senior team members with the assessment of this key audit matter.	Our audit procedures included: • Assessing the Consolidated Entity's and Bank's determination of their CGUs based on our understanding of the business and against the requirements of the accounting standards. This included analysis of how independent cash inflows of the Consolidated Entity and Bank were generated, against the requirements of the accounting standards; • Assessing the historical accuracy of forecast operating cash flows and earnings estimates by comparing actual past performance against previous forecasts and growth rates, including alignment to the Consolidated Entity and Bank's Strategic Plan and our inquiries with Management; • Performing sensitivity analysis of key assumptions, in particular discount rates, forecast growth rates and terminal growth rates, to identify those assumptions at a higher risk of bias or inconsistency in application; and • Working with our valuation specialists and using our expertise and industry knowledge to compare the discount rate, growth rate and terminal value earnings multiples to external data to form our own assessments of the feasibility of assumptions used in the model.

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

<table>
<tr><th colspan="2">Valuation of intangible computer software (Consolidated Entity: AUD $181m and Bank: AUD $168m)</th></tr>
<tr><td colspan="2">Refer to Section 4.1 Intangible assets to the Financial Reports</td></tr>
<tr><td>The Key Audit Matter</td><td>How the matter was addressed in our audits</td></tr>
<tr><td>The assessment of value of intangible computer software is considered a Key Audit Matter due to the judgement applied in estimating the value of internally generated computer software and expected useful life.

We focused on the significant assumptions the Consolidated Entity and Bank applied in estimating the value of internally generated computer software, including:

• Capitalisation of costs – The Consolidated Entity's and Bank's estimation of the value of intangible computer software is based on actual costs incurred with external developers and internal staff salary costs. In capitalising these costs, the Consolidated Entity and Bank have performed an analysis to determine the computer software meets the definition of an intangible asset in accordance with the accounting standards. This assessment is subjective in nature. We focused on the allocation of costs incurred to specific phases of a project, including the assumptions and methodologies used in recording and capitalising staff salaries; and

• Expected useful life – Once internally generated computer software is 'ready for -use', the Consolidated Entity and Bank estimate the useful life of the computer software and amortise the asset over this period. This assessment is based on the intended use of the asset. This can be judgemental and dependent upon future events, including advances in technology. We focused on the evidence supporting management's estimation of the useful life period, the utilisation of the computer software, and the analysis of impairment indicators performed by the Consolidated Entity and Bank.</td><td>Our audit procedures included:

• Evaluating the Consolidated Entity's and Bank's capitalisation policy against the capitalisation criteria and guidance set out in the relevant accounting standards;

• For a sample of internally generated computer software projects currently under development, challenging the Consolidated Entity's and Bank's application of the capitalisation policy. We challenged:

› the nature of project costs capitalised by testing a sample of capitalised costs to the project scope of work and the capitalisation criteria of the accounting standards; and

› the Consolidated Entity and Bank assessment of projects not yet classified as 'ready for-use' for any projects with indicators of 'ready for use' and should therefore begin to be amortised over a defined useful life; and

• For a sample of internally generated computer software classified as 'in-use', we challenged the Consolidated Entity's and Bank's estimated period of economic benefit forecast to be realised through the use of the software. We considered the completeness of the Consolidated Entity's and Bank's impairment triggers for the forecasted period of economic benefit.</td></tr>
</table>

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

Fair value measurement of financial instruments

- Financial assets available for sale (Consolidated Entity: AUD $3,946m and Bank: AUD $3,975m)
- Financial assets held for trading (Consolidated Entity and Bank: AUD $1,385m)
- Derivative financial assets (Consolidated Entity: AUD $135m and Bank: AUD $80m)
- Derivative financial liabilities (Consolidated Entity: AUD $294m and Bank: AUD $293m)

Refer to Sections 3.2 Financial assets, 3.6 Risk Management, 3.7 Financial instruments and 3.8 Derivative financial instruments to the Financial Reports

The Key Audit Matter	How the matter was addressed in our audits
This is considered a Key Audit Matter due to the complexity inherent in estimating the fair value of financial instruments. The Consolidated Entity and Bank uses valuation techniques to determine the fair value of financial instruments. The level of judgement and complexity increases where internal models are used to determine fair value, as opposed to quoted market prices. Due to the judgmental nature in the application of valuation techniques, this necessitated additional audit focus, including the use of valuation specialists to assess the suitability and consistency with generally accepted valuation principles.	Our audit procedures included: • Assessing the design and operating effectiveness of certain controls relating to financial instruments measured at fair value, including controls over trade attestations and market risk monitoring processes; and • For financial instruments where the Consolidated Entity and Bank use valuation models to estimate fair value, for a sample of instruments, we worked with our valuations specialists to test the accuracy of the Consolidated Entity's and Bank's valuations using KPMG's independent models. Processes including using external data, independent mark-to-market analysis and assessment of thresholds and deviations were used.

Information Technology (IT) systems and the control environment

Refer to the basis of preparation in Section 1 to the Financial Reports.

The Key Audit Matter	How the matter was addressed in our audits
The IT systems and control environment are considered a Key Audit Matter because the Consolidated Entity's and Bank's operations and financial reporting processes are heavily dependent on IT systems, including automated accounting procedures and IT dependent manual controls. The Consolidated Entity's controls over IT systems include: • The framework of governance over IT systems; • Programmed development and changes; access to process, data and IT operations; and • Governance over generic and privileged user accounts.	Together with our IT specialists, we tested the control environment for key IT applications (systems) used in processing significant transactions and recording balances in the general ledger. We also tested automated controls embedded within these systems. Our audit procedures included: • Evaluating and testing the design and operating effectiveness of certain governance controls over the operational integrity of core systems that are relevant to financial reporting; • Testing the access rights given to staff by checking them to approved records, and inspecting the reports over granting and removal of access rights. We also tested controls related to monitoring of access rights; and • Testing the operating effectiveness of automated controls that are key to our audit testing in order to assess the accuracy of certain system calculations, the generation of certain reports and operation of certain system enforced access controls.

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

Other Information

Other Information is financial and non-financial information in Bank of Queensland Limited's annual reporting which is provided in addition to the Financial Reports and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinions on the Financial Reports do not cover the Other Information and, accordingly, we do not and will not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audits of the Financial Reports, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Reports or our knowledge obtained in the audits, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Reports

The Directors are responsible for:

- preparing the Financial Reports that give a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001;*
- implementing necessary internal controls to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Consolidated Entity and Bank's ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Consolidated Entity or Bank or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audits of the Financial Reports

Our objective is:

- to obtain reasonable assurance about whether each of the Financial Reports as a whole are free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinions.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with *Australian Auditing Standards* will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Report.

A further description of our responsibilities for the audits of the Financial Reports is located at the Auditing and Assurance Standards Board website at: *http://www.auasb.gov.au/auditors_files/ar1pdf.* This description forms part of our Auditor's Report.

KPMG

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Bank of Queensland Limited

Report on the Remuneration Report

Opinion

In our opinion, the Remuneration Report of Bank of Queensland Limited for the year ended 31 August 2018, complies with *Section 300A* of the *Corporations Act 2001*.

Directors' responsibilities

The Directors of the Bank are responsible for the preparation and presentation of the Remuneration Report in accordance with *Section 300A* of the *Corporations Act 2001.*

Our responsibilities

We have audited the Remuneration Report included in pages 60 to 87 of the Directors' report for the year ended 31 August 2018.

Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with *Australian Auditing Standards*.

KPMG

Robert Warren
Partner
Sydney
3 October 2018

SHAREHOLDING DETAILS

As at Friday 21 September 2018, the following shareholding details applied:

1. TWENTY LARGEST ORDINARY SHAREHOLDERS

SHAREHOLDER	No. of ordinary shares	%
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	79,224,388	19.94
J P MORGAN NOMINEES AUSTRALIA LIMITED	34,396,489	8.66
CITICORP NOMINEES PTY LIMITED	18,437,634	4.64
NATIONAL NOMINEES LIMITED	15,992,701	4.03
MILTON CORPORATION LIMITED	7,306,078	1.84
BNP PARIBAS NOMS PTY LTD	3,039,113	0.76
BNP PARIBAS NOMINEES PTY LTD	2,483,552	0.63
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	1,692,986	0.43
WASHINGTON H SOUL PATTINSON AND COMPANY LIMITED	1,344,347	0.34
CITICORP NOMINEES PTY LIMITED	1,232,717	0.31
NAVIGATOR AUSTRALIA LTD	1,137,356	0.29
BKI INVESTMENT COMPANY LIMITED	810,000	0.20
CARLTON HOTEL LIMITED	767,873	0.19
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	756,052	0.19
AMP LIFE LIMITED	721,254	0.18
KARATAL HOLDINGS PTY LTD	692,344	0.17
THE MANLY HOTELS PTY LIMITED	655,540	0.16
PRUDENTIAL NOMINEES PTY LTD	650,000	0.16
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED – A/C 2	610,989	0.15
BOQ SHARE PLANS NOMINEE PTY LTD	584,198	0.15
Total	**172,535,611**	**43.42**

The above table includes shareholders that may hold shares for the benefit of third parties.

Voting rights

On a show of hands every person present who is a holder of ordinary shares or a duly appointed representative of a holder of ordinary shares has one vote, and on a poll each member present in person or by proxy or attorney has one vote for each share that person holds.

SHAREHOLDING DETAILS

As at Friday 21 September 2018, the following shareholding details applied:

2. TWENTY LARGEST CAPITAL NOTES SHAREHOLDERS

SHAREHOLDER	No. of capital notes	%
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	160,291	4.58
NATIONAL NOMINEES LIMITED	146,116	4.17
BNP PARIBAS NOMINEES PTY LTD HUB24 CUSTODIAL SERV LTD DRP	75,642	2.16
JOHN E GILL TRADING PTY LTD	54,593	1.56
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED – A/C 2	40,798	1.17
DOMER MINING CO PTY LTD	32,200	0.92
TRUSTEES OF CHURCH PROPERTY FOR THE DIOCESE OF NEWCASTLE	27,499	0.79
BNP PARIBAS NOMS PTY LTD	21,014	0.60
HAVENFLASH PTY LTD	21,000	0.60
J P MORGAN NOMINEES AUSTRALIA LIMITED	18,400	0.53
ZW 2 PTY LTD	18,000	0.51
ZW 2 PTY LTD	17,200	0.49
NAVIGATOR AUSTRALIA LTD	16,300	0.47
PACIFIC DEVELOPMENT CORPORATION PTY LTD	15,500	0.44
SIMPLY BRILLIANT PTY LTD	15,000	0.43
NAVIGATOR AUSTRALIA LTD	14,829	0.42
FEDERATION UNIVERSITY AUSTRALIA	14,450	0.41
SEYMOUR GROUP PTY LTD	14,000	0.40
MRS NICOLE NAEGER	13,900	0.40
INVIA CUSTODIAN PTY LIMITED	13,795	0.39
Total	**750,527**	**21.44**

The above table includes shareholders that may hold shares for the benefit of third parties.

Voting rights

Capital Notes do not give the holders any voting rights at any general shareholders meetings, except in certain circumstances.

3. DISTRIBUTION OF EQUITY SECURITY HOLDERS

	Ordinary Shares		CPS		Capital Notes	
Category	**2018**	2017	**2018**	2017	**2018**	2017
1 – 1,000	**58,232**	57,437	–	5,537	**5,078**	–
1,001 – 5,000	**31,460**	29,024	–	339	**420**	–
5,001 – 10,000	**6,240**	5,527	–	28	**28**	–
10,001 – 100,000	**3,406**	2,764	–	14	**23**	–
100,001 – and over	**77**	75	–	0	**2**	–
Total	99,415	94,827	–	5,918	5,551	–

The number of ordinary shareholders holding less than a marketable parcel is 2,817.

The number of capital notes holders holding less than a marketable parcel is 4.

SHAREHOLDING DETAILS

4. PARTLY PAID SHARES

There are no partly paid shares.

5. SUBSTANTIAL SHAREHOLDERS

The names of substantial shareholders in the Bank, per the meaning within the *Corporations Act 2001* (Cth), and the number of shares in which each has an interest as disclosed in substantial shareholder notices given to the Bank were:

SUBSTANTIAL SHAREHOLDER	No. of ordinary shares in which interest is held (at date of notification)	Date of notification
The Vanguard Group Inc.	19,929,774	9 July 2018

6. SECURITIES EXCHANGE LISTING

The shares of Bank of Queensland Limited and Capital Notes (BOQPE) are quoted on the Australian Stock Exchange.

BOQ's medium-term notes and covered bonds are listed on the London Stock Exchange.

7. OPTIONS

At 31 August 2018, there were no options over unissued ordinary shares.

8. ON MARKET BUY-BACK

There is no current on market buy-back.

9. OTHER INFORMATION

BOQ is a publicly listed company limited by shares and is incorporated and domiciled in Australia.

SHAREHOLDER INFORMATION

SHARE REGISTRY

Link Market Services Limited

Level 21, 10 Eagle Street
Brisbane Qld 4000

Australia: 1800 779 639
International: +61 2 8280 7626
Email: boq@linkmarketservices.com.au

linkmarketservices.com.au

COMPANY DETAILS

Bank of Queensland Limited
ABN 32 009 656 740
ACN 009 656 740

Registered office:
Level 6, 100 Skyring Terrace
Newstead Qld 4006

Telephone: +61 7 3212 3333
Investor Relations: +61 7 3212 3990

boq.com.au
twitter.com/boq
facebook.com.au/BOQOnline

CUSTOMER SERVICE

Australia: 1300 55 72 72
International: +61 7 3336 2420

Postal address:
GPO Box 898
Brisbane Qld 4001

KEY SHAREHOLDER DATES

Dividend dates for ordinary shares only are:

2018	
Financial full year end	31 August 2018
Full year results and dividend announcement	4 October 2018
Final ex-dividend date	24 October 2018
Final dividend record date	25 October 2018
Final dividend payment date	14 November 2018
Annual General Meeting	29 November 2018

5 YEAR FINANCIAL SUMMARY

$ millions (unless otherwise stated)	2018 $m	2017 $m	2016 $m	2015 $m	2014 $m
FINANCIAL PERFORMANCE					
Net interest income	965	926	937	907	761
Non interest income	145	175	173	180	169
Total income	1,110	1,101	1,110	1,087	930
Operating expenses	(527)	(513)	(520)	(500)	(408)
Underlying profit before tax (1)	583	588	590	587	522
Loan impairment expense	(41)	(48)	(67)	(74)	(86)
Cash earnings before tax	542	540	523	513	436
Cash earnings after tax attributable to ordinary shareholders (2)	372	378	360	357	301
Statutory net profit after tax	336	352	338	318	261
FINANCIAL POSITION					
Gross loans and advances (3)	45,279	43,817	43,152	40,975	38,426
Total assets	52,980	51,658	50,853	48,018	46,905
Customer deposits	31,325	30,190	29,122	26,914	26,266
Total liabilities	49,124	47,869	47,266	44,549	43,564
Total equity	3,856	3,788	3,587	3,469	3,341
SHAREHOLDER PERFORMANCE					
Market capitalisation at balance date	4,565	4,932	4,020	4,698	4,560
Share price at balance date ($)	11.49	12.59	10.55	12.67	12.58
Cash basic earnings per share (cents)	94.7	97.6	95.6	97.3	89.5
Cash diluted earnings per share (cents)	89.3	93.9	90.7	92.2	87.0
Fully franked dividend per ordinary share (cents)	76	76	76	74	66
Fully franked special dividend per ordinary share (cents)	–	8	–	–	–
Cash dividend payout ratio to ordinary shareholders	81%	78% (4)	80%	77%	87%
CASH EARNINGS RATIOS (5)					
Net Interest Margin (6)	1.98%	1.87%	1.94%	1.97%	1.82%
Cost-to-income ratio	47.5%	46.6%	46.8%	46.0%	43.9%
Return on average ordinary equity	9.9%	10.4%	10.3%	10.7%	10.4%
CAPITAL ADEQUACY					
Common equity tier 1 ratio	9.31%	9.39%	9.00%	8.91%	8.63%
Total capital adequacy ratio	12.76%	12.37%	12.29%	12.72%	12.02%

(1) Underlying profit before tax is profit before impairment on loans and advances, significant items and tax.
(2) Cash earnings after tax exclude significant items (tax effected).
(3) Before specific and collective provisions.
(4) This ratio was 87% including special dividend
(5) Excludes impact of significant items.
(6) Excludes amortisation of fair value adjustments (acquisitions).

GLOSSARY

TERM	DESCRIPTION
APRA Prudential Standard (**APS**)	Prudential standards issued by APRA which are applicable to ADIs.
Australian Accounting Standards (**AASB**)	The AASB produces a series of technical pronouncements that set out the measurement and recognition requirements when accounting for particular types of transactions and events, along with the preparation and presentation requirements of an entity's financial statements.
Australian Finance Industry Association (**AFIA**)	AFIA is the national association for the equipment leasing and financing industry. Formerly Australian Equipment Lessors Association (**AELA**).
Australian Prudential Regulation Authority (**APRA**)	APRA is the prudential regulator of the Australian financial services industry. APRA oversees banks, insurance companies, credit unions, building societies, friendly societies and most of the superannuation society.
Australian Securities Exchange (**ASX**)	Australian Securities Exchange or ASX Limited (ABN 98 008 624 691) and the market activities operated by ASX Limited.
Authorised Deposit-Taking Institution (**ADI**)	A corporation which is authorised under the *Banking Act 1959* and includes banks, building societies and credit unions.
Available-for-Sale (**AFS**)	Available-for-sale is an accounting term used to classify financial assets. AFS assets represent securities and other financial investments that are neither held for trading, nor held to maturity. Under IFRS, AFS assets are defined as being all financial assets that do not fall into one of the other IFRS financial asset classifications.
Available Stable Funding (**ASF**)	Available State Funding is the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year.
Average interest earning assets	Average balance over the period for a bank's assets that accrue interest income.
Bank of Queensland Limited (**the Bank or BOQ**)	The Bank is a for-profit entity primarily involved in providing retail banking, leasing finance, and insurance products to its customers.
Basel II and III	A global regulatory framework to improve the regulation, supervision and risk management within the banking system developed by the Basel Committee on Banking Supervision.
Basis points (**bps**)	One per cent of one per cent (0.01%).
Capital Notes (**BOQPE**)	Capital Notes are perpetual, convertible, unguaranteed and unsecured notes issued by BOQ, with preferred, discretionary, non-cumulative distributions. Capital Notes may convert into common shares in certain circumstances as described in the offer documentation of the notes.
Cash Earnings	Cash Earnings is a non-accounting standards measure commonly used in the banking industry to assist in presenting a clear view of underlying earnings.
Committed Liquidity Facility (**CLF**)	The RBA provides a CLF to certain ADIs as part of Australia's implementation of the Basel III liquidity standards. The facility is designed to ensure that participating ADIs have enough access to liquidity to respond to an acute stress scenario, as specified under the relevant APS.
Common Equity Tier 1 (**CET1**)	Capital that is recognised as the highest quality component of capital under APRA prudential standards.
Common Equity Tier 1 ratio (**CET1 ratio**)	CET1 capital divided by total RWA calculated in accordance with relevant APS.
Consolidated Entity (**the Group**)	BOQ and its subsidiaries.
Convertible Preference Shares (**CPS**)	CPS are fully paid, non-cumulative, perpetual, convertible, unguaranteed and unsecured preference shares with preferred, discretionary dividends, issued by the Bank.
Cost to Income ratio (**CTI**)	Operating expenses divided by net operating income.
Corporations Act 2001	*The Corporations Act 2001* (Cth)
Covered bond guarantor	Perpetual Corporate Trust Limited ABN 99 000 341 533, incorporated with limited liability in the Commonwealth of Australia and having its registered office at Level 18, 123 Pitt Street, Sydney, NSW 2000, as trustee of the BOQ Covered Bond Trust (the Trustee).
Days past due (**dpd**)	A loan or lease payment that has not been made by a customer by the due date.

GLOSSARY

TERM	DESCRIPTION
Dividend payout ratio	Dividends paid on ordinary shares divided by earnings.
Dividend reinvestment plan (**DRP**)	A plan which provides shareholders with the opportunity to convert all or part of their entitlement to a dividend into new shares.
Dividend yield	Dividend shown as a percentage of the share price.
Earnings per share (**EPS**)	Measures of earnings attributed to each equivalent ordinary share over a twelve month period. This is calculated by dividing the company's earnings by the weighted average number of shares on issue in accordance with AASB 133 *Earnings per share.*
Effective tax rate	Income tax expense divided by profit before tax.
Equipment Hire Purchase (**EHP**)	EHP trust under the REDS securitisation program, issuing asset backed securities to the term market.
Euro-Commercial Paper (**ECP**)	ECP is an offshore short term commercial paper program.
Euro Medium Term Note (**EMTN**)	EMTN is an offshore medium term note program.
Full Time Equivalent (**FTE**)	A calculation based on number of hours worked by full and part time employees as part of their normal duties.
General Reserve for Credit Losses (**GRCL**)	An estimate of the reasonable and prudent expected credit losses over the remaining life of the portfolio and on non-defaulted assets, not covered by provisions for impairment.
Gross Loans and Advances (**GLA**)	Initially recognised at fair value plus incremental direct transaction costs and subsequently measured at each reporting date at amortised cost using the effective interest method.
High Quality Liquid Asset (**HQLA1**)	Comprises of the Bank's notes and coins and marketable securities representing claims on or guaranteed by the Australian Government or Semi-Government authorities.
Impaired assets	Exposures that have deteriorated to the point where full collection of principal and interest is in doubt.
Interest bearing liabilities	The Bank's liabilities that accrue interest expense.
International Financial Reporting Standards (**IFRS**)	International Financial Reporting Standards and interpretations issued by the International Accounting Standards Board.
Issued capital	Value of securities allotted in a company to its shareholders.
Line of Credit (**LOC**)	A flexible facility that allows a customer to draw down on their approved available credit at any time, as long as the customer does not exceed the approved credit limit.
Liquid assets	All unencumbered RBA repurchase eligible liquid assets including HQLA1 and assets able to be pledged as collateral to the RBA under the CLF.
Liquidity Coverage Ratio (**LCR**)	The ratio of high quality liquid assets that can be converted into cash easily and immediately in private markets, to total net cash flows required to meet the Group's liquidity needs for a 30 day calendar liquidity stress scenario as determined in accordance with APS.
Margin on Services (**MoS**)	MoS is the financial reporting method used by life insurers under Australian Accounting Standards. It requires that revenue from the provision of a life insurance contract is recognised in line with the provision of the life insurance service to the policyholder, over the expected life of the life insurance policy.
Net Interest Margin (**NIM**)	Net interest income divided by average interest-earning assets.
Net Stable Funding Ratio (**NSFR**)	The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding. This ratio should be equal to at least 100% on an on-going basis. "Available stable funding" is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year. The amount of such stable funding required of a specific institution is a function of the liquidity characteristics and residual maturities of the various assets held by that institution as well as those of its off-balance sheet (OBS) exposures.
Net Tangible Assets (**NTA**)	Net tangible assets are calculated as the total assets of a company minus any intangible assets such as goodwill, less all liabilities and the par value of preferred stock.
Non-interest earning assets	The Bank's assets that do not accrue interest income.

GLOSSARY

TERM	DESCRIPTION
Owner Managed Branch (**OMB**)	A branch which is run by a franchisee.
REDS	Term to describe the BOQ securitisation programs.
Reserve Bank of Australia (**RBA**)	The RBA is Australia's central bank and derives its functions and powers from the Reserve Bank Act 1959 (Cth). Its stated duty is to contribute to the stability of the currency, full employment, and the economic prosperity and welfare of the Australian people.
Residential Mortgage Backed Securities (**RMBS**)	BOQ's securitisation programme which enables the trustee to issue debt securities backed by assets originated by the Group such as mortgages and equipment finance receivables.
Return on Average Equity (**ROE**)	Net profit attributable to the owners of the Bank divided by average ordinary equity.
Return on Average Tangible Equity (**ROTE**)	Net profit attributable to the owners of the Bank divided by average ordinary equity less goodwill and identifiable intangible assets.
Required Stable Funding (**RSF**)	Required Stable Funding is an input to the calculation of the net stable funding ratio (NSFR) for bank prudential management purposes. A bank's Required Stable Funding is calculated from its assets, weighted according to their maturity, credit quality and liquidity, together with an amount in relation to off balance sheet commitments.
Risk Weighted Assets (**RWA**)	A quantitative measure of various risks including credit, operational, market and securitisation as defined by APS.
Share / issued capital	Consolidated Entity's issued and paid-up capital.
Total capital adequacy ratio	Total capital divided by total RWA calculated in accordance with relevant APS.
Treasury shares	Shares that the Bank has issued but are held by a trust included within the Bank's consolidated results. Treasury shares are not considered shares outstanding and are not included in 'per share' calculations.
Unearned Premium Reserve (**UPR**)	The UPR represents the total amount of premiums received but not yet earned or recognised as revenue.
Virgin Money Australia (**VMA**)	Virgin Money (Australia) Pty Ltd and its subsidiaries. The VMA entities are subsidiaries of the Group that engage in the provision of financial services (e.g. insurance, superannuation and home lending) on behalf of business partners, including BOQ.
Weighted Average Number of Shares (**WANOS**)	Calculated in accordance with AASB 133 *Earnings per share.*
Wholesale Capital Notes (**WCN**)	WCNs are similar to CPS as the notes may convert into common shares in certain circumstances as described in the offer documentation of the notes.

Bank of Queensland Limited
ABN 32 009 656 740