Resubmitted with Actuarial Report attached

New Zealand

ACE INSURANCE LIMITED

FINANCIAL REPORT

31 DECEMBER 2012

ACE INSURANCE LIMITED

FINANCIAL REPORT 2012

CONTENTS

ACE INSURANCE LIMITED

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 2012

The Board of Directors present the annual report of ACE Insurance Limited ("the Company") incorporating the financial statements and the auditor's report for the year ended 31 December 2012.

In accordance with section 211(3) of the Companies Act 1993, the shareholders have passed a unanimous resolution that the annual report of the Company include only the signed financial statements, the Directors' report for the accounting period completed and an Auditors' report.

The Board of ACE Insurance Limited authorised these financial statements presented on pages 6 to 45 for issue on 3 May 2013.

3rd of May 2013

For and on behalf of the Board of Directors

Director

Director

Date 3 May 2013

Date 3 May 2013

Independent auditor's report to the shareholders of ACE Insurance Limited

Report on the financial report

We have audited the financial statements of ACE Insurance Limited (the Company) on pages 6 to 45, which comprise the statement of financial position as at 31 December 2012, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended, and the notes to the financial statements that include a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial report

The Directors are responsible for the preparation of these financial statements in accordance with generally accepted accounting practice in New Zealand and that they give a true and fair view of the matters to which they relate and for such internal controls as the Directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand) and International Standards on Auditing. These standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider the internal controls relevant to the Company's preparation of financial statements that give a true and fair view of the matters to which they relate, in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

We have no relationship with, or interests in, ACE Insurance Limited other than in our capacities as auditors and providers of other assurance and taxation services. These services have not impaired our independence as auditors of the Company.

PricewaterhouseCoopers, ABN 52 780 433 757
Darling Park Tower 2, 201 Sussex Street, GPO BOX 2650, SYDNEY NSW 1171
T: +61 2 8266 0000, F: +61 2 8266 9999, www.pwc.com.au

pwc

Auditor's opinion

In our opinion, the financial statements on pages 6 to 45:

(i) comply with generally accepted accounting practice in New Zealand; and

(ii) give a true and fair view of the financial position of the Company as at 31 December 2012, and its financial performance and cash flows for the year then ended.

Report on Other Legal and Regulatory Requirements

We also report in accordance with Sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993. In relation to our audit of the financial statements for the year ended 31 December 2012:

(i) we have obtained all the information and explanations that we have required; and

(ii) in our opinion, proper accounting records have been kept by the Company as far as appears from an examination of those records.

Restriction on Distribution or Use

This report is made solely to the Company's shareholders, as a body, in accordance with Section 205(1) of the Companies Act 1993. Our audit work has been undertaken so that we might state to the Company's shareholders those matters which we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

PricewaterhouseCoopers

PricewaterhouseCoopers
Chartered Accountants

I, R Balding, am currently a member of the Institute of Chartered Accountants in Australia and my membership number is 45745.

PricewaterhouseCoopers was the audit firm appointed to undertake the audit of ACE Insurance Limited for the year ended 31 December 2012. I was responsible for the execution of the audit and delivery of our firm's audit report. The audit work was completed on 3 May2013 and an unqualified opinion was issued.

R Balding
Partner

Sydney
3 May 2013

ACE INSURANCE LIMITED

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2012

	NOTE	*2012*	*2011*
		$'000	*$'000*
Net premium revenue		43,459	48,817
Net claims incurred	9	(24,769)	(21,176)
Other underwriting expenses	7	(28,059)	(27,758)
Other underwriting revenue	5	18,233	14,988
Underwriting profit		8,864	14,871
Net investment income	6	2,704	4,472
Profit before income tax		11,568	19,343
Income tax expense	8	(2,646)	(6,357)
Profit after income tax		8,922	12,986
Profit for the year attributable to owners of the Company		8,922	12,986
Other Comprehensive Income			
Gain on revaluation of land and buildings	27(a)	-	240
Other comprehensive income for the year, net of tax		-	240
Total comprehensive income for the year, net of tax attributable to owners of the Company		8,922	13,226

The above statement of comprehensive income should be read in conjunction with the accompanying notes

ACE INSURANCE LIMITED

STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2012

	Note	2012 $000	2011 $000
ASSETS			
Cash and cash equivalents	10	7,871	14,731
Financial assets at fair value through profit or loss	13	68,193	64,738
Trade and other receivables	11	39,316	34,326
Reinsurance and other recoveries receivable	12	177,793	247,552
Reinsurance and other recoveries receivable – Life insurance business	17	27	103
Reinsurance and other recoveries receivable – Life assurance fund	17	914	684
Other assets	16	-	6
Deferred insurance costs	15	25,130	25,269
Tax refund receivable		769	-
Deferred tax assets	20	678	634
Property, plant and equipment	18	2,941	3,336
TOTAL ASSETS		**323,632**	**391,379**
LIABILITIES			
Trade and other payables	21	15,623	15,527
Current tax liabilities		-	4,241
Outstanding claims	24	201,743	271,428
Outstanding claims – Life insurance business	17	39	156
Outstanding claims – Life assurance fund	17	1,342	1,368
Provisions	25	366	431
Unearned premiums	22	57,640	53,466
Unexpired risk liability	23	-	-
Deferred tax liability	20	1,072	877
TOTAL LIABILITIES		**277,825**	**347,494**
NET ASSETS		**45,807**	**43,885**
EQUITY			
Share capital	26	16,900	16,900
Reserves	27(a)	1,242	1,242
Retained earnings	27(b)	27,665	25,743
TOTAL EQUITY		**45,807**	**43,885**

The above statement of financial position should be read in conjunction with the accompanying notes

....
Director

Date 3 May 2013

....
Director

Date 3 May 2013

ACE INSURANCE LIMITED

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2012

	NOTE	CONTRIBUTED EQUITY $000	RESERVES $000	RETAINED EARNINGS $000	TOTAL $000
At 1 January 2011		**16,900**	**1,002**	**12,757**	**30,659**
Profit for the year		-	-	12,986	12,986
Revaluation gain on land and buildings	27(a)	-	240	-	240
Total comprehensive income for the year		-	240	12,986	13,226
Transaction with owners:					
Ordinary dividends		-	-	-	-
Total transactions with owners		-	-	-	-
At 31 December 2011	26, 27	**16,900**	**1,242**	**25,743**	**43,885**

	NOTE	CONTRIBUTED EQUITY $000	RESERVES $000	RETAINED EARNINGS $000	TOTAL $000
At 1 January 2012		**16,900**	**1,242**	**25,743**	**43,885**
Profit for the year		-	-	8,922	8,922
Revaluation gain on land and buildings	27(a)	-	-	-	-
Total comprehensive income for the year		-	-	8,922	8,922
Transaction with owners:					
Ordinary dividends		-	-	(7,000)	(7,000)
Total transactions with owners		-	-	(7,000)	(7,000)
At 31 December 2012	26, 27	**16,900**	**1,242**	**27,665**	**45,807**

The above statement of changes in equity should be read in conjunction with the accompanying notes

ACE INSURANCE LIMITED

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2012

	NOTE	2012 $000	2011 $000
OPERATING ACTIVITIES			
Premiums received		123,906	110,080
Reinsurance and other recoveries received		140,698	108,102
Interest received		4,274	3,783
Rental income received		313	300
Other underwriting revenue		18,233	14,989
Claims paid		(163,862)	(138,171)
Outwards reinsurance paid		(82,644)	(59,315)
Acquisition expenses paid		(7,653)	(7,138)
Other underwriting expenses		(20,467)	(20,726)
Income tax paid		(7,505)	(1,481)
Net cash inflows from operating activities	32	**5,293**	**10,423**
INVESTING ACTIVITIES			
Proceeds from sale of financial assets		28,855	37,981
Purchase of financial assets		(34,037)	(38,988)
Payments for property, plant & equipment		(17)	(69)
Proceeds from sale of property, plant & equipment		46	-
Net cash outflows from investing activities		**(5,153)**	**(1,076)**
FINANCING ACTIVITIES			
Dividends paid		(7,000)	-
Net cash outflows from financing activities		**(7,000)**	**-**
Net increase in cash held		(6,860)	9,347
Cash at beginning of year		14,731	5,384
Cash at end of year	10	**7,871**	**14,731**

The above statement of cash flows should be read in conjunction with the accompanying notes

ACE INSURANCE LIMITED

NOTES TO FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

Contents of the notes to the financial statements **Page**

ACE INSURANCE LIMITED

NOTES TO FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

1. GENERAL INFORMATION

The financial statements are for the reporting entity ACE Insurance Limited. The Company is registered under the Companies Act 1993 and is incorporated and domiciled in New Zealand. The address of the registered office is: CU 1-3, Shed 24, Princes Wharf, Auckland, New Zealand.

The Company is a for-profit entity. The principal activities of the Company during the year were the underwriting of general insurance and the investment of funds.

These financial statements have been authorised for issue by the Board of Directors on 3 May 2013. The Directors have the power to amend the financial statements after issue.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(2.1) Basis of preparation

The financial statements have been prepared in accordance with the Companies Act 1993, the Financial Reporting Act 1993 and with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS). They are also in compliance with International Financial Reporting Standards. They have been prepared under the historical cost convention, as modified by the revaluation of certain assets as identified in specific accounting policies below.

(i) Interpretations to published standards that are not yet effective and have not been early adopted by the Company

The following new interpretations to existing standards have been published that are mandatory for the Company's accounting periods beginning on or after 1 January 2013, or later periods, but that the Company has not early adopted. When applied in future periods, these amended standards are not expected to have a material impact on the Company's results or financial position, however they may have an impact on disclosures.

- NZ IFRS 13: Fair Value Measurement (Application date: 1 January 2013)
- NZ IAS 19: Employee Benefits (Application date: 1 January 2013)
- NZ IFRS 7: Amendments to NZ IFRS 7 Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities and Disclosures – Transition Disclosures (Application date: 1 January 2013)
- NZ IAS 32: Amendments to NZ IAS 32 Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities (Application date: 1 January 2014)
- NZ IFRS 9: Financial Instruments (Application date: 1 January 2015)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.2) Foreign Currency Translations

(i) Functional and presentation currency
Items included in the financial statements are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The financial statements are presented in New Zealand dollars, which is ACE Insurance Limited's functional currency and presentation currency.

(ii) Transactions and balances
Foreign currency transactions during the year are recorded in New Zealand dollars using the rate of exchange prevailing at the date of the transaction. At balance date, amounts receivable and payable in foreign currency are translated at the exchange rate prevailing at that date. Exchange gains and losses are brought to account in determining the profit or loss for the year.

(2.3) Premium Revenue

Direct and inwards reinsurance premiums comprise amounts charged to the policyholders or other insurers, including government levies but excluding amounts collected on behalf of third parties, principally GST. The earned portion of premiums received and receivable, including unclosed business is recognised as revenue. Premiums on unclosed business are brought to account by reference to the previous year's premium processing delays with due allowance for any changes in the pattern of new business and renewals.

Premiums where there is a deposit component are not unbundled where the deposit component can be reliably measured. The rights and obligations arising from any deposit component are immediately recorded as assets and liabilities in the balance sheet.

The pattern of recognition of income over the policy or indemnity periods is based on time, which is considered to closely approximate the pattern of risks underwritten. Unearned premium is determined by apportioning the premium written in the year on a daily pro rata basis.

(2.4) Outwards Reinsurance

Premiums ceded to reinsurers are recorded as an outwards reinsurance expense and are recognised in the Statement of Comprehensive Income from the attachment date over the period of indemnity of the reinsurance contract in accordance with the expected pattern of the incidence of risk ceded.

Reinsurance and other recoveries are recognised as revenue within net claims incurred. Recoveries receivable on outstanding claims are measured as the present value of the expected future receipts, calculated on the same basis as the liability for outstanding claims.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.5) Receivables and Creditors

All debtors are recognised at the amounts receivable as trade debtors. The fair value of trade receivables is deemed to approximate the original amount less any impairment. The impairment is determined by assessing the likelihood of collectability of all trade debtors on a regular basis. Debts that are known to be uncollectible are written off.

Trade and other creditors represent liabilities for goods and services provided to the Company prior to the end of the financial year and which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition for unrelated creditors and within 90 days for related parties.

(2.6) Claims

Claims incurred expense and liabilities for outstanding claims are recognised in respect of the direct and inwards reinsurance business. The liability covers claims incurred but not yet paid, incurred but not yet reported and the anticipated direct and indirect costs of settling those claims. Claims outstanding are assessed by reviewing individual claim files and estimating unnotified claims and settlement costs using statistics based on past experience and trends.

The liability for outstanding claims is measured as the present value of the expected future payments reflecting the fact that all the claims do not have to be paid out in the immediate future. The expected future payments are estimated on the basis of the ultimate cost of settling claims which is affected by factors arising during the period to settlement such as normal inflation and "superimposed inflation". The expected future payments are then discounted to present value at the balance date using a risk free rate. The details of rates applied are included in Note 4.

A risk margin is added to the outstanding claims provision net of reinsurance and other recoveries to increase the probability that the net liability is adequate at a sufficiency level deemed appropriate by the Directors.

(2.7) Acquisition costs

A portion of acquisition costs relating to unearned premium is deferred where it represents future benefits to the Company and can be reliably measured. Deferred acquisition costs are amortised over the period expected to benefit from the expenditure and are stated at the lower of cost and recoverable value.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.8) Unexpired Risk Liability

At each reporting date the Company is required to perform a liability adequacy test and immediately recognise any deficiencies if the carrying amount of unearned premium less any related deferred acquisition costs does not meet estimated future claims costs including risk margins. The liability adequacy test is calculated using 4 portfolios of broadly similar risk based on the clients and product offerings, being Property and Casualty, Accident and Health, Personal Business, and Combined.

The adequacy of the unearned premium liability in respect of each class of business is assessed by considering current estimates of all expected future cash flows to future claims covered by current insurance contracts.

If the present value of the expected future cash flow relating to future claims plus the additional risk margin to reflect the inherent uncertainty in the central estimate exceeds the unearned premium liability less related deferred costs then the unearned premium liability is deemed to be deficient. The Company applies a risk margin to achieve the same probability of sufficiency for future claims as is applied to the outstanding claims liability (note (2.6)).

The entire deficiency, if any, is recognised immediately in the statement of comprehensive income. The deficiency is recognised first by writing down the related deferred acquisition costs with any excess being recorded in the balance sheet as an unexpired risk liability.

(2.9) Financial Assets Backing Insurance Contract Liabilities

All financial assets are deemed to back insurance contract liabilities and are measured at fair value through profit or loss at each balance date. All financial assets are managed and evaluated on a fair value basis which is consistent with the Company's documented investment strategy. They are initially recorded at fair value and are subsequently remeasured at fair value at each balance date. Changes in the fair value of financial assets at the balance date from their fair values at the previous balance date (or cost of acquisition, if acquired during the financial year) are recognised as revenue or expense in the statement of comprehensive income. Fair value is determined for listed equities and quoted debt securities by reference to market quotations.

Regular purchases and sales of investments are recognised on trade-date – the date on which the Company commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

Investment income is brought to account on an accruals basis and dividends are taken into account when received.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.10) Taxation

The income tax expense or revenue for the year is the tax payable on the current year's taxable income adjusted for changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements and changes in unused tax losses.

Deferred tax assets and liabilities are recognised for temporary differences at the tax rates expected to apply when the assets are recovered or liabilities are settled. The relevant tax rates are applied to the cumulative amounts of deductibles and assessable temporary differences to measure the deferred tax assets or liability. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred income tax arises from the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not accounted for. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

(2.11) Property, Plant and Equipment

The Company has taken the option to measure owner occupied freehold land and buildings at fair value at each balance date. Changes in the fair value of owner occupied freehold land and buildings are recognised directly to a revaluation reserve in the balance sheet. Changes in fair value are net of deferred tax.

Fair values for freehold land and buildings are at directors' valuation by reference to an independent valuation and are performed annually. Buildings are depreciated and any adjustments are carried out as part of the revaluation increment or decrement. Any remaining balance in the revaluation reserve is credited to retained earnings when the corresponding property is sold.

Plant and equipment are measured at historical cost less deprecation. Historical cost includes expenditure that is directly attributable to the acquisitions of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Depreciation is calculated on a straight line basis, so as to allocate the cost of the assets or the revalued amounts less their residual value over their useful lives. The rates are as follows:

Buildings	4%
Computer equipment	20% to 36%
Furniture and fittings	7% to 13%
Office equipment	25%

Gains and losses on disposal of fixed assets are taken into account in determining the operating profit for the year.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.12) Intangible Assets

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful life (3 years).

Computer software development costs recognised as an asset are amortised using the straight line method over their useful lives, not exceeding a period of 3 years.

(2.13) Financial Assets

The Company classifies its investments as financial assets at fair value through profit or loss. All other financial assets are classified as loans and receivables.

(i) Financial assets at fair value through profit or loss

A financial asset is classified into the "financial assets at fair value through profit or loss" category at inception if acquired principally for the purpose of selling in the short term, if it forms part of a portfolio of financial assets in which there is evidence of short term profit making, or if so designated by management.

Financial assets designated as at fair value through profit or loss at inception as those that are managed and whose performance is evaluated on a fair value basis. Information about these financial assets is provided internally on a fair value basis to the Company's key management personnel. The Company's investment strategy is to invest in debt securities and to evaluate them with reference to their fair values. Assets that are part of these portfolios are designated upon initial recognition at fair value through profit or loss.

Financial assets that are designated as at fair value through profit or loss are subsequently carried at fair value. Realised and unrealised gains and losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are included in the Statement of Comprehensive Income in the period in which they arise.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active, the Company establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models making maximum use of market inputs and relying as little as possible on entity-specific inputs.

Gains or losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are presented in the Statement of Comprehensive Income within net fair value gains on financial assets at fair value through income in the period in which they arise.

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than those that the Company intends to sell in the short term or that it has designated as at fair value through profit or loss or available for sale. Receivables arising from insurance contracts are also classified in this category and are reviewed for impairment as part of the impairment review of loans and receivables.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.14) Impairment of Non Financial Assets

Assets, other than financial assets, that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

(2.15) Cash and Cash Equivalents

Cash and cash equivalents includes cash on hand, deposits held at call with banks, other short term highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts.

(2.16) Share Capital

Shares are classified as equity when there is no obligation to transfer cash or other assets. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax.

(2.17) Operating Leases

Leases under which all the risks and benefits of ownership are substantially retained by the lessor are classified as operating leases. Payments made under operating leases (net of incentives) are charged to the Statement of Comprehensive Income on a straight line basis over the period of the lease.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.18) Employee Benefits

(i) Wages, Salaries and Annual Leave
Liabilities for employees' entitlements to wages and salaries, annual leave and other current employee entitlements expected to be paid within one year are measured as the amount unpaid at the reporting date at current pay rates in respect of employees' services up to that date. Payments of non-accumulating sick leave are recognised when the leave is taken.

(ii) Long Service Leave
A liability for long service leave is recognised, and is measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date.

Consideration is given to expected future wage and salary levels, experience of employee departures and period of service. Expected future payments are discounted using interest rates at the reporting date on national government guaranteed securities with terms to maturity that match, as closely as possible, the estimated future cash flows.

(iii) Pension obligations
The Company operates a defined contribution pension plan. The scheme is funded through payments to a trust administered fund. A defined contribution plan is a pension plan under which the Company pays fixed contributions to a separate entity. The Company has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits to employee service in the current and prior periods.

The Company pays contributions to a privately administered insurance plan on a mandatory, contractual or voluntary basis. The Company has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due.

(iv) Share based compensation
The Company operates a long term incentive plan under which restricted stock awards are granted. Shares granted are for shares in the Ultimate Parent Entity. For restricted share awards the value of shares on the grant date is expensed over the period that the shares vest.

The fair value of the share options at grant date is independently determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the impact of dilution, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk free interest rate for the term of the option.

(v) Termination benefits
Termination benefits are payable when employment is terminated before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Company recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without the possibility of withdrawal or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after the balance sheet date are discounted to present value.

(vi) Bonus plans
The Company recognises an expense for bonuses. A provision is recognised where contractually obliged or where there is a past practice that has created a constructive obligation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(2.19) Fair Values of Financial Assets and Liabilities

The fair value of cash and cash equivalents and non-interest bearing monetary financial assets and financial liabilities of the entity approximates their carrying amounts.

The fair value of other monetary financial assets and financial liabilities is based upon market prices where a market exists or by discounting the expected future cash flows by the current interest rates for assets and liabilities with similar risk profiles.

(2.20) Statement of Cash Flows

The following are the definitions of the terms used in the Statement of Cash Flows:

(a) Operating activities include all transactions and other events that are not investing or financing activities;
(b) Investing activities are those activities relating to the acquisition, holding and disposal of property, plant and equipment and of investments. Investments include securities not falling within the definition of cash;
(c) Financing activities are those activities that result in changes in size and composition of the capital structure. This includes both equity and debt not falling within the definition of cash. Dividends paid in relation to capital structure are included in financing activities; and
(d) Cash is considered to be cash on hand, current accounts in banks, and deposits on call, net of bank overdrafts.

(2.21) Goods and Services Tax

Revenue, expenses and certain assets are recognised net of the amount of GST, except where the GST is not recoverable. In these circumstances, the GST is included in the related asset or expense. Receivables and payables are stated inclusive of GST. The net amount of GST recoverable from, or payable to, the Inland Revenue Department is included as receivable or a payable in the balance sheet.

(2.22) Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the financial statements.

(2.23) Changes in accounting policies

There have been no significant changes in accounting policies during the current period. Accounting policies have been applied on a basis consistent with the prior year, where applicable.

(2.24) Life claims provision

The Life Claims provision comprises the estimated cost of reported Life claims at balance sheet date.

(2.25) Life assurance fund

The liability is based on a valuation undertaken by Marianne Clifford FSA, MAAA where she completed the 6th schedule and schedule II in terms of section 18 of the Life Assurance Act 1908.

The net liability is derived using values by the 1958 CSO table and the 1952 Disability study tables at 3%.

3. RISK MANAGEMENT POLICIES AND PROCEDURES

The Company's operations are exposed to a number of key risks including insurance risk and financial risk. The Company's policies and procedures in respect of managing these risks are set out below.

(i) Financial risk

The Company's operations are exposed to a variety of financial risks including market risk (including currency and interest rate risks), credit risk and liquidity risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Company.

The Company's principal investment objective is to ensure that funds will be available to meet its primary insurance and reinsurance obligations. Within this broad liquidity constraint, the investment portfolio's structure seeks to maximise return subject to specifically-approved guidelines of overall asset classes, credit quality, liquidity and volatility of expected returns. As such, the investment portfolio is invested primarily in investment-grade fixed income securities as measured by the major rating agencies. The Investment Committee conducts quarterly reviews with funds managers on the portfolio's performance and ensures investment mandates as set by the Company are adhered to.

(a) Market risk
Market risk represents the potential for loss due to adverse changes in the fair value of financial instruments. The Company is exposed to various market risks, including changes in interest rates and foreign currency exchange rates. The investment portfolio consists mainly of fixed income securities, which are sensitive to changes in interest rates.

(b) Credit risk
The significant areas exposed to credit risk are premium collections and reinsurance recoveries on outstanding claims from related parties.

Most premium revenue is derived from brokers operating in the New Zealand insurance market who are subject to industry credit terms. Credit risk arising from reinsurance recoveries is managed by settling the majority of reinsurance recoveries in the month following payment by the Company of the direct claim and monitoring the credit rating of reinsurers on a continual basis. It is also Company policy that all reinsurers are required to be approved by the ACE Global Reinsurance Security Committee.

The investment portfolio is managed following prudent standards of diversification. Specific provisions in the investment mandate limit the allowable holdings of a single issue and issuers.

(c) Liquidity risk
Prudent liquidity risk management implies maintaining sufficient cash and marketable securities to meet the Company's insurance and reinsurance obligations. The Company's cash position is monitored daily and funding requirements are managed through a structured investment portfolio that allows flexibility in funding.

Liquidity risk controls include quarterly actuarial reviews of insurance reserves, matching asset and liability duration and cash flow monitoring.

3. RISK MANAGEMENT POLICIES AND PROCEDURES (continued)

(ii) Insurance risk

(a) Objectives in managing risks arising from insurance contracts and policies for mitigating those risks
Risk management forms part of management's responsibilities and is integrated into the Company's planning process.

The Company's policies and procedures, processes and controls are designed to manage risk. These systems address all material risks, financial and non-financial, likely to be faced by the Company. The Board, aided by the Board Audit Committee and the Enterprise Risk Committee directs and monitors implementation, practice and performance throughout the organisation. Key processes and controls include:

- employment of consistent, disciplined pricing and risk selection in order to maintain a profitable book of business;
- a formal underwriting review process to periodically test compliance standards and guidelines;
- employment of catastrophe loss and risk modeling techniques to ensure that risks are well distributed and those loss potentials are contained within our financial capacity;
- centrally coordinated reinsurance management facilitates appropriate risk transfer and efficient cost-effective use of external reinsurance markets. Reinsurance is placed with a select group of only the most financially secure and experienced companies in the reinsurance industry;
- the maintenance and use of information systems provide up to date and reliable data, thus ensuring integrity of data to management and financial models;
- claims management team ensures there is consistent approach to reserving practices and the settlement of claims;
- all operating units and functional areas are subject to review by a corporate audit team that regularly carries out operational audits; and
- specific guidelines and mandates with respect to investment assets including an independent Investment Committee.

(b) Terms and conditions of insurance and inwards reinsurance business
The terms and conditions attaching to insurance contracts affect the level of insurance risk accepted by the Company. The majority of direct insurance contracts written are entered into on a standard form basis. Inwards reinsurance contracts are subject to substantially the same conditions. There are no special terms and conditions in any non standard contracts that have a material impact on the financial statements.

(c) Concentration of insurance risks
The Company's exposure to concentrations of insurance risk is mitigated by a diverse portfolio of business written across a broad range of locations and industries.

The Company has a specific concentration risk associated with natural catastrophes. This risk is mitigated through a combination of underwriting strategy, management of risk accumulations and reinsurance.

(d) Development of claims
There is a possibility that changes may occur in the estimate of our obligations at the end of a contract period. The tables in note 24(c) show our estimates of total claims outstanding for each underwriting year at successive year ends.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Company makes estimates and judgements in respect of certain key assets and liabilities. 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 resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing material adjustments to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(i) The ultimate liability arising from claims made under non-life insurance contracts

Provision is made at the end of the year for the estimated cost of claims incurred but not settled at the balance date. These reserves include estimates for both claims that have been reported and those that have been incurred but not reported (IBNR), and include estimates of expenses associated with processing and settling these claims.

The process of establishing reserves is subject to considerable variability as it requires the use of informed estimates and judgements. These estimates and judgements are based on numerous factors, and may be revised as additional experience and other data become available or as regulations change.

Outstanding claims provision is estimated by class of business. Historical experience and other statistical information are used to estimate the ultimate claim costs. To determine outstanding claims provisions for a particular line of business, more than one method may be used to estimate ultimate losses and loss expenses and use the results to select a single point estimate. These methods may include, but are not necessarily limited to, extrapolations of historical reported and paid loss data, application of industry loss development patterns to the reported or paid losses, expected loss ratios developed by management, or historical industry loss ratios. Underlying judgments and assumptions that may be incorporated into these actuarial methods include, but are not necessarily limited to, adjustments to historical data used in models to exclude aberrations in claims data such as catastrophes that are typically analysed separately, adjustments to actuarial models and related data for known business changes, such as changes in claims covered under insurance contracts, and the effect of recent or pending litigation on future claims settlements.

Provisions are calculated gross of any reinsurance recoveries and a separate estimate is made of the amounts that will be recoverable from reinsurers.

The following assumptions were made in determining the outstanding claims liabilities:

	2012	**2011**
Discounted average weighted term to settlement from reporting date	1.40	1.35
Ultimate claim numbers - current accident year	4,454	4,828
Average claims size – current accident year	10,515	64,218
Indirect claims handling expense rate	1.4%	1.2%
Discount rate	2.7%	2.8%

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

(i) The ultimate liability arising from claims made under non-life insurance contracts (continued)

The processes used to determine these assumptions are as follows:

Discounted average weighted term to settlement from reporting date
The discounted average weighted term to settlement is calculated separately by class of business based on historical payment patterns. The average term of payment for all short tail classes is relatively small and therefore future inflation of the payment pattern is implicit in the ultimate loss development assumptions. Inflation costs between one accident year and the next is reflected in the average claim size.

Ultimate claim number current year
The ultimate claim number for the current accident year is estimated separately by class of business by projecting the number of claims reported to date based on historical reporting patterns.

Average claims size - current year
The average claim size for the current accident year is estimated separately by class of business by projecting the ultimate claims costs based on historical claim development patterns and dividing by the estimated ultimate claim number.

Indirect claims handling expense rate
The indirect claims handling expense rate is calculated separately by class of business based on historical indirect claims handling expenses as a percentage of historical payments.

Inflation rate
The inflation rate is implicit in the valuation models used so no explicit inflation rate is used in the valuation. Movement in average claim size provides a de facto estimate of the inflation rate implied in the valuation.

Discount rate
The discount rate is derived from market yields of New Zealand Government securities at the balance date.

Risk margin
The overall risk margin is determined allowing for uncertainty of the outstanding claim estimates. Uncertainty is analysed at a total portfolio level which includes an implicit assumption for diversification between individual classes of business.

The assumptions regarding uncertainty are applied to the gross and net central estimates to arrive at an overall provision which is intended to have a 75% (2011: 75%) probability of sufficiency.

The Company conducts sensitivity analysis to quantify the exposure to changes in the key underlying variables. The valuations included in the reported results are calculated using certain assumptions about these variables as disclosed above. The movement in any key variables will impact the performance and equity of the Company. The below table shows how a change in each assumption will affect the outstanding claims liabilities both gross and net of reinsurance and shows an analysis of the sensitivity of the profit/(loss) and equity to changes in these assumptions. As no explicit inflation rate is used in the valuation no sensitivity analysis is able to be carried out for a change in the inflation rate.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Risk margin (continued)

Impact of changes in key variables

		Impact on profit before tax		
		Gross of Reinsurance $'000	Net of Reinsurance $'000	Impact on Equity $'000
Claims incurred per the statement of comprehensive income		94,327	24,769	
Total equity per balance sheet				45,807
Variables:				
Discounted average weighted term to settlement	+0.5 years	91,694	24,438	46,039
	-0.5years	96,966	25,105	45,572
Ultimate claim number	+10%	99,527	26,842	44,356
	-10%	89,127	22,696	47,258
Average claims size	+10%	99,527	26,842	44,356
	-10%	89,127	22,696	47,258
Indirect claims handling expense rate	+1%	96,316	26,758	44,415
	-1%	92,338	22,780	47,199
Discount rate	+1%	92,631	24,427	46,047
	-1%	96,055	25,179	45,520

(ii) Assets arising from reinsurance contracts

Reinsurance recoverable includes the balances due to the Company from reinsurance companies for paid and unpaid losses and loss expenses based on contracts in force, net of uncollectible reinsurance - determined based upon a review of the financial condition of the reinsurers and other factors.

The recognition of reinsurance recoverable requires two key judgements. The first involves the estimation of the gross IBNR to be ceded to reinsurers. Ceded IBNR is developed as part of the loss reserving process and consequently, its estimation is subject to similar risks and uncertainties as the estimation for gross IBNR. The second judgement involves the estimation of the amount of the reinsurance balance that ultimately will not be recovered from reinsurers due to insolvency, contractual dispute, or for other reasons. Amounts estimated to be uncollectible on unpaid losses are reflected in the reinsurance IBNR.

(iii) Unclosed business

Due to insufficient information available at the end of a reporting period to accurately identify the business written with date of attachment of risk prior to the reporting date, provision is made at the end of the financial year to estimate the Company's unclosed business. Unclosed business is estimated using historical data which measures effective date of the transaction against processing date. From this data patterns are modeled and ultimate written premium projected for months where the full amount of the effective premium is yet to be processed. This estimation is adjusted for the impact of recent trends and events and consistency checks are made against historical written premium.

5. REVENUE

	NOTE	*2012* *$'000*	*2011* *$'000*
Revenue from ordinary activities			
Premium revenue:			
Direct		125,200	106,212
Inwards reinsurance		1,136	1,066
		126,336	107,278
Reinsurance and other recoveries revenue	9	69,558	311,054
Investment revenue:			
Investment income	6	4,430	4,017
Commission revenue		18,233	14,988
Total revenue from ordinary activities		218,557	437,337

6. INVESTMENT INCOME

Interest		4,110	3,846
Rental and other		313	300
Foreign exchange losses		7	(129)
Investment and other income before fair value gains	5	4,430	4,017
Net realised and unrealised gains on financial assets held at fair value through profit or loss		(1,726)	455
Net investment income		2,704	4,472

7. EXPENSES

	NOTE	*2012* *$'000*	*2011* *$'000*
Claims expense	9	94,327	332,230
Outwards reinsurance expense		82,877	58,461
Acquisition expenses		7,858	6,176
Underwriting expenses		9,057	9,496
Commission expense		11,144	12,086
Total expenses		205,263	418,449

8. TAXATION

Profit before income tax		11,568	19,343
Permanent difference:			
Expenditure not deductible for tax purposes		78	3,359
Profit subject to tax		11,646	22,702
Prima facie tax payable at 28% (2011: 28%)		3,261	6,357
Over provision in prior year – current tax		(937)	-
Under provision in prior year – deferred tax		322	-
Income tax recognised in statement of comprehensive income		**2,646**	**6,357**
Comprising:			
Estimated current year tax assessment		3,432	6,023
Over provision in prior year		(937)	-
Net movement in deferred tax	20	151	334
		2,646	**6,357**

IMPUTATION BALANCES		
Balance at the beginning of the year	1,585	104
Tax payments (net of refunds)	6,457	1,481
Dividend paid imputation credit	(2,722)	-
Balance at the end of the year	5,320	1,585

9. NET CLAIMS INCURRED

	2012 Current Year $'000	Prior Year $'000	Total $'000	*2011* Current Year $'000	Prior Year $'000	Total $'000
Gross claims expense						
Direct	56,101	36,908	93,009	342,287	(7,919)	334,368
Discount movement	(773)	2,091	1,318	(5,470)	3,332	(2,138)
Discounted gross claims expense	55,328	38,999	94,327	336,817	(4,587)	332,230
Reinsurance and other recoveries revenue						
Reinsurance and other recoveries revenue – undiscounted	(25,478)	(42,749)	(68,227)	(312,176)	(3,895)	(316,071)
Discount movement	(170)	(1,161)	(1,331)	5,422	(405)	5,017
Discounted reinsurance and other recoveries revenue	(25,648)	(43,910)	(69,558)	(306,754)	(4,300)	(311,054)
Net claims incurred	29,680	(4,911)	24,769	30,063	(8,887)	21,176

10. CASH AND CASH EQUIVALENTS

	2012 *$000*	*2011* *$000*
Cash on hand and at bank	5,011	10,841
Deposits at call	2,860	3,890
Total	**7,871**	**14,731**

(a) Cash at bank and on hand

These are interest bearing.

(b) Deposits at call

Short term deposits are bearing floating interest rates averaging 2.72% (2011: 3.05%). These deposits are at call.

11. TRADE AND OTHER RECEIVABLES

	2012 *$'000*	*2011* *$'000*
Premiums and other trade debtors:		
Premiums and other trade debtors receivable – direct insurance	34,176	26,842
Less impairment	(250)	(250)
	33,926	26,592
Premiums and other trade debtors receivable – inwards reinsurance	179	826
Other receivables	5,211	6,908
Total trade and other receivables	39,316	34,326
Current	39,316	34,326
Non current	-	-
Total	39,316	34,326

Movements in the provision for impairment of receivables are as follows:

	2012	2011
Opening balance as at 1 January	250	250
Provision for impairment recognised/(released) during the year	-	-
Total	250	250

12. REINSURANCE AND OTHER RECOVERIES RECEIVABLE

	2012	2011
Reinsurance recoveries on claims paid	1,421	1,388
Expected future reinsurance recoveries on outstanding claims	180,058	251,181
Discount to present value	(3,686)	(5,017)
Total reinsurance and other recoveries	177,793	247,552
Current	139,701	202,311
Non current	38,092	45,241
Total	177,793	247,552

13. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2012 *$'000*	*2011* *$'000*
Government bonds	48,502	47,138
Corporate bonds	19,549	17,448
Life insurance policy loans	142	152
Total financial assets at fair value through profit or loss	68,193	64,738
Current	18,235	4,099
Non current	49,958	60,639
	68,193	64,738

The fair value of investments has been determined based on quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data (Level 2).

The following analysis illustrates the credit rating of financial assets as at the end of the reporting period. This includes deposits at call in Note 10.

S&P rating		
AAA	2%	2%
AA	91%	92%
A	5%	6%
Unrated[1]	2%	-
Total	100%	100%

[1] This represents financial assets rated by Moodys as Baa3.

A sensitivity analysis has been carried out on the portfolio as at the end of the 2011 and 2012 reporting periods. The sensitivity analysis has been performed on the portfolio using a movement in credit spreads. The table below shows the following increases/decreases of an increase in the spread rates of 100 bps on the portfolio:

	Upgraded Impact on Investments ($)	Downgraded Impact on Investments ($)	Upgraded Impact on Equity ($)	Downgraded Impact on Equity ($)
2011	359,604	(359,604)	258,915	(258,915)
2012	374,030	(374,030)	269,302	(269,302)

Using portfolio duration as a measure, an upward/downward parallel shift in the yield curve of 1% would result in the following decreases/increases to the portfolio:

	Upward Impact on Investments ($)	Downward Impact on Investments ($)	Upward Impact on Equity ($)	Downward Impact on Equity ($)
2011	(1,233,794)	1,233,794	(888,332)	888,332
2012	(1,591,916)	1,591,916	(1,146,179)	1,146,719

14. FINANCIAL INSTRUMENTS

(a) Interest rate risk exposures

The Company's exposure to interest rate risk is managed primarily through investments in interest rate futures and adjustments to existing investment portfolios. The Company's exposure to interest rate risk and the effective weighted average interest rate by maturity periods is set out in the following table.

			Fixed interest maturing in:							
2012	**Notes**	**Floating interest rate $'000**	**1 year or less $'000**	**Over 1 to 2 years $'000**	**Over 2 to 3 years $'000**	**Over 3 to 4 years $'000**	**Over 4 to 5 years $'000**	**More than 5 years $'000**	**Non-interest bearing $'000**	**Total $'000**
Financial assets										
Cash and cash equivalents	10	7,871	-	-	-	-	-	-	-	7,871
Receivables	11,12	-	-	-	-	-	-	-	40,737	40,737
Financial assets at fair value through profit or loss	13	-	18,773	6,117	15,443	2,570	25,148	142	-	68,193
		7,871	18,773	6,117	15,443	2,570	25,148	142	40,737	116,801
Weighted average interest rate		2.78%	2.66%	3.63%	3.04%	4.17%	2.96%	6.00%		

2011	**Notes**	**Floating interest rate $'000**	**1 year or less $'000**	**Over 1 to 2 years $'000**	**Over 2 to 3 years $'000**	**Over 3 to 4 years $'000**	**Over 4 to 5 years $'000**	**More than 5 years**	**Non-interest bearing $'000**	**Total $'000**
Financial assets										
Cash and Cash equivalents	10	14,731	-	-	-	-	-	-	-	14,731
Receivables	11,12	-	-	-	-	-	-	-	35,714	35,714
Financial assets at fair value through profit or loss	13	-	4,099	29,961	4,783	22,847	2,037	1,011	-	64,738
		14,731	4,099	29,961	4,783	22,847	2,037	1,011	35,714	115,183
Weighted average interest rate		2.68%	3.97%	2.63%	3.85%	2.96%	4.54%	3.69%	-	

(b) Credit risk exposure

The credit risk on financial assets in the balance sheet is generally the carrying amount, net of any impairment.

(c) Net fair value of financial assets and liabilities

The net fair value of financial assets and financial liabilities is their carrying amounts. As noted in the accounting policy 2.9, investments are measured at fair value through profit or loss at balance date.

15. DEFERRED INSURANCE COSTS

	NOTE	*2012* *$'000*	*2011* *$'000*
Deferred acquisition costs as at 1 January		3,131	2,168
Acquisition costs deferred		3,029	3,168
Write down for premium deficiency	23(b)	-	(37)
Amortisation charged to income		(3,131)	(2,168)
Deferred acquisition costs as at 31 December		3,029	3,131
Deferred reinsurance premiums at 1 January		22,138	18,242
Deferral of reinsurance premiums on contracts entered into in the period		22,308	21,720
Earning of reinsurance premiums on contracts entered into in previous periods		(22,345)	(17,824)
Deferred reinsurance premiums at 31 December		22,101	22,138
Total deferred insurance costs		25,130	25,269

16. OTHER ASSETS

Prepayments	-	6

17. LIFE INSURANCE BUSINESS

	2012 *$000*	*2011* *$000*
Net outstanding claims liability		
Outstanding claims liability	39	156
Reinsurance and other recoveries receivable	(27)	(103)
Asset and liability included in Statement of Financial Position	12	53
Life assurance fund		
Life assurance fund as at 1 January	684	869
Renewal premiums received	73	72
Due and deferred premium adjustment	(2)	2
Less:		
Claims paid/incurred	(221)	(144)
Surrender of policies	(46)	(58)
Reinsurance recoveries	(77)	77
	411	818
Outstanding claims liability – Life assurance fund	1,342	1,368
Reinsurance and other recoveries receivable – Life assurance fund	(914)	(684)
Net Life assurance fund as at 31 December	428	684
Surplus from Life Insurance operations	**(17)**	**134**
Less: claims, underwriting and administration costs	-	(10)
Profit/(Loss) included in Statement of Comprehensive Income	**(17)**	**124**

18. PROPERTY, PLANT AND EQUIPMENT

	2012 *$'000*	*2011* *$'000*
Land and building		
Valuation at 1 January	2,890	2,650
Revaluation	-	240
Valuation at 31 December	2,890	2,890
Office equipment and fittings		
At 31 December:		
Opening net book value	446	947
Additions	17	69
Disposals	(98)	-
Accumulated depreciation on disposal	84	-
Depreciation charge for year	(366)	(570)
Work in progress	(32)	-
Closing net book value	51	446
At 31 December:		
Cost	2,062	1,968
Accumulated depreciation	(2,011)	(1,522)
Net book value	51	446
Total property, plant and equipment	2,941	3,336

Valuation of land and building

The valuation basis of the land and building is fair value being the amounts for which the assets could be exchanged between willing parties in an arm's length transaction, based on current prices in an active market for similar properties in the same location and condition. The 2012 and 2011 valuations were based on independent assessments by qualified valuers. The revaluation surplus net of applicable deferred income taxes was credited to the property revaluation reserve (Note 27(a)).

19. INTANGIBLE ASSETS

	2012 *$000*	*2011* *$000*
Opening net book value	-	17
Movement during year:		
Additions	-	-
Disposals	-	-
Amortisation charge for year	-	(17)
Closing net book value	-	-
At 31 December		
Cost	145	145
Accumulated amortisation	(145)	(145)
Net book value	-	-

20. DEFERRED TAX

	2012	2011
Total deferred tax assets	678	634
Total deferred tax liabilities	(1,072)	(877)
Net deferred tax asset/(liability)	(394)	(243)
Movements:		
Opening balance 1 January	(243)	91
Prior period adjustment	(323)	-
Credited/(charged) to Statement of Comprehensive Income	172	(334)
Closing balance at 31 December	(394)	(243)
Deferred tax assets		
At 1 January	634	698
Prior period adjustment	(99)	-
Depreciation	27	(49)
Unexpired risk liability	-	(153)
Accrued expenses	(31)	34
Employee benefits	147	104
At 31 December	678	634
Deferred tax liabilities		
At 1 January	877	607
Prior period adjustment	224	-
Deferred acquisition costs	(29)	270
At 31 December	1,072	877

21. TRADE AND OTHER PAYABLES

	2012 $000	2011 $000
Outwards reinsurance expense liability – balance due to reinsurers:		
Related companies	3,032	3,852
Non related companies	4,804	3,788
Other creditors and accruals	7,787	7,887
Total trade and other payables	15,623	15,527
Current	15,623	15,527
Non-current	-	-
	15,623	15,527

22. UNEARNED PREMIUMS

	2012 $000	2011 $000
Unearned premium liability as at 1 January	53,466	44,374
Movement in unearned premium		
Deferral of premiums on contracts written at year end	57,404	52,484
Earning of premiums deferred in prior years	(53,230)	(43,392)
Unearned premium liability as at 3 December	57,640	53,466
Current	57,125	52,302
Non-current	515	1,164
	57,640	53,466

The unearned premium liability is subject to a Liability Adequacy Test as described in accounting policy (2.8). Details of the amounts recognised in respect of any surplus/deficiency are set out in Note 23.

23. UNEXPIRED RISK LIABILITY

(a) Unexpired Risk Liability

	2012 $000	2011 $000
Unexpired risk liability as at 1 January	-	547
Recognition of unexpired risk liability in the period	-	-
Release of unexpired risk liability recorded in the previous year	-	(547)
Unexpired risk liability as at 31 December	-	-

(b) Release recognised in the Statement of Comprehensive Income

	2012 $000	2011 $000
Net movement in unexpired risk liability	-	(547)
Write down of deferred acquisition costs	-	37
Total release recognised in the Statement of Comprehensive Income	-	**(510)**

24. OUTSTANDING CLAIMS

(a) Outstanding claims liability

	2012 *$000*	*2011* *$000*
Central estimate of outstanding claims liability	179,874	242,376
Risk margin	23,968	32,207
Claim handling expenses	2,604	2,866
Total undiscounted claims liability	206,446	277,449
Discount to present value	(4,703)	(6,021)
Total discounted claims liability	**201,743**	**271,428**
Current	153,734	216,238
Non-current	48,009	55,190
	201,743	**271,428**

(b) Gross risk margins applied

	2012	2011
New Zealand	13.1%	13.1%

(c) Reconciliation of movement in discounted outstanding claims liability

	2012			2011		
	Gross $'000	Reinsurance $'000	Net $'000	Gross $'000	Reinsurance $'000	Net $'000
Brought forward	271,428	246,164	25,264	77,459	48,794	28,665
Effect of changes in assumptions	49,682	48,276	1,406	(1,286)	815	(2,101)
Increase in claims incurred/recoveries anticipated over the year	44,645	21,282	23,363	333,516	310,239	23,277
Incurred claims recognised in statement of comprehensive income	94,327	69,558	24,769	332,230	311,054	21,176
Claims payments/recoveries during the year	(164,012)	(139,350)	(24,662)	(138,261)	(113,684)	(24,577)
Carried forward	201,743	176,372	25,371	271,428	246,164	25,264

24. OUTSTANDING CLAIMS (continued)

(c) Claims development tables:

The following table shows the development of gross and net undiscounted outstanding claims relative to the ultimate expected claims for the five most recent accident years.

Gross

Accident year	**2006 & Prior $000**	**2007 $000**	**2008 $000**	**2009 $000**	**2010 $000**	**2011 $000**	**2012 $000**	**Total $000**
Estimate of ultimate claims cost:								
At end of accident year		6,849	7,776	5,867	6,396	6,106	8,434	
One year later		5,919	9,382	5,612	5,250	5,296	-	
Two years later		6,727	8,530	4,663	4,298	-	-	
Three years later		5,109	7,098	4,264	-	-	-	
Four years later		4,980	6,131	-	-	-	-	
Five years later		4,712	-	-	-	-	-	
Six years later								
Current estimate of cumulative claims cost		4,712	6,131	4,264	4,298	5,296	8,434	
Cumulative payments		4,002	3,845	1,498	1,501	733	83	
Outstanding claims undiscounted	2,405	710	2,286	2,766	2,797	4,563	8,351	23,878
Discount	118	44	109	136	164	249	601	1,421
Outstanding claims	2,287	666	2,177	2,630	2,633	4,314	7,750	22,457
Short tail outstanding claims								153,375
Claims handling expenses								2,500
Total gross central estimate								178,332
Risk margin								23,411
Total gross outstanding claims per statement of financial position								**201,743**

24. OUTSTANDING CLAIMS (continued)

Net

Accident year	2006 & Prior $000	2007 $000	2008 $000	2009 $000	2010 $000	2011 $000	2012 $000	Total $000
Estimate of ultimate claims cost:								
At end of accident year		3,748	5,157	3,192	3,278	3,281	3,125	
One year later		4,169	5,263	2,759	2,604	2,745	-	
Two years later		3,831	4,816	2,807	2,308	-	-	
Three years later		3,406	4,095	3,124	-	-	-	
Four years later		2,950	3,448	-	-	-	-	
Five years later		2,924	-	-	-	-	-	
Current estimate of cumulative claims cost		2,924	3,448	3,124	2,308	2,745	3,125	
Cumulative payments		2,712	2,498	1,383	1,436	618	55	
Outstanding claims undiscounted	1,352	212	950	1,741	872	2,127	3,070	10,324
Discount	64	12	46	87	48	115	243	615
Outstanding claims	1,288	200	904	1,654	824	2,012	2,827	9,709
Short tail outstanding claims								10,221
Claims handling expenses								2,500
Total net central estimate								22,430
Risk margin								2,941
Total net outstanding claims per statement of financial position								**25,371**

25. PROVISIONS

	2012 $'000	*2011 $'000*
Employee benefits	366	431
	366	431
Current	270	347
Non-Current	96	84
	366	431

26. SHARE CAPITAL

	2012 *$000*	*2011* *$000*
Issued share capital at 1 January	16,900	16,900
Shares issued during the year	-	-
Issued share capital at 31 December	**16,900**	**16,900**

As at 31 December 2012, the Company had 16,899,558 (2011: 16,899,558) ordinary shares that were issued for 100 cents per share. All issued shares are fully paid. Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of and amounts paid on the shares held. Each share is entitled to one vote.

27. RESERVES AND RETAINED EARNINGS

(a) Reserves

Property revaluation reserve	1,242	1,242
	1,242	1,242

Movements:

Property revaluation reserve:		
Balance at the beginning of the year	1,242	1,002
Revaluation	-	240
Balance at end of year	**1,242**	**1,242**

(b) Retained earnings

Balance at the beginning of year	25,743	12,757
Profit for the year	8,922	12,986
Dividends paid	(7,000)	-
Balance at end of year	**27,665**	**25,743**

(c) Nature and purpose of reserves

(i) Property revaluation reserve

The property, plant and equipment revaluation reserve is used to record increments and decrements on the revaluation of owner occupied freehold land and buildings. Revaluation increments and decrements are taken directly to the reserve account as described in accounting note 2.11.

28. SOLVENCY CAPITAL REQUIREMENTS

The Company maintains a Minimum Solvency Capital policy that provides guidance to the level of capital maintained and approved by the Board of Directors. The objective of this policy is to hold sufficient levels of capital that is commensurate with the Company's overall risk profile and to maintain a level that enables efficient use of capital.

The Minimum Solvency Capital required to be retained to meet solvency requirements are shown below. The Actual Solvency Capital exceeds the minimum requirements by $15,756,000.

	2012
	$000
Actual Solvency Capital	45,807
Minimum Solvency Capital	30,051
Solvency Margin	15,756
Solvency Coverage multiple	1.52

The methodology and bases for determining the Solvency Margin are in accordance with the requirements of the Solvency Standards published by the Reserve Bank of New Zealand. The Company has applied the materiality provisions in those standards.

29. COMMITMENTS AND CONTINGENT LIABILITIES

(a) Capital expenditure commitments

At year end there is no estimated capital expenditure under contract but not recognised as liabilities in the financial statements of the Company.

(b) Operating lease commitments

	2012	*2011*
	$000	*$000*
Commitments in relation to leases contracted for at the reporting date but not recognised as liabilities, payable:		
Not later than one year	145	375
Later than one year but not later than five years	48	196
Later than five years	-	-
Non cancellable operating leases	193	571

The Company leases office premises in Wellington and Auckland. The leases are both subject to renewal rights and have varying terms. On renewal, the terms of the leases are renegotiated.

(c) Contingent liabilities

During 2011 the Company received personal grievance claims from an employee (formerly a contracted agent with Combined Insurance) and two contracted agents in the Combined Division. The employee left the Company during 2012.

The personal grievance claim received from a former employee and the subject of Employment Relations Authority proceedings during 2012 was settled in December 2012, with no further liability to the Company. The two former contracted agents in the Combined Division threatened personal grievance claims in 2012, which included claims that they were employees rather than independent contractors. Neither agent has formerly pursued any claim against the Company.

As at 31 December 2012, there were no other contingent liabilities.

30. REMUNERATION OF AUDITORS

During the year the auditors of the Company, PricewaterhouseCoopers, were paid for the following services:

Assurance services	*2012* $	*2011* $
Audit services		
Fees paid to PricewaterhouseCoopers Australian firm:		
- Audit and review of financial report	133,000	133,000
- Audit of regulatory return	5,000	5,000
Total remuneration for audit services	**138,000**	**138,000**
Taxation services		
Fees paid to PricewaterhouseCoopers New Zealand firm for Tax compliance and advisory services	79,000	47,690
Total remuneration for taxation services	**79,000**	**47,690**

It is the Company's policy to employ PricewaterhouseCoopers on assignments additional to their statutory audit duties where PricewaterhouseCoopers expertise and experience with the Company are important and these assignments are obtained on a competitive basis. These assignments are principally tax advice and other advisory services.

31. RELATED PARTIES

(a) Controlling Entities

ACE Insurance Limited is a wholly owned subsidiary of ACE INA International Holdings, Ltd, registered in Delaware, United States of America. The ultimate holding company is ACE Limited, whose principal office is located in Zurich, Switzerland.

(b) Directors and key executives

The following persons were directors of ACE Insurance Limited during the financial year: Kenneth Brown (Executive Chairman), Jarrod Hill, Alexander Houvardas, Paul Martin and Giles Ward (executive directors), Graeme Evans and David Kennedy (non-executive directors).

On 1 May 2012, Graeme Evans was appointed Chairman and non-executive director, along with David Kennedy who was appointed as a non-executive director. Kenneth Brown, Alexander Houvardas and Jarrod Hill resigned as directors on the same day.

(c) Key management compensation

Key management personnel include the directors and six key roles performed by key executives during the year (2011: six key roles) with the influence and authority to execute the strategic direction of the Company during the financial year. Total compensation for key management personnel is set out as follows:

	2012 $	*2011* $
Short term employee benefits	1,028,581	931,742
Post employment benefits	85,664	58,206
Other long term benefits	4,904	4,239
Termination benefits	-	-
Share based payments	149,147	171,293
Total	**1,268,296**	**1,165,480**

31. RELATED PARTIES (continued)

(d) Transactions and balances

The Company has transactions in the normal course of business with fellow subsidiaries. These comprise of insurance and reinsurance transactions (based on written premiums and incurred claims), and management and support services. The significant transactions are as follows:

	2012	*2011*
	$	$
Expenses with commonly controlled entities:		
Reinsurance premiums	69,070,969	55,086,548
Management and systems support	5,887,534	4,086,308
Commissions paid	140,555	147,924
Losses paid	336,391	66,068
Revenue with commonly controlled entities:		
Reinsurance and other recoveries revenue	72,247,379	242,148,717
Commissions received	18,197,216	14,947,689
Premiums assumed	1,136,007	1,020,072
Dividend paid to Parent entity	7,000,000	-

(e) Outstanding balances

The following balances are outstanding at the reporting date in relation to transactions with related parties:

	2012	*2011*
	$	*$*
Receivables:		
Commonly controlled entities with the Ultimate Parent	159,630,124	221,812,515
Payables:		
Commonly controlled entities with the Ultimate Parent	3,917,751	5,219,868

No impairment has been recognised in relation to any outstanding balances, and no impairment has been recognised in respect of debts due from related parties.

(f) Terms and conditions

All transactions were made on normal commercial terms and conditions and at market rates. Services are usually negotiated with related parties on a cost-plus basis, allowing a reasonable profit margin. Outstanding balances are unsecured and are repayable in cash.

32. RECONCILIATION OF PROFIT AFTER INCOME TAX TO NET CASH INFLOWS FROM OPERATING ACTIVITIES

	2012 *$000*	*2011* *$000*
Profit for the year	8,922	12,986
Adjusted for:		
Depreciation and amortisation	366	587
Fair value change on financial assets	1,726	(455)
Change in operating assets and liabilities:		
Increase/(Decrease) in unearned premium reserve	4,174	9,092
Increase/(Decrease) in unexpired risk liability	-	(547)
Increase/(Decrease) in outstanding claims	(69,828)	193,970
Increase/(Decrease) in trade and other creditors	97	3,277
Increase/(Decrease) in employee entitlements	(65)	247
Increase/(Decrease) in deferred tax liabilities	195	270
Increase/(Decrease) in tax liabilities	(4,241)	4,241
Decrease/(Increase) in deferred insurance costs	139	(4,859)
Decrease/(Increase) in other receivables	1,697	(5,346)
Decrease/(Increase) in policyholder debtors	(6,687)	(5,731)
Decrease/(Increase) in reinsurance and other recoveries	69,605	(197,668)
Decrease/(Increase) in deferred tax assets	(44)	64
Decrease/(Increase) in tax receivable	(769)	301
Decrease/(Increase) in other assets	6	(6)
Net cash inflows from operating activities	**5,293**	**10,423**

33. EVENTS OCCURRING AFTER REPORTING DATE

The directors are not aware of any matter or circumstance not otherwise dealt with in this report that has significantly or may significantly affect the operations of the Company, the results of those operations or the state of affairs of the Company in subsequent financial years.

34. CREDIT RATING

On 17 July 2012, the Company's financial strength rating of 'A/Stable' was reaffirmed by rating agency Standard and Poor's in accordance with the Insurance Companies Rating and Inspections Act 1994.

35. CHARGE

Under the Trust Deed, which governs the operation and management of the accident insurance business, the Public Trustee maintains a floating first charge over the assets of the Company.

36. SHARE BASED PAYMENT TRANSACTIONS

ACE Limited has a restricted share grant plan, a restricted share option plan and an employee share purchase plan.

Restricted Share Grant Plan
Under ACE Limited's long term incentive plan, 2,039 restricted ordinary shares were awarded during the year ended 31 December 2012 (2011: 3,021) and 1,166 (2011: nil) restricted ordinary shares were transferred to other ACE entities due to employee transfers during the year ended 31 December 2012. These shares vest at various dates over a 4 year period from the grant dates and any unvested shares are cancelled on termination of the employment of the eligible employees. This plan is a group scheme with expenses incurred under the scheme charged out by ACE Limited to the Company on an annual basis. The annual expense is based on an amortised calculation that is reflective of the current year's expense portion of all restricted share grants issued in the current and prior years, and is consistent with the treatment required by NZ IFRS. There is no liability to the Company for the unamortised portion of the restrictive stock grants issued. The amortised calculation incorporates the fair market value of ACE Limited's common stock in determining the expense amount. Expected future dividend payments in relation to the restrictive stock grants issued are made directly by ACE Limited to the eligible employees. The total expense for the year was NZD $171,860 (2011: NZD $300,221).

Restricted Share Option Plan
Under ACE Limited's long term incentive plan, restrictive share options were granted to eligible employees of the Company. The exercisable price of these options is the fair market value at issue date. These options vest at various dates over a 3 year period from the grant date and any unvested options are cancelled on termination of employment. This plan is a group scheme with expenses incurred under the scheme charged out by ACE Limited to the Company on an annual basis. Any option not exercised or cancelled pursuant to the terms of plan will be forfeited by the tenth anniversary from the date of grant. The total value of the options granted during the year was NZD $33,898 (2011: NZD $62,629).

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

	2012		2011	
	Average exercise price in NZD per share	Options	Average exercise price in NZD per share	Options
At 1 January		10,343		10,689
Granted	89.76	1,700	83.86	2,514
Forfeited	-	-	-	-
Exercised	53.88	(1,658)	65.58	(2,860)
Transferred out		(1,504)		-
At 31 December		8,881		10,343

36. SHARE BASED PAYMENT TRANSACTIONS (continued)

Out of the 8,881 outstanding options (2011: 10,343 options), 4,658 options (2011: 4,210) were exercisable. Options exercised in 2012 resulted in 1,658 shares (2011: 2,860) being issued at 53.88 NZD (2011: 65.58). The weighted average remaining life of the share options outstanding at the end of the period is 6 years (2011: 7 years).

Share options outstanding at the end of the year have the following expiry date and exercise prices:

Expiry Year	Exercise price NZD per share	Share options 2012	Share options 2011
2012	53.72	-	450
2013	33.74	600	700
2014	53.31	510	510
2015	54.43	180	180
2016	69.02	-	-
2017	68.70	290	290
2018	73.77	465	465
2019	47.13	1,115	2,324
2020	61.64	2,260	2,910
2021	76.66	1,762	2,514
2022	89.76	1,700	-
		8,881	10,343

The weighted average fair value of options granted during the period determined using the Black-Scholes valuation model was 18.82 NZD per option (2011: 18.98 NZD). The significant inputs into the model were share price of 89.76 NZD (2011: 83.86 NZD), at the grant date, the exercise price shown above, volatility of 30.00% (2011: 29.00%), dividend yield of 2.67% (2011: 2.23%), and an expected option life of 5 years and on annual risk-free interest rate of 1.01% (2011: 2.17%). The volatility measured at the standard deviation of continuously compounded share returns is based on statistical analysis of daily share prices over the last three years.

Employee Share Purchase Plan

The Company collects monies from local eligible employees and acquires ordinary shares in ACE Limited on behalf of the employees on a bi-annual basis. The price paid by the eligible employees is set at a discount of 15% to the fair value of the ordinary shares at the date of acquisition; this discount is incurred at the group level by ACE Limited and not charged to the Company. The total amount of discount applied to the employee share plan purchases in the current year was NZD $0 (2011: NZD $0).

CU1-3, Shed 24
Princes Wharf
Auckland 1010

PO Box 734
Shortland Street
Auckland 1140

(649) 377 1459 *tel*
(649) 303 1909 *fax*
www.aceinsurance.co.nz

ace insurance

Company No. 104656
FSP No. 35924

To: Mr Paul Martin, Country President, ACE Insurance Limited

From: Stephen Wilson, Appointed Actuary for ACE Insurance Limited

Cc: Mr G Evans, Mr D Kennedy, Mr G Ward, Mr A Hourvardas, Ms F Eagles, Mr R Roy, Mr J Downes

Date: 24 May 2013

Re: Section 78 Appointed Actuary's Report - ACE Insurance Limited

1. Introduction and scope

In accordance with section 78 of the *Insurance (Prudential Supervision) Act 2010* (**IPSA**), as the appointed actuary for ACE Insurance Limited (**AIL**), this report documents my review under section 77 of IPSA.

In particular:

- Section 77 (1) of IPSA specifies that "A licensed insurer must ensure that the actuarial information contained in, or used in the preparation of, the financial statements of the insurer and any group financial statements referred to in section 81(1) (*of IPSA*) is reviewed by the appointed actuary."
- Section 77 (3) specifies that the "review must be carried out in accordance with an applicable solvency standard."
- Section 77 (4) specifies that "For the purposes of this section and section 78, actuarial information means—

  (a) information relating to an insurer's calculations of premiums, claims, reserves, dividends, insurance and annuity rates, and technical provisions;

  (b) information relating to assessments of the probability of uncertain future events occurring and the financial implications for the insurer if those events do occur;

  (c) information specified in an applicable solvency standard as being actuarial information for the purposes of this section."

With respect to section 77 (4)(c) of IPSA, section 130 of the Reserve Bank of New Zealand's (RBNZ) Solvency Standard for Non-Life Business, specifies the actuarial information as:

a) the Premium Liabilities as defined in this solvency standard;
b) the Net Outstanding Claims Liability as defined in this solvency standard;
c) the reinsurance and any other recovery asset(s) relevant to the Reinsurance Recovery Risk Capital Charge;
d) any deferred acquisition cost or deferred fee revenue relevant to the Premium Liabilities; and
e) any other information deemed by the appointed actuary to warrant actuarial review.

With respect to section 77 (4)(c) of IPSA, section 144 of the RBNZ's Solvency Standard for Life Business, specifies the actuarial information as:

a) the Policy Liability;
b) the reinsurance and any other recovery asset(s) relevant to the Policy Liability, or relevant to outstanding claims reserves or incurred but not reported claims reserves held outside of the Policy Liability;
c) any deferred or other tax asset relevant to the Policy Liability;
d) any deferred acquisition cost or deferred fee revenue relevant to the Policy Liability;
e) the unvested policyholder benefits liability; and
f) any other information deemed by the appointed actuary to warrant actuarial review for the purpose of profit or solvency reporting.

Each of these items are addressed and documented in detail (to the extent relevant and material) in AIL's Insurance Liability Valuation Report dated 29 April 2013.

Additional analysis has been performed in the preparation of my Financial Condition Report which will be finalized prior to the AIL Board meeting on 20 June 2013.

2. Information required

a) Name: Stephen James Wilson

b) Work done by the actuary:

I confirm that I have reviewed the following in respect of AIL's financial statements:

- Information relating to an insurer's calculations:

  - **Premiums**

    - Discussions and review of written, earned and unearned premium data with AIL Finance and PwC Auditors

  - In addition, as part of my Insurance Liability Valuation (ILV) I have calculated an amount of unclosed written, earned and unearned premium, gross and net of reinsurance

- **Claims** – As part of my Insurance Liability Valuation Report (ILVR) dated 29 April 2013, I have:

  - Reconciled the actuarial claims data with Finance claims data
  - Analysed AIL's claims data using actuarial techniques

- **Reserves** – As part of my ILVR I have:

  - Reconciled the actuarial claim reserve data with Finance claim reserve data
  - Analysed the strength of AIL's claims reserves using actuarial techniques
  - Had detailed discussions regarding large claim reserve with underwriting and claims departments
  - Determined Insurance Liability Reserves (including both Outstanding Claim Liabilities and Premium Liabilities) in accordance with the Reserve Bank of New Zealand's (RBNZ) Solvency Standards for Non-Life Business and Life Business

- **Dividends** – Reviewed the 2012 and proposed future level of dividends in the context of AIL's current and forecast financial condition as part of my analysis for AIL's Financial Condition Report (FCR), which will be delivered in June 2013

- **Insurance** (and annuity) **rates** – Reviewed the adequacy and profitability of AIL's premium rates as part of my analysis for AIL's FCR

- **Technical provisions** – Determined and documented as part of my ILVR

- Information relating to assessments of the probability of uncertain future events occurring and the financial implications for the insurer if those events do occur

  - An assessment of the probability of uncertain future events has been performed and documented as part of my ILVR

- Information specified in an applicable solvency standard as being actuarial information for the purposes of this section.

  - I have reviewed the information (both actuarial and non-actuarial) required under both the RBNZ's Solvency Standard for Non-Life Business and RBNZ's Solvency Standard for Life Business.

- I confirm that my review covered:

  - Net outstanding claims as per NZ IFRS 4 including:
    - central estimate of expected claims and recoveries;
    - discounting at a risk free rate;
    - allowance for claim handling expenses; and
    - a risk margin intended to provide the specified probability of sufficiency;

  - The relevant accounting provisions (unearned premium, deferred acquisition cost, deferred reinsurance expense, deferred reinsurance commissions, and unexpired risk);

  - The actuarial estimate of net premium liabilities comprising:

    - determination of the appropriate assessment period for Premium Liabilities;
    - central estimate of expected claims and recoveries;
    - discounting at a risk free rate;
    - allowance for policy administration and claim handling expenses;
    - allowance for the cost of any future **reinsurance** (i.e. that has not yet been purchased) required to cover unexpired risks; and
    - a risk margin intended to provide a 75% POS.

  - Application of the Liability Adequacy Test

  - The level of deferred acquisition cost in the financial statements after the application of the Liability Adequacy Test.

c) Scope and limitations of the review

The scope of my review has been to review the information referred to as "actuarial information" in Section 77 (4) of IPSA, and detailed above, namely:

- information relating to an insurer's calculations of premiums, claims, reserves, dividends, insurance and annuity rates, and technical provisions;
- information relating to assessments of the probability of uncertain future events occurring and the financial implications for the insurer if those events do occur;
- information specified in an applicable solvency standard as being actuarial information for the purposes of this section; and
- legal advice provided in conjunction with the compilation of the solvency return.

There have been no limitations placed on my review.

ace insurance

d) The existence of any relationship (other than that of actuary) that the actuary has with, or any interests that the actuary has in, the licensed insurer or any of its subsidiaries

I confirm that I am an employee of a related corporate entity, ACE Insurance Limited (Australia) – which is not a subsidiary of AIL - and I am not a Director of AIL.

e) Whether the actuary has obtained all information and explanations that he or she has required

I confirm that I have obtained all information and explanations required to perform my review.

f) Whether, in the actuary's opinion and from an actuarial perspective:

i) the actuarial information contained in the financial statements and any group financial statements has been appropriately included in those statements (and if not, the respects in which it has been inappropriately included)

ii) the actuarial information used in the preparation of the financial statements and any group financial statements has been used appropriately (and if not, the respects in which it has been used inappropriately).

I confirm that in my opinion, and from an actuarial perspective, the actuarial information contained in AIL's financial statements has been appropriately included and has been used appropriately.

g) Whether, in the actuary's opinion and from an actuarial perspective, the licensed insurer is maintaining the solvency margin that applies under a condition imposed under section 21(2)(b) (as at the balance date of the insurer)

I confirm that in my opinion, and from an actuarial perspective, AIL has maintained the solvency margin in accordance with both the RBNZ's Solvency Standard for Non-Life Business and RBNZ's Solvency Standard for Life Business.

I am mindful of the RBNZ's Solvency Standard for Non-Life Business and the requirement for a 100% capital charge when assets are subject to a fixed or floating charge. I have reviewed and relied upon the legal advice provided by Bell Gully dated 24 May 2013. My interpretation of that advice is that the value of assets charged is currently estimated to be $32,000. I am comfortable that the potential exposure in respect of those claims is unlikely to develop materially from that estimate. Hence the charge that could be secured over AIL's assets is unlikely to ever be materially higher than $32,000.

ace insurance

h) in the case of a life insurer, whether, in the actuary's opinion and from an actuarial perspective, the life insurer is maintaining the solvency margins that apply in respect of its statutory funds under a condition imposed under section 21(2)(c) (as at the balance date of the insurer).

Not applicable as AIL is a non-life insurer and, despite having a small amount of life insurance business (in run-off), AIL has been given an exemption from holding statutory funds in respect of this life insurance business.

Please do not hesitate to contact me if you would like to discuss any aspect of this memorandum.

Stephen Wilson
Appointed Actuary, ACE Insurance Limited

Email: stephenj.wilson@acegroup.com
DDI: +61 2 9335 3213

Enc. Valuation of Insurance Liabilities - 31 December 2012 - ACE Insurance Limited (New Zealand)

Valuation of Insurance Liabilities
31 December 2012

ACE Insurance Limited (New Zealand)

29 April 2013

29 April 2013

Mr Paul Martin
Country President
ACE Insurance Limited (New Zealand)
Shed 24, Princes Wharf
AUCKLAND 1010

Dear Paul

ACE Insurance Limited (New Zealand) – Valuation of Insurance Liabilities as at 31 December 2012

I have pleasure in enclosing a copy of our report "ACE Insurance Limited (New Zealand) – Valuation of Insurance Liabilities as at 31 December 2012".

Should you have any questions or require any further information please do not hesitate to contact me.

Yours sincerely

Stephen Wilson
Appointed Actuary
Fellow of the Institute of Actuaries of Australia

Valuation of Insurance Liabilities 31 December 2012

Part I Executive Summary

1 Executive Summary

ACE Insurance Limited (New Zealand) (AIL NZ) has appointed Stephen Wilson, Chief Actuary Australia & New Zealand, as Appointed Actuary of AIL NZ. The purpose of this report is to assist AIL NZ in establishing insurance liability provisions for balance sheet purposes and reporting on the total insurance liabilities to RBNZ for solvency purposes.

This is the first valuation report prepared by Stephen Wilson in his role as AIL NZ's Appointed Actuary.

This executive summary presents the major results from the valuation. Judgements regarding the data, methods and assumptions contained in the report should be made only after studying the entire report, as conclusions reached by a review of a section or sections on an isolated basis may be incorrect.

2 Summary of Results

My estimate of the discounted general insurance liabilities are summarised in Table 1 below. The results include a risk margin sufficient to secure the outstanding claims liability to a 75% probability of sufficiency.

Table 1 – Estimated Insurance Liabilities as at 31 December 2012

	Outstanding Claims $'000	Premium Liabilities $'000	Total $'000
Estimate of Gross Claims Liability	175,832	27,811	203,643
Plus Future Claims Expenses	2,500	14,197	16,696
Central Estimate of Gross Liability	**178,332**	**42,008**	**220,340**
Less Recoveries	155,901	17,194	173,096
Central Estimate of Net Liabilities	**22,430**	**24,814**	**47,244**
Plus Risk Margin on Net Liability	2,942	3,170	6,112
Net Insurance Liabilities	**25,372**	**27,984**	**53,356**

The total estimated net insurance liabilities as at 31 December 2012 are $53.4 million. The above table excludes life insurance policy liabilities (refer Section 6).

A review of risk margins was undertaken for the previous review. The risk margins determined in that review have been determined to be appropriate for this valuation.

The gross outstanding claims liabilities include $110 million for the 2010 and 2011 Canterbury earthquakes claims. Gross IBNR of $17.25m has been adopted for 2010 in relation to development on the Universities of NZ claims, in particular in relation to Lincoln University. These amounts were reserved in January. The net liability for the earthquake claims is $0 (excluding CHE).

In my judgement, I have employed techniques and assumptions that are appropriate, and the conclusions presented herein are reasonable, given the information currently available. However, it should be recognised that future loss emergence will likely deviate, perhaps materially, from our estimates.

3 Adequacy of Previous Valuation

With the benefit of hindsight, we now estimate that the undiscounted net central estimate of outstanding claims liabilities from the previous valuation of $19.3 million was overstated by $0.6 million. Releases from Casualty, Financial Lines and Accident and Health were partially offset by strengthening in the Fire portfolio.

There was negligible change in the discounted liabilities due to little change to discount rates during 2012.

4 2012 Claims Experience

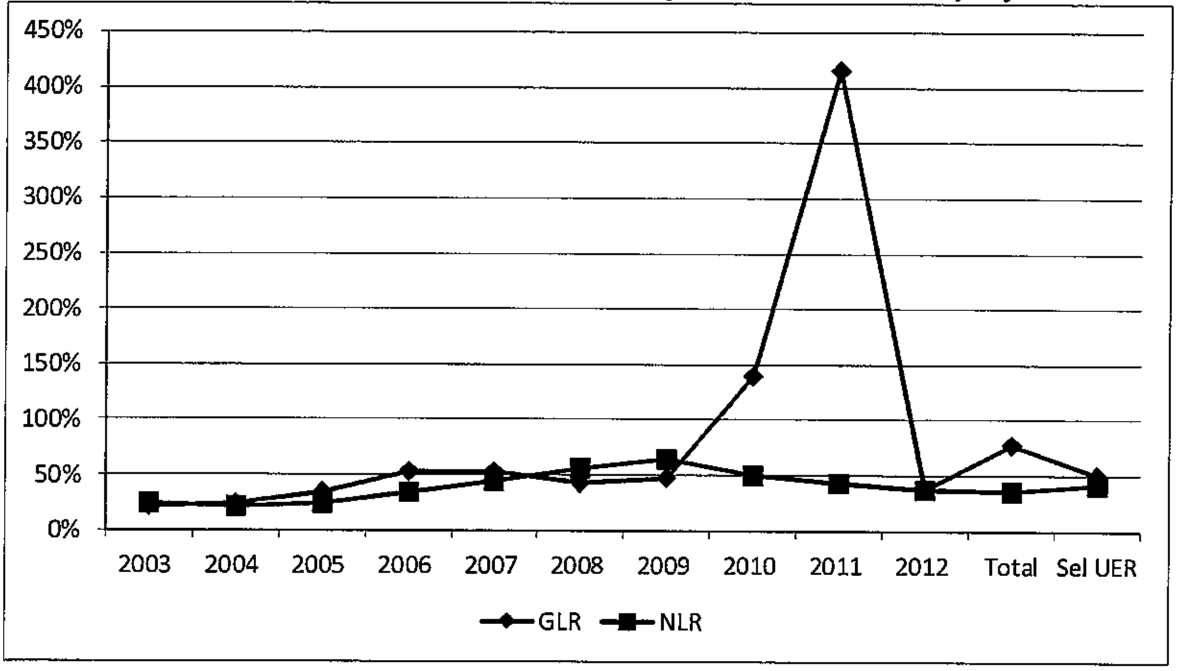
The key features of the 2012 experience from a claims viewpoint were:

- Releases from Casualty and Financial Lines experience ($1.3 million) and Accident and Health ($0.9 million) offset by strengthening of Fire reserves ($1.6 million) on a central estimate basis.
- Reported gross claims costs associated with the 2011 Canterbury Earthquakes developed by $33 million during 2012. The net development was nil due to the low catastrophe retention and the net cost outstanding is nil.
- The performance of the Combined Portfolio was stable (and very good).

5 Loss Ratio Analysis

Figure 2.1 shows AIL NZ's projected company total loss ratios, including IBNR allowance, by accident year for the past 10 years.

Figure 2.1 – Projected Ultimate Loss Ratios by Accident Year – Company Total



The impact of the Earthquake claims on the gross loss ratio for the recent accident years is evident.

We are projecting the 2012 accident year will be slightly better than 2011. This primarily reflects improvement in the A&H Broker and Fire portfolios. The latter benefitted from the hardening rate levels.

6 Life Insurance Policy Liabilities

The life insurance policy liabilities in respect of the Combined Life run-off business are $1.3 million gross and $0.4 million net of quota share reinsurance.

The life insurance policy liabilities are determined by Marianne Clifford, an Actuary with Combined Insurance Company of America, part of the ACE Group.

Results of the valuation of the life insurance policy liabilities are shown in Appendix G. Due to the immaterial size of these liabilities, I have not discussed these further in this report.

Part II Detailed Findings

1.1 Introduction

ACE Insurance Limited (New Zealand) (AIL NZ) has appointed Stephen Wilson, Chief Actuary Australia & New Zealand, as Appointed Actuary of AIL NZ. The purpose of this report is to assist AIL NZ in establishing insurance liability provisions for balance sheet purposes and reporting on the total insurance liabilities to RBNZ for solvency purposes.

This is the first valuation report prepared by Stephen Wilson in his role as AIL NZ's Appointed Actuary.

The previous valuation at 31 December 2011 was prepared by Tim Andrews of Finity Consulting Pty Limited (Finity) in his role as AIL NZ's Appointed Actuary. Tim Andrews became the Appointed Actuary during 2011 and continued in this role until August 2012 when Stephen Wilson was appointed. I had the opportunity to discuss the previous valuation with them in the course of our review.

The prior annual Actuarial Valuation, carried out effective 31 December 2010, was prepared by Andrew Bendall and Robert Cameron as documented in their report dated 25 March 2011.

The purpose of this report is to provide written advice on the valuation of insurance liabilities and includes the following items:

- A central estimate of the outstanding claims liabilities. This is an estimate that has no deliberate bias (upwards or downwards) and thus represents our best estimate.
- A central estimate of the premium liabilities, and
- A risk margin that relates to the inherent uncertainty in the central estimate and, when added to the central estimate, is intended to increase the probability of sufficiency of the insurance liabilities from approximately 50% to 75%.

1.2 Reliance on ResQ

The main valuation calculations were undertaken in ResQ, which is reserving software licensed by ACE on a global basis.

1.3 Compliance with Relevant Standards

IFRS4

This valuation is intended to meet the requirements of NZ Accounting Standard IFRS4. IFRS4 governs the preparation of general purpose accounts for general insurers in New Zealand.

Reserve Bank of New Zealand Solvency Standard for Non-life Insurance Business

The Reserve Bank of New Zealand's (RBNZ) Solvency Standard for Non-life Insurance Business (solvency standard) sets out the requirements of a licensed insurer's appointed actuary in respect of the review of "actuarial information" for the purpose of the solvency standard. The specified information, as required by Section 77 of the Insurance (Prudential Supervision) Act 2010, for the purpose of the solvency standard is:

- The Premium Liabilities as defined in the solvency standard
- The Net Outstanding Claims Liability as defined in the solvency standard
- The reinsurance and any other recovery asset(s) relevant to the Reinsurance Recovery Risk Capital Charge (as defined in the solvency standard)
- Any deferred acquisition cost or deferred fee revenue relevant to the Premium Liabilities; and
- Any other information deemed by the appointed actuary to warrant actuarial review for the purpose of profit or solvency reporting.

As mentioned in section 1.1 this report provides advice on:

- The central estimate of Net Outstanding Claims Liabilities
- The central estimate of Premium Liabilities, and
- Risk margins to provide a 75% probability of sufficiency on insurance liabilities.

New Zealand Society of Actuaries Professional Standards

This report has been prepared in accordance with the following New Zealand Society of Actuaries actuarial standards:

(i) PS04 – The preparation of actuarial reports on technical liabilities of general insurers

(ii) PS09 – Communication of Professional Advice, and

(iii) the New Zealand Society of Actuaries Code of Professional Conduct.

This report includes the results of the valuation of the run-off life insurance policy liabilities. These results are considered relatively immaterial in the context of the general insurance business of AIL.

1.4 Control Process and Review

PS04 requires the documentation of control processes undertaken in the valuation. The key control processes are incorporated in this report and include:

- Data reconciliations (Section 2.1)
- Analysis of Loss Ratios (Section 3 and Appendix C)
- Inclusion of a Risk Margin (Section 5)
- Reconciliation with Previous Estimates (Section 7)
- Sensitivity Analysis (Section 8)

An audit review of this valuation has also been carried out by PricewaterhouseCoopers. This provides a further control process where, in additional to the controls above, the audit review examines the valuation methodology undertaken and assumptions selected for the Outstanding Claims Liability (Section 3) and the Premium Liability (Section 4).

2 Data

The previous valuation report described the data used for the valuation. The data is taken from PCW, ACE's Global Data Warehouse. The previous report included reconciliation of the data to 2011, which was adequate. The 2012 reconciliation was also adequate as described below.

The data was categorised into 24 classes of business for this analysis compared to 23 in the previous valuation. This was due to split of the A&H Travel Individual into A&H Travel Integrated and A&H Travel Traditional.

PCW contains the following data used for the valuation of liabilities:

- Claim header file
- Policy header file
- Claim transaction file
- Premium transaction file.

In addition to the PCW files, the following data was used for this valuation:

- General Ledger reports provided by Finance Department for:
  - 2012 financial year claim transactions
  - 2012 financial year premium transactions
- Unearned Premium at 31 December 2012
- Details of operating expenses by major function for the past five financial years
- Details of AIL NZ's reinsurance programme (current and historical)
- NZ risk-free investment yields as at 31 December 2012 (obtained from the Reserve Bank), which were used to discount the projected outstanding claims liability cash flows to present value.

2.1 Reconciliation of 2012

For the 2012 transaction year, claims paid, movement in case estimates and written premium from ResQ were reconciled to the Peoplesoft Ledger. Earned premium data is also used in the valuation of outstanding claims liabilities.

As shown in Table 2.1 below, the reconciliation shows that there are small differences on case estimates and written premiums, but these are not material in the context of the overall liabilities.

Table 2.1 – Data Reconciliation for 2012 Transaction Year

Item	ResQ Data ($'000s)	Ledger ($'000s)	Difference ($'000s)
Gross Claims Payments	161,146	161,240	94
Net Claims Payments	26,361	26,361	0
Gross Case Estimate Movement	-65,660	-65,343	318
Net Case Estimate Movement	-3,111	-2,819	292
Gross Written Premium	129,339	129,338	-1
Net Written Premium	49,500	49,500	0

The reconciliation shows that payments reconcile exactly and there is only a small difference in Gross and Net case estimate movement.

Gross and net earned premium data is also used in the valuation of outstanding claims liabilities. The earned premium is calculated on an exposure year basis and therefore cannot be directly reconciled to the financial accounts, however consistency checks have been undertaken to ensure the reasonableness of the data.

3 Outstanding Claims Liability

3.1 General Approach

The general approach to actuarial estimation of outstanding claims is to analyse all available past experience with respect to numbers of claims, claim payments and changes in case estimates. This allows patterns to be detected in the past experience from which the future run-off of outstanding claims can be estimated.

The claim reporting pattern, claim payment pattern and the progression of case estimates exhibited by a particular portfolio depend upon many factors, including:

- Claim management procedures;
- Case estimation procedures;
- Reinsurance arrangements;
- Type of event giving rise to the claim (e.g. storm, fire etc); and
- External factors such as the judicial system and general economic conditions.

The methods used to analyse past claims experience and to project future claims experience are largely determined by the available data and the nature of the portfolio.

As AIL NZ has relatively low per risk retentions, it is generally necessary to analyse the past data on both gross and net of reinsurance bases.

The estimation of the outstanding claims provision involves two steps:

(i) The determination of a central estimate of the outstanding claims liability at the balance date. The central estimate represents the actuary's best estimate of the present value of expected future net claims cost, including allowance for claims incurred but not reported ("IBNR") and an allowance for claims handling expenses. Technically, the central estimate represents the theoretical mean of the distribution of possible outstanding claims outcomes.

(ii) The determination of a risk margin to be added to the central estimate to increase the probability of adequacy of the provision from approximately 50% (i.e. the central estimate) to the company's desired level, 75%.

The remainder of this section documents the determination of the central estimate. The assessment of risk margins is discussed in Section 4.

3.2 Business Segments and Reinsurance Structure

AIL NZ's business is divided into 4 major portfolios as follows:

- Accident & Health (A&H) – a portfolio of personal accident and travel business distributed to corporate customers through Insurance Brokers or consumers via selected sponsors such as American Express. These portfolios are protected by excess of loss reinsurance with a 70% quota share reinsurance applying below the excess of loss. Note that the Amex business has additional external quota share.
- Property & Casualty (P&C) – a portfolio of predominantly short tail property and long tail casualty & financial lines business for corporate customers distributed through Brokers. These portfolios are generally protected by excess of loss reinsurance with a net retention of US$250,000. The net retention is low relative to the size of the business insured and provides considerable protection against large losses.
- Commercial Lines – a portfolio of predominantly property business for small to medium size enterprises (SME) distributed through Brokers. During 2011 parts of this portfolio was placed into run-off and the remaining parts were transferred to the Fire class.
- Personal Other – this portfolio consists solely of a contract with Vodafone, providing mobile phone insurance for Vodafone customers. This is reinsured 100% back to a captive insurance company of Vodafone.
- Combined – a portfolio of personal accident and health products distributed through a network of sales agents. This portfolio is protected by excess of loss reinsurance with a 70% quota share reinsurance applying below the excess of loss (the quota share has increased from 50% in the previous valuations).

Table 4.1 summarises gross and net written premium by class of business

Table 3.1 – Written Premium by Business Segment

Class of Business	2012 GWP $'000s	2012 GWP % of Total	2012 NWP $'000s	2012 NWP % of Total
A&H DM - AMEX NAC	2,117	2%	513	1%
A&H DM - AMEX Other	2,211	2%	468	1%
A&H DM - Other	765	1%	248	1%
A&H GPA & Other	7,500	6%	2,154	4%
A&H Travel Group	7,000	5%	1,815	4%
A&H Travel - Integrated	836	1%	258	1%
A&H Travel - Traditional	12	0%	3	0%
A&H Travel - Partner Other	113	0%	66	0%
A&H Travel - Partner AMEX	0	0%	0	0%
A&H Total	**20,553**	**16%**	**5,525**	**11%**
B&M	2,200	2%	1,101	2%
CAR EAR	2,891	2%	1,075	2%
Commercial Auto	355	0%	0	0%
Fire & SME	54,736	42%	23,434	48%
Marine Cargo & Hull	130	0%	38	0%
Oil & Petro Offshore	0	0%	0	0%
Oil & Petro Onshore	0	0%	0	0%
D&O	2,287	2%	1,063	2%
Financial Instit	654	1%	278	1%
GL Excess	1,136	1%	1,123	2%
GL Primary	8,941	7%	5,160	10%
Professional Indemnity	1,350	1%	756	2%
WC EL	85	0%	79	0%
P&C Total (incl. SME)	**74,766**	**57%**	**34,109**	**69%**
Personal Other	2,700	2%	0	0%
Commercial Lines Total (excl. SME)	**2,700**	**2%**	**0**	**0%**
Combined	**32,085**	**25%**	**9,626**	**20%**
Total	**130,104**	**100%**	**49,259**	**100%**

3.3 Valuation Methods Used

The valuation methods used in this investigation are:

- Incurred Claim Development ("ICD")
- Paid Claim Development ("PCD")
- Bornhuetter-Ferguson Method ("BF")
- Bornhuetter-Ferguson Method on Paid Claims ("PBF")
- Loss Ratio ("LR")
- Formula Method.

All methods have been applied to yearly cohorts of claims data arranged in the common accident year/development quarter format. Separate models were derived for gross and net liability estimates.

The methods implicitly allow for inflation, both "normal" and "superimposed".

Selection of Appropriate Methods

The selection of the method or methods (as some years are based on a blend of models) to adopt for each accident year for each class depends on:

- The maturity of the accident year: for most classes the transition is from the Loss Ratio method for the latest year or years to the BF method for the intermediate years to the ICD method for the most developed years. In effect this reflects a transition from exposure based reserves for the latest accident periods, where not much is known about the actual claims experience, to claims experience based reserves for the older periods where most of the claim development tends to reflects case estimate development of existing claims.
- The rate of transition between methods depends on the loss development multiplier for a particular year. If the loss development multiplier is high (i.e. the claims costs are expected to develop significantly) then the transition between methods is slower. Hence long tailed classes can sometimes be based on the Loss Ratio method for two years whereas short-tail classes will generally be based on the BF method at the end of the first development year.
- The rate of transition between the BF and ICD methods also depends on how closely the emerging costs are matching the initial expected selected loss ratio. If the costs are departing significantly from the expected loss ratio, then the transition to ICD is slower. In periods when claims costs are emerging at lower than expected levels (as has tended to be the case for the AIL NZ portfolios) this has the effect of increasing the IBNR.
- The formula method selects on of the ICD, BF or LR methods or a blend of these methods base on an explicit set of criteria.
- The methods selected are broadly consistent with the prior valuation for each class.

3.4 Short Tail Classes

By their nature, the liabilities in respect of short tail classes of business are generally well represented by the individual case by case estimates in respect of reported claims. The allowance for IBNR claims and IBNER (incurred but not enough reported) development is generally very small, and for some classes in some older accident years can even be negative.

The assumed initial loss ratios used for the BF method are consistent with the annual Business Plan for each portfolio.

For Combined business we have adopted the PCD method for accident years prior to 2011 and the PBF method for the 2011 and 2012 accident years.

Appendices E and F contain details of the claims triangulations and chain ladder development ratio selections. In general, only minor changes have been made to the model selections from the previous valuation.

Table 3.2 below summarises the gross and net central estimates (discounted, including indirect claims handling expenses). We have also shown the resulting undiscounted net IBNR estimates (excluding indirect claims handling expenses). Details of the estimates by accident year are contained in Appendix E.

Table 3.2 – Short Tail Liabilities

Class of Business	Gross Central Estimate 31.12.2012 $'000	Net Central Estimate 31.12.2012 $'000	Net Central Estimate 31.12.2011 $'000	Net IBNR 31.12.2012 $'000	Net IBNR 31.12.2011 $'000
A&H DM - AMEX NAC	*229*	*155*	*120*	*116*	*428*
A&H DM - AMEX Other	*157*	*39*	*81*	*26*	*47*
A&H DM - Other	*74*	*22*	*19*	*16*	*16*
A&H GPA & Other	*2,076*	*673*	*691*	*187*	*111*
A&H Travel Group	*2,366*	*1,079*	*1,114*	*406*	*382*
A&H Travel - Integrated + Traditional	*127*	*45*	*90*	*25*	*47*
A&H Travel - Partner Other	*4*	*2*	*3*	*2*	*2*
A&H Travel - Partner AMEX	*0*	*0*	*1*	*0*	*0*
A&H Total	***5,031***	***2,016***	***2,120***	***777***	***1,034***
B&M	*346*	*77*	145	60	*26*
CAR EAR	*2,119*	*976*	*662*	*247*	*23*
Commercial Auto	*17*	*1*	*1*	*0*	*0*
Fire & SME	*141,156*	*6,747*	*4,663*	*3,956*	*631*
Marine Cargo & Hull	*65*	*14*	*45*	*9*	*0*
Oil & Petro Offshore	*0*	*0*	*0*	*0*	*0*
Oil & Petro Onshore	*0*	*0*	*0*	*0*	*0*
P&C Short Tail Total	***143,704***	***7,816***	***5,516***	***4,272***	***679***
Personal Other	*982*	*0*	*25*	*0*	*0*
Commercial Lines Total (excl. SME)	***982***	***0***	***25***	***0***	***0***
Combined	***4,876***	***1,610***	***2,649***	***1,610***	***2,649***
Short Tail Total	**154,594**	**11,441**	**10,309**	**6,659**	**4,362**

Notes: A&H Travel Integrated and Traditional shown together for comparison pursposes
2011 Combined net estimates are based on 50% QS; 2012 on 70% QS

These results show that there has been an increase of $2.3 million in the IBNR provision compared with the previous investigation. The key drivers of this increase are:

- The increase in the IBNR for Fire and SME reflects the adjustments made for incorrectly processed reinsurance recoveries at the previous valuation.
- The IBNR provision for the Combined class has reduced significantly since the previous valuation due to the increase in quota share percentage from 50% ceded to 70%.
- An explicit $0.3 million IBNR has been released for AMEX NAC.

Earthquake Claims

The gross outstanding claims liabilities include $110 million for the 2010 and 2011 Canterbury earthquakes claims. Gross IBNR of $17.25m has been adopted for 2010 in relation to development on the Universities of NZ claims, in particular in relation to Lincoln University. These amounts were reserved in January. The net liability for the earthquake claims is $0 (excluding CHE).

3.5 Casualty

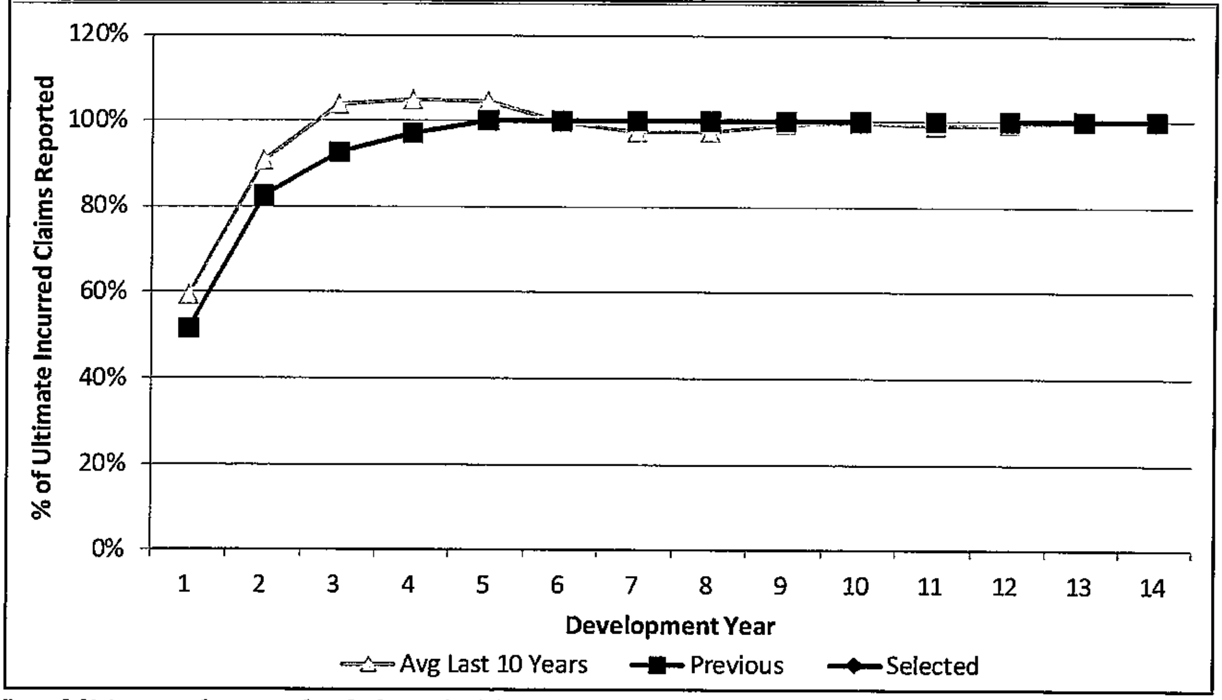
AIL NZ's Casualty business consists of primary and excess generally liability policies covering both public and products liability. There are some accounts with overseas exposures, including USA and Australian bodily injury exposure.

The primary general liability portfolio has exhibited a relatively stable and consistent pattern of claim development over a very long history (over 20 years). This is a "medium" tailed portfolio with incurred claims generally developing for 4 to 5 years.

We have assumed initial estimated net loss ratios of 42% for 2012 compared to 60% for 2011. The 2012 loss ratio reflect our plan loss ratios for 2012 and recognised the favourable experience in recent years. I have not revised the initial estimated net loss ratio for earlier accident years and have retained the assumptions from the previous investigation.

The expected incurred claim development pattern for primary liability has been derived from historical experience reflecting the unique nature of the New Zealand environment, with the Accident and Compensation Commission providing insurance coverage for most bodily injury claims. These development factors are unchanged from the previous investigation.

Figure 3.1 – Primary General Liability Net Incurred Claims Development Factors

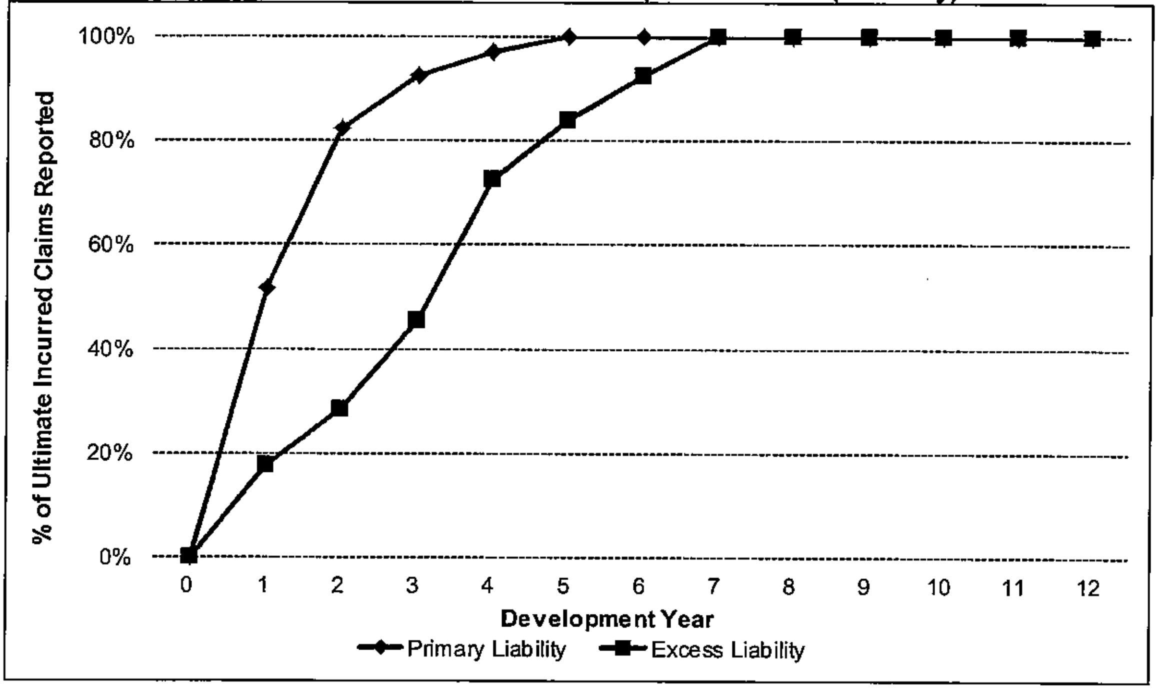


In addition to the standard chain ladder projections we have added an additional reserve in accident year 2000 for AIL NZ's potential exposure to "leaky building" claims. During 2012 there has been only limited activity on leaky building claims. I have retained the IBNR allowance for net losses of $0.6 million and gross losses of $1.0 million from the previous investigation.

For the general liability excess portfolio, there have been negligible incurred claims over the past 20 years. There remains a material exposure to potential large losses. This exposure, however, is limited by the low XOL reinsurance attachment. I have adopted the Formula method which adopts the Loss Ratio Method for the 2012 accident year, a mixture of the Loss Ratio and BF methods for the 2011 accident year, and the BF method for all prior accident years. This is consistent with the selection of methods adopted at the last valuation. I have assumed an initial estimated net loss ratio of 10% reflecting the low frequency of these claims and the reinsurance protection against large losses.

As there have been negligible incurred claims for excess liability, the expected incurred claim development pattern adopted for excess liability has regard to (but is faster than) ACE Group's experience in Australia reflecting the fact that exposures for this portfolio are often outside New Zealand. The development pattern is considerably slower than the development factors adopted for the primary liability portfolio. The primary and excess development patterns are detailed in Figure 3.2 below and are unchanged from the previous valuation.

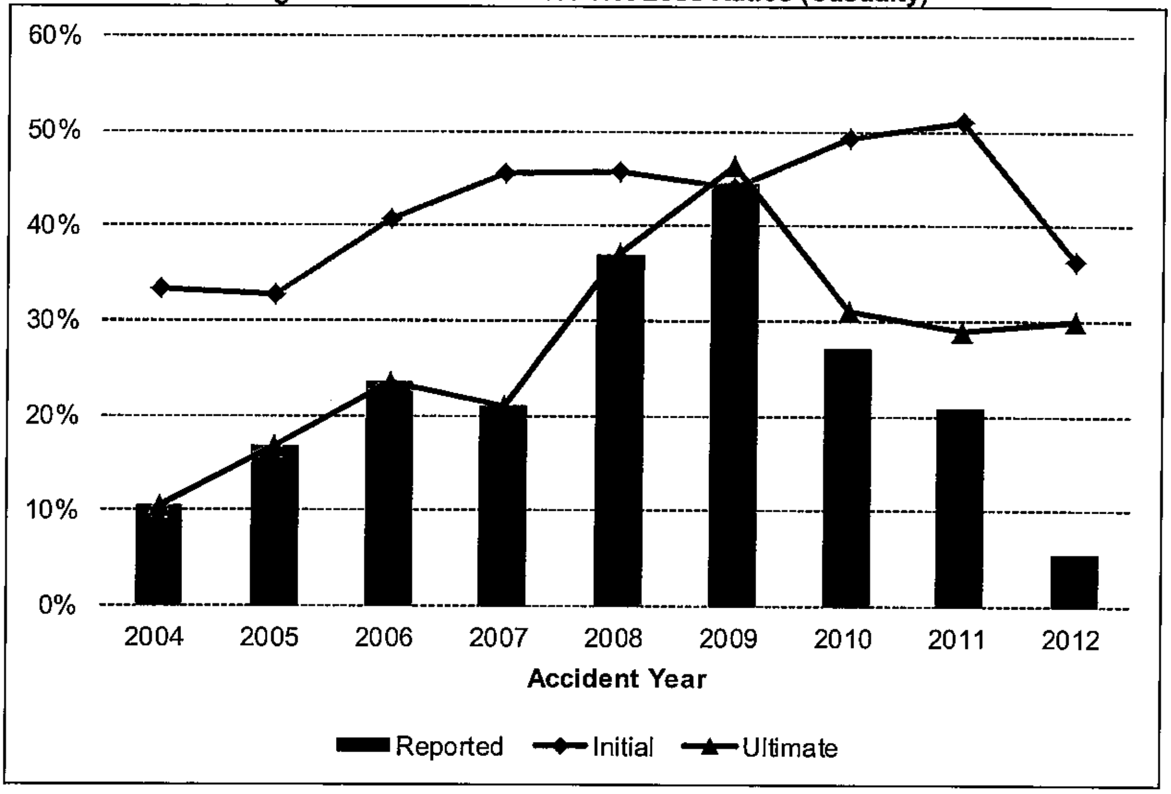
Figure 3.2 – Incurred Claim Development Pattern (Casualty)



The total central estimate provision for outstanding claims (discounted, including claims handling expenses) is $6.85 million net and $14.2 million gross.

The combination of the above initial loss ratios and incurred claims development patterns leads to the following net ultimate loss ratios for the total Casualty portfolio.

Figure 3.3 – Undiscounted Net Loss Ratios (Casualty)



This graph shows that the consistently favourable performance of this portfolio with only the 2009 accident year impacted by large losses.

Appendices E and F contain details of the incurred claims triangulations, chain ladder development ratio selections and BF projections.

3.6 Financial Lines

AIL NZ's Financial Lines business consists of relatively small portfolios of Directors & Officers, Financial Institutions and Professional Indemnity business. The Professional Indemnity portfolio has reduced considerably in recent years following the loss of an accountant's scheme arrangement in 2008. These classes are long tailed with claims typically developing up to 8 to 10 years.

Generally the selected methods are consistent with the principles described in Section 3.3 and the selections adopted at the previous valuation.

For Financial Institutions manual adjustments have been made due to very low and volatile net premiums which are impacted by a mismatch in the timing of reinsurance premium payments relative to the gross premiums.

For Directors & Officers and Financial Institutions I have initial net loss ratios of 40% for 2005 and prior increasing to around 50% in 2012. The increase in initial loss ratios reflects premium rate reductions over this period. These initial loss ratios are the same as adopted at the previous valuation.

Due to the small size of the portfolio and the limited claims experience the initial loss ratios are subjective but take into account the following: following:

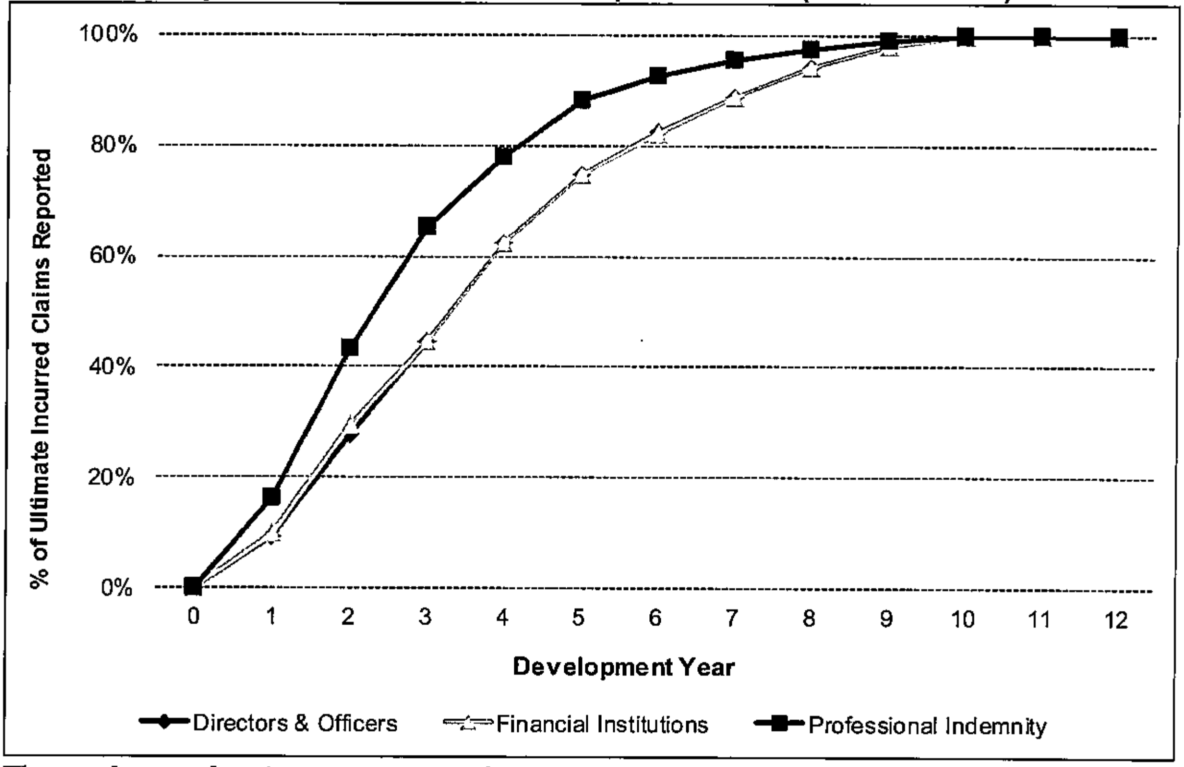
- ICNZ industry statistics
- Reinsurance premium and structure
- AIL NZ emerging New Zealand experience
- ACE Group regional claims experience.

For Professional Indemnity, the loss ratios the 2005 year are impacted by leaky building claims. I have adopted the ICD method which is consistent with the previous valuation. The initial expected loss ratios for years 2006 onwards have been retained from the previous valuation.

The 2012 net loss ratio of 47% is consistent with the plan loss ratio assumption which was based on a detailed review of prior accident year experience.

At last year's valuation, for the expected incurred claim development pattern, Finity derived a development pattern based on their knowledge of AIL NZ's Financial Lines and the emerging experience of each of these portfolios. Professional Indemnity claims are expected to develop more quickly than the other Financial Lines classes. The development patterns detailed in Figure 3.4 below, are consistent with the loss development selections for the Professional Indemnity class from the previous investigation.

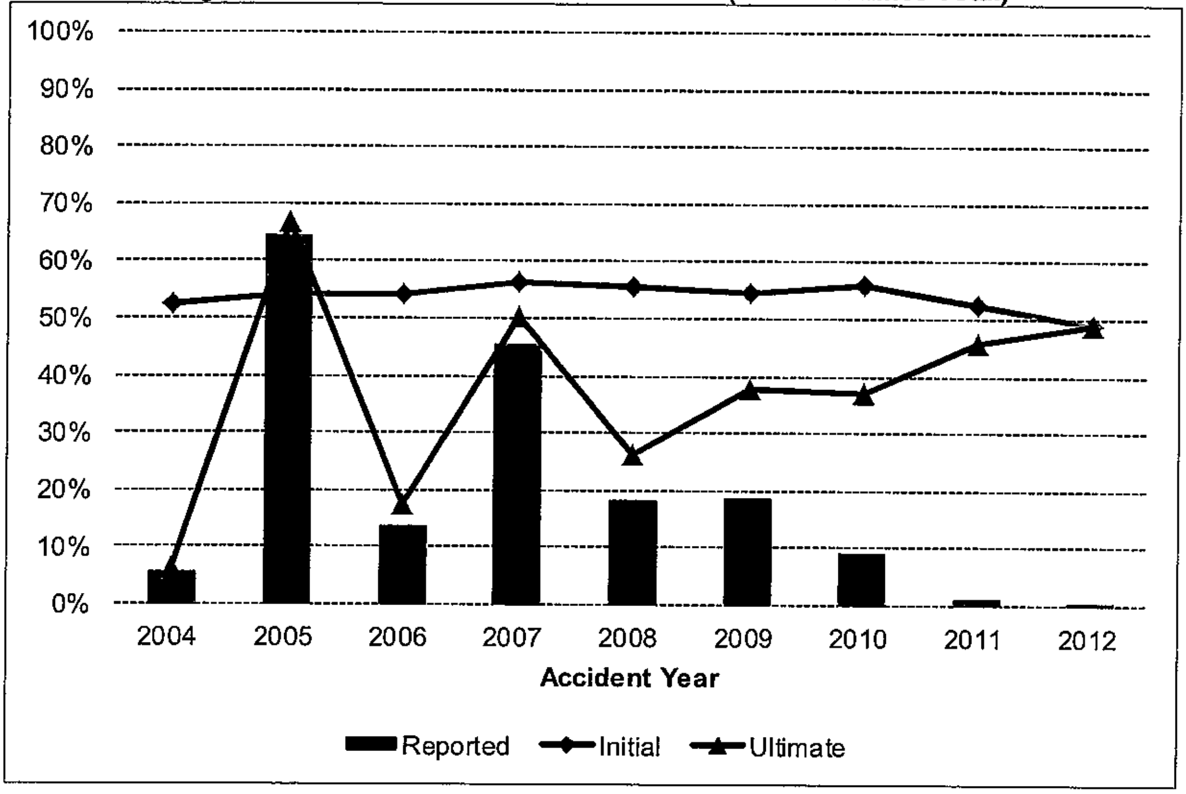
Figure 3.4 – Incurred Claim Development Pattern (Financial Lines)



The total central estimate provision for outstanding claims (discounted, including claims handling expenses) for the Financial Lines portfolio is $4.0 million net and $9.4 million gross.

The combination of the above initial loss ratios and incurred claim development patterns leads to the following estimated net ultimate loss ratios for the total Financial Lines portfolio as detailed in Figure 3.5 below:

Figure 3.5 – Undiscounted Net Loss Ratios (Financial Lines Total)



The Professional Indemnity portfolio has generally had greater incurred claims relative to the Directors & Officers and Financial Institutions portfolio. The 2005 accident year was impacted by leaky building claims and the 2007 accident year was impacted by large Professional Indemnity claims.

Appendices E and F contain details of the incurred claims triangulations, chain ladder development ratio selections and BF projections.

3.7 Worker's Compensation

AIL NZ underwrote Worker's Compensation business in 1999 and 2000 during the period of the privatisation of this market. The experience has generally been benign with only a small amount of case estimate remaining that relates to a claim where the claimant is unable to return to work and ongoing medical care is required.

As it is now 11 years since exposure ceased on this portfolio. We consider the case estimates to be an adequate estimate of the future claims liabilities with no allowance for IBNR. This is the same basis as adopted at the previous valuation.

In addition to this Worker's Compensation AIL NZ underwrites a small portfolio of Workers Compensation business that provides DIC (Difference in Conditions) coverage to insurance provided by the New Zealand Accident & Compensation Commission. For 2009 and prior years this business is included in the general liability primary portfolio.

There have been no claims against this portfolio and the formula method has selected the Loss Ratio method for the latest accident year and BF method for prior accident years to value this portfolio. The assumed initial loss ratio for 2012 is 64% net and 50% gross based on our plan for this class.

The net liability for this class is $0.1 million (excluding CHE).

3.8 Unrecoverable Reinsurance

AIL NZ has relatively limited exposure to unrecoverable reinsurance as most of the projected reinsurance recoveries are from internal XOL treaties (with Tempest Re). AIL NZ does have some exposure to external reinsurers via facultative reinsurance and historical external reinsurance treaties. AIL NZ also has some exposure to other ACE Group entities (for example ACE Malaysia, as demonstrated in the case of the NZ earthquakes).

As at 31 December 2012, AIL NZ's Finance department has advised that there are no known exposures to unrecoverable reinsurance on outstanding claims.

Owing to the valuation methods adopted for this investigation, there is an indirect allowance for future unrecoverable reinsurance to the extent that the past claims experience contains net claim payments that are gross of uncollectible reinsurance. Taking this into account we have made no explicit allowance for any further future unrecoverable reinsurance.

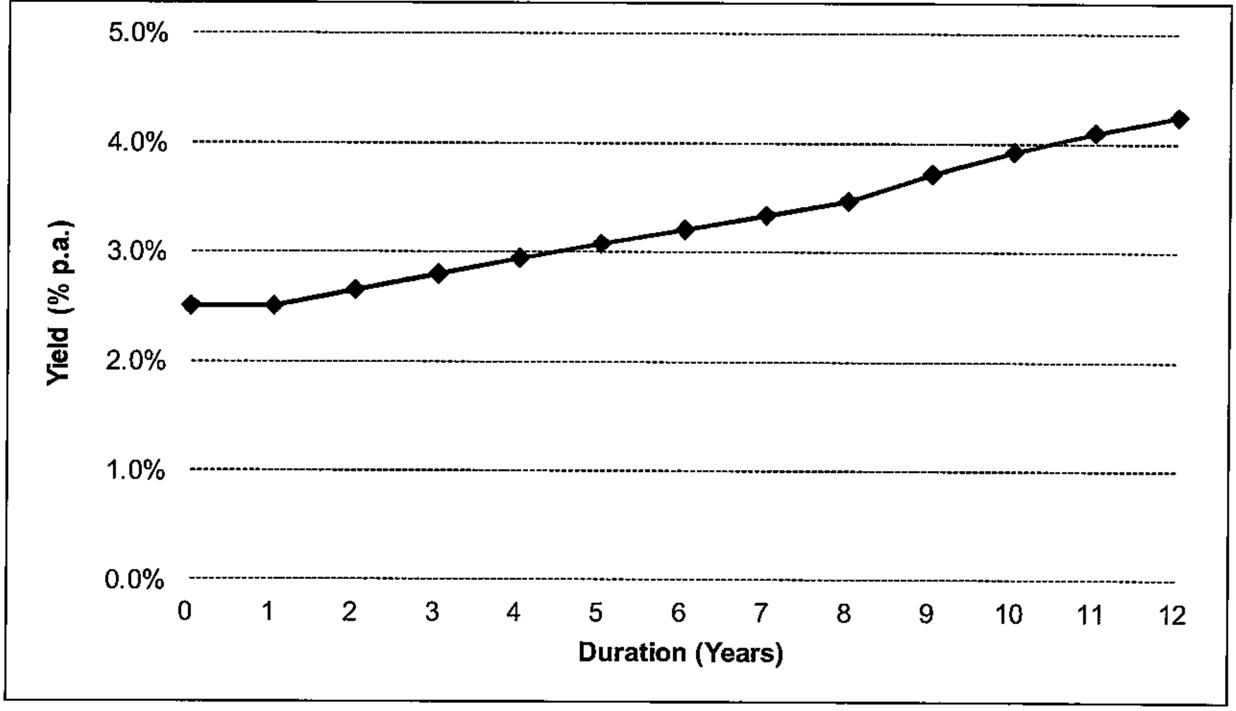
3.9 Discounting for Investment Income

The estimates of the outstanding claims are required to be discounted for future investment income attributable to the provision during the run-off period.

The discount rate adopted for the outstanding claims liabilities is based on NZ risk free Government Bond yields as at 31 December 2012. The adopted yield curve is shown in the following chart.

In comparison to the previous investigation, the yield curve has fallen slightly across all durations. This change has an immaterial impact on the net outstanding claims reserves.

Figure 3.6 – NZ Government Bond Yield Curve as at 31 December 2012



3.10 Claims Handling Expenses (CHE)

The accounting standard IFRS4 requires an allowance for indirect claims handling expenses (CHE) to be included in the provision for outstanding claims.

Details of indirect CHE are available from AIL NZ's Enhanced Expense Management System ("EEMS"). EEMS captures direct costs associated with the claims management function as well as apportioning indirect costs (e.g. such as AIL NZ management).

In late 2007 AIL NZ undertook a regional initiative to reduce expenses by developing a specialised Shared Services Unit (SSU) in the Philippines. The SSU undertook processing of most aspects of claims for the Accident & Health classes of business. This has led to investment costs that will be incurred over a number of years that has led to the additional cost strain on the New Zealand business.

Indirect CHE as a percentage of gross claim payments average 2.6% over the period 2006 to 2017. In 2008 this percentage increased to 8.1% before reducing to 4.7% in 2010. In 2011 and 2012, the percentage fell once again to 1.5%, impacted by the high gross claim payments on the catastrophe losses. I have retained the CHE assumptions (as a % of gross claim payments) of 4.5% for Combined and 5.7% for all other classes except Fire and SME.

For the Fire and SME portfolios the impact of the Canterbury Earthquake has been to increase the gross outstanding claims for these classes considerably. It is not expected that corresponding CHE will increase significantly. Consequently the future CHE for these classes has been reduced to 0.43%, the same assumption as adopted for the previous valuation.

4 Premium Liabilities

The Premium Liabilities are defined as Insurance Liabilities that relate to claim payments arising from future events insured under existing policies up until their next renewal. The value of Premium Liabilities will also need to include an allowance for claims handling expenses associated with these claim payments and also expenses associated with the future periods of exposure under existing policies up until their next renewal.

4.1 Methodology

The methodology used to determine the Premium Liabilities is as follows:

(i) Calculate the gross and net unearned premium by valuation class, including an allowance for unclosed business.

(ii) Calculate appropriate gross and net undiscounted loss ratios

(iii) Determine the expected ultimate cost of claims arising by multiplying the unearned premium by the adopted undiscounted loss ratio for each class of business

(iv) Apply discounting to the expected ultimate cost to arrive at the gross and net discounted central estimates, net of expenses

(v) Set an expense allowance for the remainder of the policy year

(vi) Calculate the future reinsurance costs and expected recoveries for the remainder of the policy year

(vii) Determine the Premium Liabilities central estimate as the sum of items iv to vi

4.2 Unearned Premium

The unearned premium in respect of closed business was provided by AIL NZ's Finance department from the "Peoplesoft" ledger.

To estimate the unearned premium in respect of unclosed business with an effective date prior to year end, a projection model was developed which uses standard actuarial techniques to project to ultimate the written premium and the ultimate earned premium by attachment quarter and class of business. The projected future written and earned premium bookings by quarter were then calculated. The unearned portion was then calculated by subtracting the unclosed earned premium from the unclosed written premium. For classes with losses occurring XOL reinsurance the estimate of unclosed unearned premium includes an implicit allowance for the future reinsurance cost.

The net unearned premium in respect of closed business does not include unearned reinsurance premium in respect of losses occurring XOL treaty reinsurance (with the exception of Accident & Health). As such, an adjustment is required to the unearned premium before applying the selected loss ratios to derive the expected claims cost for the unexpired risk. The adjustment is based on the losses occurring XOL treaty reinsurance rates detailed below.

A summary of the unearned premium calculations is shown in Table 4.1.

Table 4.1 – Net Unearned Premium Summary

Class	Closed Net UEP ($'000s)	Unclosed Net UEP ($'000s)	Total Net UEP ($'000s)	XOL RI Adjustment	Total Adjusted Net ($'000s)
A&H DM - AMEX NAC	35	0	35	0.0%	35
A&H Travel - Partner AMEX	2	0	2	0.0%	2
A&H DM - AMEX Other	8	33	41	0.0%	41
A&H DM - Other	6	0	6	0.0%	6
A&H Travel - Partner Other	9	43	52	0.0%	52
A&H GPA & Other	2,083	228	2,312	0.0%	2,312
A&H Travel Group	20	222	241	0.0%	241
A&H Travel - Traditional	0	0	0	0.0%	0
B&M	1,364	140	1,504	42.7%	862
CAR EAR	435	34	469	39.8%	283
Combined	2,239	67	2,306	0.0%	2,306
Commercial Auto	0	0	0	0.0%	0
D&O	998	104	1,102	0.0%	1,102
Financial Instit	183	42	225	0.0%	225
Fire	21,776	2,067	23,842	35.9%	15,280
GL Excess	199	93	292	0.0%	292
GL Primary	2,271	309	2,579	0.0%	2,579
GL Tail	0	0	0	0.0%	0
Marine Cargo & Hull	21	1	23	15.3%	19
Oil & Petro Offshore	0	0	0	0.0%	0
Oil & Petro Onshore	0	0	0	0.0%	0
Personal Other	0	0	0	0.0%	0
Professional Indemnity	400	55	455	0.0%	455
SME	7	0	7	0.0%	7
WC EL	31	11	42	0.0%	42
Total	32,085	3,449	35,535	26.4%	26,141

4.3 Undiscounted Loss Ratios

The selected loss ratios to apply to the unearned premium to determine the net claims cost for the unexpired risk are shown in Table 4.2. I have also included the selected loss ratios from the 31 December 2011 valuation.

Table 4.2 – Selected Net Loss Ratios

Class	Selected 2012	Selected 2011
A&H DM - AMEX NAC	35.0%	35.0%
A&H Travel - Partner AMEX	40.3%	40.3%
A&H DM - AMEX Other	20.1%	20.1%
A&H DM - Other	20.2%	20.2%
A&H Travel - Partner Other	48.3%	48.3%
A&H GPA & Other	50.0%	50.0%
A&H Travel Group	90.0%	90.0%
A&H Travel - Traditional	73.7%	73.7%
B&M	39.7%	39.7%
CAR EAR	40.5%	40.5%
Combined	25.0%	25.0%
Commercial Auto	77.0%	77.0%
D&O	50.0%	50.0%
Financial Instit	50.0%	50.0%
Fire	42.3%	42.3%
GL Excess	10.0%	6.0%
GL Primary	42.4%	42.4%
GL Tail	0.0%	0.0%
Marine Cargo & Hull	62.8%	62.8%
Oil & Petro Offshore	0.0%	0.0%
Oil & Petro Onshore	0.0%	0.0%
Personal Other	30.0%	30.0%
Professional Indemnity	46.9%	46.9%
SME	50.6%	50.6%
WC EL	0.0%	0.0%

The adopted loss ratios for this valuation are generally consistent with those adopted at the previous valuation. The only change is in respect of GL Excess which has been adjusted to bring the assumption in line with the plan loss ratio.

4.4 Discounting

The expected future cash flows are derived by applying the claim payment patterns, determined from the outstanding claims analysis, by class of business to the undiscounted central estimates (net of expenses).

Discounted cash flows are then determined by applying the discount rates as set out in Section 3.

4.5 Non-acquisition Expense Allowance

Expenses, other than the cost of acquisition, have been estimated from an analysis of AIL NZ's past expenses.

The allowance for claims handling expenses is based on the same percentage as that adopted for the outstanding claims investigation. It is noted that the allowances could be slightly different due to the additional cost of setting up a new claim (which is required for unexpired risk but not for outstanding claims). However, any such adjustment is considered not to be material.

The allowance for policy maintenance expenses has been determined in a similar way to claims handling expenses using AIL NZ's EEMS reports and grouping of classes of business. Table 4.3 shows the selected underwriting expenses expressed as a percentage of Gross Written Premium (excluding all statutory charges and levies).

Table 4.3 – Underwriting Expenses (% of Gross Written Premium)

Class	Selected 2012	Selected 2011
A&H DM - AMEX NAC	12.0%	12.0%
A&H Travel - Partner AMEX	12.0%	12.0%
A&H DM - AMEX Other	12.0%	12.0%
A&H DM - Other	12.5%	12.5%
A&H Travel - Partner Other	12.5%	12.5%
A&H GPA & Other	12.5%	12.5%
A&H Travel Group	12.5%	12.5%
A&H Travel - Traditional	12.5%	12.5%
B&M	12.5%	12.5%
CAR EAR	12.5%	12.5%
Combined	17.5%	17.5%
Commercial Auto	12.5%	12.5%
D&O	12.5%	12.5%
Financial Instit	12.5%	12.5%
Fire	12.5%	12.5%
GL Excess	12.5%	12.5%
GL Primary	12.5%	12.5%
GL Tail	12.5%	12.5%
Marine Cargo & Hull	12.5%	12.5%
Oil & Petro Offshore	12.5%	12.5%
Oil & Petro Onshore	12.5%	12.5%
Personal Other	12.5%	12.5%
Professional Indemnity	12.5%	12.5%
SME	12.5%	12.5%
WC EL	12.5%	12.5%

A work effort analysis of underwriting expenses carried out in 2008 estimated that 60% of expenses relate to acquisition and product development costs leaving 40% of the above expenses to be allocated to policy maintenance costs. The analysis excluded "solicitation" expenses relating to external telemarketing expenses.

Since 2008 this assumption of a 60% / 40% allocation of underwriting expenses has been adopted for all classes except direct marketing classes. For direct marketing, 90% of underwriting expenses have been allocated to acquisition.

Following the finalisation of the valuation results I have been provided with an updated work effort analysis carried out in February 2013. This analysis estimated that 46% of expenses relate to acquisition and product development costs leaving 54% of the above expenses to be allocated to policy maintenance costs.

I have reviewed this analysis. I have retained my original assumptions for policy maintenance costs and believe they remain appropriate for the following reasons:

- The underwriting expenses assumptions in table 4.3 are conservative based on my updated analysis of expenses
- The 54% of underwriting expenses allocated to policy maintenance costs is not uniformly applicable to premium liabilities as these expenses are on average weighted towards the start of the policy period (e.g. policy processing). Hence the 54% assumption will be reduced towards the current assumption of 40%.

I will perform a more detailed analysis of expenses at the next valuation.

4.6 Non-Reinsurance Recoveries and GST

The adopted rates for non-reinsurance recoveries and GST adjustments are the same as those set out in the outstanding claims analysis and are documented in Appendix E.

4.7 Future Reinsurance Costs and Recoveries

For premium liability estimates, an allowance must be made for the expected XOL losses occurring treaty reinsurance expense subsequent to the balance date (i.e. associated with the unexpired risk). Losses occurring XOL treaties apply only to short tail class treaties. Table 4.4 details the XOL percentages applied based on known 2012/2013 reinsurance treaty rates, and compares these to the 2011/2012 rates.

For Accident & Health and Fire treaty rates reduced. For Fire, despite AIL maintaining the same statutory net retention of USD 250,000, ACE Tempest Re (ATR) retained more of the reinsurance programme internally. The cost to AIL of the reinsurance retained by ATR was less expensive than the cost of external reinsurance arrangements.

For quota share and risks attaching treaties reinsurance has been expensed when the premium was written.

Future reinsurance recoveries on unexpired risk are allowed for via the selection of gross and net loss ratios.

Table 4.4 – Losses Occurring XOL RI Treaty Rates

Class	Selected 2012	Selected 2011
A&H DM - AMEX NAC	8.3%	9.1%
A&H Travel - Partner AMEX	8.3%	9.1%
A&H DM - AMEX Other	8.3%	9.1%
A&H DM - Other	8.3%	9.1%
A&H Travel - Partner Other	8.3%	9.1%
A&H GPA & Other	8.3%	9.1%
A&H Travel Group	8.3%	9.1%
A&H Travel - Traditional	8.6%	9.1%
B&M	42.7%	42.7%
CAR EAR	39.8%	39.8%
Combined	0.0%	0.0%
Commercial Auto	0.0%	0.0%
D&O	0.0%	0.0%
Financial Instit	0.0%	0.0%
Fire	35.9%	49.8%
GL Excess	0.0%	0.0%
GL Primary	0.0%	0.0%
GL Tail	0.0%	0.0%
Marine Cargo & Hull	15.3%	13.5%
Oil & Petro Offshore	0.0%	0.0%
Oil & Petro Onshore	0.0%	0.0%
Personal Other	0.0%	0.0%
Professional Indemnity	0.0%	0.0%
SME	0.0%	0.0%
WC EL	0.0%	0.0%

4.8 Central Estimate Results

Table 4.5 provides a summary of the gross and net central estimates of AIL NZ's premium liabilities at 31 December 2012. Full details of the results on a discounted and undiscounted basis and by valuation class of business are set out in Appendix B.

Table 4.5 – Premium Liabilities Central Estimate at 31 December 2012

Premium Liabilities	$'000
Estimate of Gross Claims Liability	27,811
Plus Future Claims Expenses	14,197
Central Estimate of Gross Liability	**42,008**
Less Recoveries	17,194
Central Estimate of Net Liabilities	**24,814**

The total net liability for premium liabilities requires a risk margin to be added to the above net central estimate. Results including risk margins are presented in Section 6.

5 Risk Margins

5.1 Uncertainty

There is inherent uncertainty in any estimate of insurance liabilities that limits its accuracy. The estimates given in Section 3 and 4 are indeed estimates in the sense that there is a degree of uncertainty as to the difference that will ultimately arise between those estimates and the final actual result of experience.

This uncertainty can be considered to arise from five sources:

(i) Because the nature of the claims process is not fully understood, it might be that none of the various models used is an entirely accurate representation of reality.

(ii) Because there are components of randomness in the claims process, it is not possible to estimate the parameters of that process with complete precision even if complete confidence were felt in the nature of the model.

(iii) Any erroneous data will similarly have introduced uncertainties into the estimate of those parameters.

(iv) Even if the parameters could be estimated with precision, it would not be possible to predict outstanding claims with the same precision because of the random component in future experience.

(v) It is possible that systemic (i.e. non-random) changes may occur in claims experience.

It may be possible to estimate the extent of uncertainty attributable to ii and iv above by statistical techniques. The other sources of uncertainty are not readily quantifiable.

The central estimate represents the best estimate of the insurance liabilities and hence contains no deliberate bias towards over or under estimation. In general terms, we consider it equally likely that the ultimate claims outcome on business brought to account at the effective date of valuation will be greater or less than that provided for by the central estimate.

5.2 Risk Margins

As it is impossible to predict future claims outcomes with certainty, a value judgement has to be made as to the level of reserves that offers a reasonable assurance of sufficiency. Setting this level is the responsibility of AIL NZ's Board of Directors. It is usual, and in our view proper, for the Board of Directors of a general insurer to require more than the 50% probability of adequacy that we assess the central estimate provides. The additional probability of adequacy is provided by the addition of a Risk Margin.

The setting of a risk margin involves subjective assessment. In our view, it should take into account the following factors:

- The variability of the claims experience of the portfolio. For instance, property risks are less variable than liability risks, and because they are settled sooner are not as prone to the uncertain impacts of factors such as inflation and landmark court cases.
- Portfolio size - taken in aggregate outcomes for smaller portfolios will be subject to greater relative variability than larger portfolios.
- The extent of reinsurance protection – reinsurance may have the effect of reducing the relative variability of claims outcomes.
- The quality and quantity of historical data, both from the point of view of reliability of data and comparability to business currently underwritten.
- The risk appetite of the Company directors. A more risk averse company will require a higher level of confidence that its provisions will ultimately prove to be adequate than a company that is less risk averse.
- Any statutory or regulatory requirements (see below for comments).
- Consistency between different years of account. This is an important issue. Change should reflect changing circumstances such as a change in the nature of the business underwritten, or a perceived change in the reliability of the estimates.

5.3 Statutory/Regulatory requirements for Risk Margins

Under NZ Accounting Standard IFRS4 and RBNZ solvency standard for non-life insurance business there is a requirement to include a risk margin. AIL NZ Board of Directors has advised that they wish the risk margin to be set to a 75% probability of sufficiency.

5.4 Quantium Review

During 2012 AIL NZ commissioned a review of the risk margins by Quantium. A copy of this work is attached at Appendix D. Last year Finity reviewed the Quantium report at a high level and discussed the results with them. I am satisfied that the risk margins adopted for the previous valuation remains appropriate for this valuation.

The following table compares the risk margins to those used for the previous valuation.

Table 5.1 – Current and Previous Adopted Risk Margins

	Adopted Risk Margins	
Class	Outstanding Claims	Premium Liabilities
A&H	10.6%	12.8%
Combined A&H	8.2%	10.7%
P&C ST / SME	13.2%	19.1%
Financial Lines	15.0%	23.6%
Casualty	13.8%	20.9%
Other	14.4%	22.2%
Total	14.1%	20.0%

Previously the analysis was undertaken for all portfolios combined (excluding the Combined portfolio), and the same margin was thus adopted for each class. Hence the comparison by class may be misleading. But in any case, the risk margins have reduced significantly. We believe the lower margins are reasonable, having regard to the stability in the loss development experience we have observed.

5.5 Summary of Selected Risk Margins

Table 5.2 shows the recommended risk margins for gross and net outstanding claims and premium liabilities as a percentage of the corresponding net central estimates, by class of business, to achieve an overall 75% probability of adequacy.

Table 5.2 – Selected Risk Margins 75% Probability of Sufficiency

	Outstanding Claims		Premium Liabilities	
Class of Business	Gross	Net	Gross	Net
A&H DM - AMEX NAC	11%	11%	13%	13%
A&H Travel - Partner AME	11%	11%	13%	13%
A&H DM - AMEX Other	11%	11%	13%	13%
A&H DM - Other	11%	11%	13%	13%
A&H Travel - Partner Othe	11%	11%	13%	13%
A&H GPA & Other	11%	11%	13%	13%
A&H Travel Group	11%	11%	13%	13%
A&H Travel - Traditional	11%	11%	13%	13%
B&M	13%	13%	19%	19%
CAR EAR	13%	13%	19%	19%
Combined	8%	8%	11%	11%
Commercial Auto	13%	13%	19%	19%
D&O	15%	15%	24%	24%
Financial Instit	15%	15%	24%	24%
Fire	13%	13%	19%	19%
GL Excess	14%	14%	21%	21%
GL Primary	14%	14%	21%	21%
GL Tail	14%	14%	21%	21%
Marine Cargo & Hull	13%	13%	19%	19%
Oil & Petro Offshore	13%	13%	19%	19%
Oil & Petro Onshore	13%	13%	19%	19%
Personal Other	14%	14%	22%	22%
Professional Indemnity	15%	15%	24%	24%
SME	13%	13%	19%	19%
WC EL	14%	14%	21%	21%

6 Summary of Results

Our estimate of the insurance liabilities valued in accordance with IFRS4 is summarised in the table below. The results include a risk margin sufficient to secure the insurance liabilities to a 75% probability of sufficiency.

Table 6.1 – Summary of Insurance Liabilities

	Outstanding Claims $'000	Premium Liabilities $'000	Total $'000
Estimate of Gross Claims Liability	175,832	27,811	203,643
Plus Future Claims Expenses	2,500	14,197	16,696
Central Estimate of Gross Liability	**178,332**	**42,008**	**220,340**
Less Recoveries	155,901	17,194	173,096
Central Estimate of Net Liabilities	**22,430**	**24,814**	**47,244**
Plus Risk Margin on Net Liability	2,942	3,170	6,112
Net Insurance Liabilities	**25,372**	**27,984**	**53,356**

The total recommended net outstanding claims liability provision as at 31 December 2012 is $25.4 million. This compares with the recommended provision at 31 December 2011 of $25.3 million. This combined with a recommended premium liability provision of $28.0 million gives a total insurance liability provision of $50.472M.

Full details of the results on undiscounted and discounted bases are provided in Appendix E.

7 Reconciliation with Previous Estimates

Under PS300 the net outstanding claims liabilities are required to be reconciled to the net outstanding claims and premium liabilities at the previous investigation. We have split this reconciliation into 2011 and prior year experience (outstanding claims liability at previous investigation) and 2012 experience (premium liability at previous investigation).

The basis adopted for reconciling the outstanding claims liability at the previous investigation is as follows:

- Calculate the expected undiscounted central estimate at 31 December 2012 by deducting the payments made in 2012 from the undiscounted central estimate at the previous valuation.
- Produce the roll forward reserve at 31 December 2012 by applying the previous years' valuation models to the current data. No changes are made to any assumptions. The difference between the roll forward reserve and the expected reserve is the experience movement.
- Calculate the movement in the undiscounted central estimate by changing the assumptions made for the 31 December 2011 valuation. The impact of the changes in assumptions have been split into the following categories:
  - Change in IELR selections for BF method
  - Change in ICD factors
  - Change in selected model
  - Other changes
- Calculate the discounted outstanding claims reserve assuming prior year CHE, Risk Margin (at 75% probability of sufficiency) and Discount Rate.
- Calculate the movement in discounted outstanding claims reserve by changing the assumptions for CHE and Risk Margins then applying the current year Discount Rate.

The basis adopted for reconciling the premium liability at the previous investigation is as follows:

- Calculate the expected undiscounted central estimate by multiplying the undiscounted premium liability loss ratio at the previous investigation by the net earned premium for the 2012 accident year and then deducting payments made in 2012.
- Produce the roll forward reserve at 31 December 2012 by applying the previous year's valuation models to the current data. No changes are made to any assumptions. The difference between the roll forward reserve and the expected reserve is the experience movement.

- Calculate the movement in the undiscounted central estimate by changing the assumptions made for the 31 December 2012 valuation. The impact of the changes in assumptions have been split into the following categories:
  - Change in IELR selections for BF method
  - Change in ICD factors
  - Change in selected model
  - Other changes
- Calculate the discounted outstanding claims reserve assuming prior year CHE, Risk Margin and Discount Rate.
- Calculate the movement in discounted outstanding claims reserve by changing the assumptions for CHE and Risk Margins then applying the current year Discount Rate.

The reconciliation is shown by portfolio in Appendix C. The overall results are shown below.

Table 7.1 – Reconciliation of 2011 Net Outstanding Claims Reserve – Total

	Health ($'000s)	Tail ($'000s)	Tail ($'000s)	Lines ($'000s)	Combined ($'000s)	Total ($'000s)
2011 Undisc OSC (excl CHE & RM)	**1,813**	**5,338**	**11,450**	**-703**	**1,492**	**19,390**
Paid 2012	1,321	854	8,577	-716	1,166	11,203
Expected Undisc OSC (excl CHE & RM)	**1,321**	**854**	**8,577**	**-716**	**326**	**10,363**
Experience Impact	*-873*	*-126*	*-916*	*0*	*-78*	*-1,994*
Change in ICD Factors/IELRs	*0*	*1,730*	*-78*	*64*	*0*	*1,716*
Change in Method	*19*	*0*	*-329*	*0*	*0*	*-310*
Changes - Other	*0*	*0*	*0*	*0*	*0*	*0*
2012 Actual Undiscounted Reserve	**468**	**2,458**	**7,253**	**-652**	**248**	**9,775**

Table 7.2 – Reconciliation of 2011 Net Premium Liability Reserve – Total

	Accident & ($'000s)	P&C Short ($'000s)	P&C Long ($'000s)	Commercial ($'000s)	Combined ($'000s)	Total ($'000s)
2011 Undisc PL (excl CHE, UW Exp & RM)	**1,622**	**4,030**	**2,069**	**0**	**1,426**	**9,147**
2011 Undisc PL (excl CHE, UW Exp & RM) - 2012 NE	**3,058**	**8,232**	**3,489**	**-27**	**2,683**	**17,436**
Paid 2012	*1,703*	*2,760*	*55*	*0*	*1,405*	*5,923*
Expected Undisc OSC (excl CHE & RM)	**1,355**	**5,472**	**3,434**	**-27**	**1,278**	**11,513**
Experience Impact	*99*	*0*	*0*	*0*	*-92*	*7*
Change in ICD Factors/IELRs	*396*	*-5*	*39*	*-1*	*0*	*429*
Change in Method	*-548*	*-80*	*-404*	*28*	*0*	*-1,003*
Changes - Other	*0*	*0*	*0*	*0*	*0*	*0*
2012 Actual Undiscounted Reserve	**1,302**	**5,387**	**3,070**	**0**	**1,187**	**10,945**

Table 7.1 shows that there has been favourable experience for 2012, with the undiscounted claims costs for prior accident years $0.6 million lower than was estimated at the previous valuation. The main driver of the variation was favourable development for Casualty, Financial Lines and Accident and Health, offset partially by Fire.

Table 7.2 shows that the current estimate of claim costs for the 2012 accident year is $0.6 million lower than that expected based on the loss ratio assumptions adopted for the previous premium liability valuation, primarily relating to long tail classes.

The impact of changing discount rates has had an immaterial impact.

8 Sensitivity Analysis

A sensitivity analysis has been carried out on the net discounted outstanding claims liability and premium liability (including CHE but excluding Risk Margins) considering changes to selected assumptions adopted in the valuation.

The assumptions have been selected based on what have been considered the major areas of uncertainty in the valuation. It should be noted that the assumptions selected for the sensitivity analysis are judgemental, and are consistent with sensitivity analysis conducted for the 2013 Business plan and AIL's Internal Capital Adequacy Assessment Process (ICAAP) and take into consideration a level of deterioration that may result in a review of business strategy. It should be noted that the assumptions selected do not represent the upper or lower bounds of possible outcomes of future experience.

Outstanding claim liability

The first 3 assumption scenarios selected for the outstanding claims sensitivity analysis are based on a 1 in 5 year scenario. The fourth scenario considers a 3 percentage point decrease in discount rate, which roughly equates to a 1 in 30 year scenario.

The assumptions selected for the outstanding claims sensitivity analysis are as follows:

- 10% increase in net outstanding claim liability arising from deterioration in the development experience. This is equivalent to a 15% reduction in the assumed proportion of ultimate claim cost reported to date.
- 10% increase in net outstanding claim liability arising from deterioration in the loss ratio experience. This is equivalent to a 19% deterioration in loss ratio across all classes.
- 0.5 percentage point decrease in the discount rate
- 3 percentage point decrease in the discount rate

Table 8.1 summarises the results of this sensitivity analysis on the outstanding claims liability.

Table 8.1 – Outstanding Claims Sensitivity Analysis (excluding Risk Margins)

Assumption	Net Discounted OSC (incl. CHE) ($mil)	Movement ($mil)	Movement %
Valuation Basis	22.4		
Deterioration in development experience	24.7	2.2	9.9%
Deterioration in loss ratio experience	24.7	2.2	10.0%
0.5 percentage point decrease in discount rate	22.6	0.2	0.8%
3 percentage point decrease in discount rate	23.4	0.9	4.2%

Premium liability

The first 3 assumption scenarios selected for the outstanding claims sensitivity analysis are based on a 1 in 5 year scenario, (although the 2 additional catastrophe events is likely to be more conservative potentially more akin to a 1 in 7 to 1 in 10 year scenario). The fourth scenario considers a 3 percentage point decrease in discount rate, which roughly equates to a 1 in 30 year scenario.

The assumptions selected for the premium liability sensitivity analysis are as follows:

- 15% increase in net premium liability arising from deterioration in the loss ratio experience. This is equivalent to a 15% deterioration in loss ratio across all classes.
- An additional 2 catastrophe events
- 0.5 percentage point decrease in the discount rate
- 3 percentage point decrease in the discount rate.

Table 8.2 summarises the results of this sensitivity analysis on the premium liability.

Table 8.2 – Premium Liability Sensitivity Analysis (excluding Risk Margins)

Assumption	Net Discounted PL (incl. CHE) ($mil)	Movement ($mil)	Movement %
Valuation Basis	24.8		
15% increase in selected net loss ratios	28.5	3.7	15.0%
Additional 2 Net Cat losses	25.4	0.6	2.4%
0.5 percentage point decrease in discount rate	24.7	-0.1	-0.3%
3 percentage point decrease in the discount rate	25.4	0.5	2.2%

9 Reliances and Limitations

The valuation results detailed in this report are estimates, and are subject to a degree of uncertainty regarding the final outcome.

In our judgement, we have employed techniques and assumptions that are appropriate, and the conclusions presented herein are reasonable, given the information currently available. However, it should be recognised that future loss emergence will likely deviate, perhaps materially, from our estimates.

We have performed the work assigned and have prepared this report in conformity with its intended utilisation by persons technically familiar with the areas addressed and for the stated purposes only. Judgements based on the data, methods and assumptions contained in the report should be made only after studying the report in its entirety, as conclusions reached by a review of a section or sections on an isolated basis may be incorrect.

We have made no allowance for catastrophic aggregation of claims from latent sources other than as reflected in the data and from information we have received. Latent claim sources are those where the date of origin of a claim is many years prior to the claim being reported.

This report may be distributed to AIL NZ's auditors and other ACE Group entities. However, we require that if the report is distributed to third parties outside AIL NZ then it must be distributed in its entirety.

Neither the whole of this report, or any part thereof, or any reference thereto may be published in any document, statement or circular nor in any communication with other third parties without prior written approval of the form and context in which it will appear.