AMI INSURANCE LIMITED

ANNUAL REPORT

FOR THE PERIOD ENDED 30 JUNE 2012

KPMG

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Independent Auditor's Report

DIRECTORS' REPORT

The Directors of AMI Insurance Limited (the Company) submit the annual financial statements of the Company for the financial period from date of incorporation on 7 December 2011 to 30 June 2012.

In order to comply with the annual report provisions of the Companies Act 1993, the Directors report as follows:

The names and particulars of the Directors of the Company during or since the end of the financial period are:

Directors

Name	Particulars
The following Directors held office during and since the end of the financial period:	
M M Devine	Appointed 27 April 2012
H A Fletcher	Appointed 05 April 2012
N B Hawkins	Appointed 05 April 2012
J S Johnson	Appointed 05 April 2012
H M Price	Appointed 05 April 2012
R J Wagstaffe	Appointed 05 April 2012
M J Wilkins	Appointed 05 April 2012
The following Directors held office during the financial period:	
J B Balmforth	Appointed 07 December 2011, Resigned 05 April 2012
R M Flower	Appointed 07 December 2011, Resigned 05 April 2012
B D Garguilo	Appointed 07 December 2011, Resigned 05 April 2012
T L Kerr	Appointed 07 December 2011, Resigned 05 April 2012
K G L Nolan	Appointed 07 December 2011, Resigned 05 April 2012
D J Pritchard	Appointed 07 December 2011, Resigned 05 April 2012
P M Shewell	Appointed 07 December 2011, Resigned 05 April 2012

Entries recorded in the Interests Register

No entries in the Interests Register have been made during the financial period ended 30 June 2012 requiring disclosure in this Annual Report pursuant to sections 211(1)(e) and 140(1) of the Companies Act 1993.

Directors' Interest in transactions

There have been no interests registered by Directors in transactions during the financial period ended 30 June 2012.

Share dealings by Directors

There have been no share dealings by Directors during the financial period ended 30 June 2012.

Disclosure of interests by Directors

There are no disclosures of interest required for the period ended 30 June 2012.

Changes in state of affairs

On 16 December 2011, the Company entered into a Sale and Purchase Agreement ('SPA') to acquire the insurance operations of the 'old AMI' (now called Southern Response Earthquake Services Limited, previously AMI Insurance Limited) excluding claims relating to the Canterbury earthquakes of 2010 and 2011 and claims with reinsurance recoveries (defined as 'retained claims'). All conditions of the SPA were met on 5th April 2012. On that day the insurance operations excluding retained claims were transferred to the company and all of the shares in the company were purchased by IAG (NZ) Holdings Limited.

The Directors believe that the state of affairs of the Company at 30 June 2012 is satisfactory.

Appointment of Auditor

The Board has appointed KPMG as auditor to the Company.

KPMG

Use of Company information
During the period, the Board received no notices from the Directors requesting to use company information received in their capacity as Directors, which would not otherwise have been available to them.

Director Remuneration
During the period no directors received any remuneration from the Company.

Director Retirement Allowance
The Company does not provide for retirement allowances to Directors.

Employee Remuneration
Grouped below, in accordance with section 211(1)(g) of the Companies Act 1993, are the number of employees or former employees of the Company, excluding Directors of the Company, who received remuneration and other benefits in their capacity as employees, totalling $100,000 or more, during the period ended 30 June 2012.

Remuneration	Number of employees
$100,000 - $2,089,999	0
$2,090,000 - $2,100,000	1

Remuneration includes salary, performance bonuses, retirement allowances, redundancy payments, payments in lieu of notice, employer's contributions to superannuation, health and insurance plans, motor vehicle and other sundry benefits received in their capacity as employees.

This annual report, together with the accompanying financial statements were approved and authorised for issue by the Board on 13 August 2012.

For and on behalf of the Board

Director

H A Fletcher
Director

KPMG

AMI INSURANCE LIMITED

Statement of Comprehensive Income

for the period Ended 30 June 2012

	Note	2012 *$000*
Premium Revenue		92,334
Less Reinsurance Expense		(19,378)
Net Premium Income		72,956
Less Net Claims Incurred	6	(46,105)
Less Operating Costs	7	(20,630)
Net Underwriting Profit		6,221
Net Investment Income	8	1,221
Net Surplus Before Taxation		7,442
Less Taxation Expense	9	(2,092)
Net Surplus After Taxation		5,350
Other Comprehensive Income net of tax		
Movement in Actuarial Value of Defined Benefit Superannuation Scheme		(1,649)
Business transfer – the difference between consideration paid and net assets	3	(252,399)
Other Comprehensive Loss for the period, net of tax		(254,048)
Total Comprehensive Loss for the period		$(248,698)

AMI INSURANCE LIMITED

Statement of Changes in Equity

for the period Ended 30 June 2012

	Note	Share Capital *$000*	Retained Earnings *$000*	Total Equity *$000*
2012				
Opening Balance		0	0	0
Share Capital issued on 3 April 2012		120,000	0	120,000
Share Capital issued on 5 April 2012		380,000	0	380,000
Share Capital Redeemed 5 April 2012		(120,000)	0	(120,000)
Profit for the Period		0	5,350	5,350
Business transfer – the difference between consideration paid and net assets	3	0	(252,399)	(252,399)
Actuarial movement in defined benefit superannuation scheme		0	(2,290)	(2,290)
Tax Effect of Actuarial movement in defined benefit superannuation scheme	10	0	641	641
Other Comprehensive Loss for the Period		0	(254,048)	(254,048)
Total Comprehensive Loss for the Period		0	(248,698)	(248,698)
Closing Balance 30 June 2012		$380,000	$(248,698)	$131,302

AMI INSURANCE LIMITED

Statement of Financial Position

As at 30 June 2012

	Note	2012 *$000*
SHAREHOLDERS' EQUITY		
Total Shareholders' Equity		$131,302
Represented By:		
ASSETS		
Financial Assets		
Cash and Cash Equivalents	11	135,818
Premium Receivables		113,615
Receivables	12	7,996
Other recoveries on outstanding claims		10,980
Investments	13	124,113
Deferred Reinsurance Expense		76,448
Deferred Acquisition Costs	14	14,444
Deferred Tax Asset	9	349
Plant and Equipment	15	7,302
Intangible Assets	16	18,003
Total Assets		**$509,068**
Less:		
LIABILITIES		
Trade and Other Payables		32,787
Employee Entitlements	19	8,004
Related Party Liabilities		82,970
Unearned Premium Liabilities	20	203,131
Outstanding Claims Liabilities	21	43,234
Defined Benefit Superannuation Scheme	18	7,640
Total Liabilities		**$377,766**
Net Assets		**$131,302**

AMI INSURANCE LIMITED

Statement of Cash Flows

for the period Ended 30 June 2012

	Note	2012 *$000*
CASH FLOWS FROM OPERATING ACTIVITIES		
Premiums Received from Customers		90,696
Interest Received		1,141
Dividends Received		0
Other Investment Income		(72)
Claim Costs		(46,432)
Payments to Suppliers and Employees		(17,577)
Payments For Reinsurance		(586)
Income Tax Paid		0
Net Cash Inflow From Operating Activities	10	**27,170**
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from Issue of Shares on 3 April 2012		120,000
Proceeds from issue of shares pursuant to a Subscription Agreement entered into with IAG (NZ) Holdings Limited on 5 April 2012		380,000
Redemption of initial shares issued		(120,000)
Net Cash Inflow From Financing Activities		**380,000**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase Price Payment for the insurance business of the 'old AMI' (excluding retained claims) net of cash acquired		(142,974)
Payments for Plant and Equipment		(256)
Payments for Intangible Assets		(3,813)
IAG Asset Management Limited Technical Reserves Investment		(130,000)
IAG Asset Management Limited Shareholders Funds Investment		(90,000)
Transfer of IAG Asset Management investments to cash		95,691
Net Cash Outflow From Investing Activities		**(271,352)**
NET INCREASE IN CASH AND CASH EQUIVALENTS		**135,818**
Add Opening Cash and Cash Equivalents		**0**
ENDING CASH AND CASH EQUIVALENTS		**$135,818**

Notes to the Financial Statements

1. SUMMARY OF ACCOUNTING POLICIES

1.1 General Information

AMI Insurance Limited (the Company) is a limited liability company incorporated and domiciled in New Zealand. The Company is a licensed insurer and is therefore deemed an issuer under the Financial Reporting Act 1993.

The Registered office for the Company is located at NZI Centre, 1 Fanshawe Street, Auckland Central, Auckland, 1010.

The Company is wholly owned by IAG (NZ) Holdings Limited. The ultimate parent entity is Insurance Australia Group Limited (IAG), an entity incorporated in Australia. As part of the IAG Group, the Company complies with a variety of policies and procedures developed by IAG for application by all entities in the IAG Group where applicable.

The Company's principal business is fire and general insurance, AMI writes almost exclusively domestic lines of business (private motor, dwelling, contents and pleasure boat) with a small number of commercial policies (farm properties and "light commercial use" motor vehicles).

The financial statements for the Company were authorised for issue by the Directors on 13 August 2012.

2. BASIS OF PREPARATION

2.1 Statement of Compliance

The Company financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP) and also in accordance with the Financial Reporting Act 1993 and the Companies Act 1993. They comply with the New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable financial reporting standards as appropriate for profit oriented companies.

2.2 Basis of Measurement

The financial statements have been prepared on a historical cost basis, except for Financial Assets which have been measured at fair value. All outstanding claims liabilities and reinsurance receivables (if any) have been measured at present value as required by *NZ IFRS 4 Insurance Contracts.*

Accounting policies are selected and applied in a manner that ensures the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

2.3 Presentation Currency

The financial statements are presented in New Zealand dollars and unless specifically stated otherwise are rounded to the nearest thousand dollars.

2.4 Presentation Format

The Company presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within twelve months after the reporting date (current) and more than 12 months after the reporting date (non current) is presented in the notes.

2.5 Changes in accounting policies and comparatives

These financial statements cover the period from 7 December 2011 (the date of the Company's incorporation) and 30 June 2012. As this is the first period of operation for the Company there are no comparative figures.

2.5.1 New NZ IFRS standards and interpretations issued but not yet adopted

At the date of authorisation of these financial statements, certain new standards and interpretations to existing standards have been published but not yet effective, and have not been adopted early by the Company.

Management anticipates that all pronouncements will be adopted in the first accounting period beginning on or after the effective date of the new standard. Information on new standards, amendments and interpretations that are expected to be relevant to the Company financial statements is provided below. Certain other new standards and interpretations issued but not yet effective that are not expected to have a material impact on the Company's financial statements have not been disclosed.

The International Accounting Standards Board (IASB) issued the following accounting standards that will be incorporated into NZ IFRS:

2.5.1.1 Recently issued standards (effective for periods beginning from 1 January 2013)

- *NZ IFRS 13 Fair Value Measurement* replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. It explains how to measure fair value when it is required or permitted by other IFRSs. It does not introduce new requirements to measure assets or liabilities at fair value, nor does it eliminate the practicability exceptions to fair value measurements that currently exist in certain standards.
- *NZ IAS 19 Employee Benefits* the amended IAS 19 includes the following requirements:
  - Actuarial gains and losses are recognised immediately in other comprehensive income; this change will remove the corridor method and eliminate the ability for entities to recognise all changes in the defined benefit obligation and in plan assets in profit or loss, which currently is allowed under IAS 19; and
  - Expected return on plan assets recognised in profit or loss is calculated on the rate used to discount the defined benefit obligation.

2.5.1.2 Recently issued standards (effective for periods beginning from 1 January 2014)

- *NZ IAS 32 Offsetting Financial Assets and Liabilities* are intended to amend IAS 32 to clarify the offsetting criteria and address inconsistencies in their application

2.5.1.3 Recently issued standards (effective for periods beginning from 1 January 2015)

- *NZ IFRS 9 Financial Instruments Classification and Measurement* retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortised cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply. It also adds the requirements related to the classification and measurement of financial liabilities, and derecognition of financial assets and liabilities and includes those paragraphs of IAS 39 dealing with how to measure fair value and accounting for derivatives embedded in a contract that contains a host that is not a financial asset, as well as the requirements of IFRIC 9 Reassessment of Embedded Derivatives.

The full impact of these standards has yet to be assessed by the Company.

3. PURCHASE TRANSACTION

The Company was incorporated on 7 December 2011 under the name of AMI Insurance (Operations) Limited ('new AMI').

On 16 December 2011 a Sale and Purchase agreement (SPA) was entered into between AMI Insurance Limited ('old AMI'), Clic Car Insurance Limited (a 100% owned subsidiary of 'old AMI'), 'new AMI' and IAG (NZ) Holdings Limited, subject to certain conditions being met.

On 5th April 2012 all material conditions under the SPA were met. On that day 'old AMI' restructured its operations and transferred its normal go-forward insurance business to 'new AMI'. 'Old AMI' retained the claims liabilities arising from the 2010/11 Canterbury earthquakes and certain other claims that were subject to reinsurance recoveries. After the business restructuring IAG (NZ) Holdings Limited (IAG) acquired 'new AMI', thereby becoming the sole shareholder of the company and renamed it AMI Insurance Limited (AMI).

The business restructuring did not meet the definition of a 'business combination' stipulated in NZ IFRS 3 *Business Combinations*, therefore business acquisition accounting stipulated in that standard do not apply. The transaction was therefore recognised at book values, with the difference between the consideration paid and net assets being recorded directly to equity. AMI then changed its accounting policies to align them with IAG. This change has been carried out retrospectively in compliance with generally accepted accounting practice.

The details of the sale and purchase transaction are as follows:

- 'New AMI' issued $120 million of share capital to 'old AMI'. 'Old AMI' paid for these shares prior to 5 April 2012.

- 'New AMI' purchased the insurance business (excluding retained claims) for $260 million on 5 April 2012.

- Contemporaneously, new AMI issued $380 million of shares to IAG (NZ) Holdings Ltd and the $120 million share capital held by the 'old AMI' was redeemed. At that time, ownership & control of 'new AMI' changed from 'old AMI' to IAG (NZ) Holdings Ltd.

- 'Old AMI' then changed its name to Southern Response Earthquake Services Ltd (SRESL).

- The Company or 'New AMI' changed its name to AMI Insurance Ltd (previously AMI Insurance (Operations) Ltd).

On completion of the sale, the Company restated the assets & liabilities acquired to align with the accounting policies of the ultimate parent company.

	Adjusted Balance Sheet for acquisition purposes
ASSETS	
Financial Assets	
Cash and Cash Equivalents	237,025
Premium Receivables	106,793
Receivable From SRESL	2,409
Other recoveries on outstanding claims	10,517
Other Receivables	4,180
Deferred Reinsurance Expense	12,241
Deferred Acquisition Costs	14,712
Deferred Taxation	1,800
Plant and Equipment	7,792
Intangible Assets	14,797
Total Assets	412,266
Less:	
LIABILITIES	
Trade and Other Payables	30,182
Employee Entitlements	8,086
Defined Benefit Superannuation Scheme	5,294
Unearned Premium	197,946
Outstanding Claims	43,157
Total Liabilities	284,665
Net Assets	127,601
Difference between consideration paid and net assets	252,399
Total Consideration	380,000

4. SPECIFIC ACCOUNTING POLICIES

4.1 Significant accounting policies related to general insurance contracts

All of the general insurance products on offer, or utilised, meet the definition of an insurance contract (a contract under which one party, the insurer, accepts significant insurance risk from another party, the policyholder, by agreeing to compensate the policyholder if a specified uncertain future event, the insured event, adversely affects the policyholder).

4.1.1 Premium Revenue

Premium revenue comprises amounts charged to policyholders (direct premium) for insurance contracts.

Premium revenue is recognised as earned from the date of attachment of risk (generally the date a contract is agreed to) over the period of the related insurance contracts, in accordance with the pattern of the incidence of risk expected under the contracts. The pattern of the risks underwritten is generally matched by the passing of time. The unearned portion of premium is recognised as an unearned premium liability on the Statement of Financial Position.

4.1.2 Premium Receivables

Premium receivables are recognised on the due date and they are normally settled within one year. The recoverability of premium receivable is assessed and provision is made for impairment based on objective evidence and having regard to past default experience. Premium receivable is presented on the Statement of Financial Position net of GST and any provision for impairment.

4.1.3 Levies and Charges

Levies and charges collected as agent on behalf of the New Zealand Fire Service and Earthquake Commission are not recognised as income or expense in the Statement of Comprehensive Income. The portion held but not yet paid is included in Cash and Cash Equivalents on the Statement of Financial Position and a corresponding amount is included as a liability in Trade and Other Payables.

4.1.4 Liability Adequacy Test

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

The Liability Adequacy test is carried out on a company level, as the Company's insurance portfolio is subject to broadly similar risks and is managed together as a single portfolio

If the present value of the expected future cash flows relating to future claims, plus the additional risk margin to reflect the inherent uncertainty in case estimates, exceeds the unearned premium liability less related intangible assets and related deferred acquisition costs, then the unearned premium liability is deemed to be deficient.

The entire deficiency (if any) is recognised immediately in the Statement of Comprehensive Income, both gross and net of reinsurance. The deficiency is recognised first by writing down any related intangible assets and then related deferred acquisition costs, with any excess being recorded in profit or loss as an unexpired risk liability.

4.1.5 Outwards Reinsurance

Premiums paid to reinsurers under reinsurance contracts held by the Company are recognised as an outwards reinsurance expense in profit or loss 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.

4.1.6 Outstanding Claims Liability

The outstanding claims liability is measured as the central estimate of the present value of expected future payments relating to claims incurred at the reporting date, plus a risk margin.

The expected future payments include those in relation to claims reported but not yet paid; claims incurred but not reported (IBNR); claims incurred but not enough reported (IBNER); and estimated claims handling costs.

To allow for the inherent uncertainty of the central estimate, a risk margin is applied to the outstanding claims liability net of reinsurance and other recoveries. The risk margin increases the probability that the net liability is adequately provided for.

The estimation of the outstanding claims liability involves a number of key assumptions and is the most critical accounting estimate. All reasonable steps are taken to ensure that the information used regarding claims exposures is appropriate. However, given the inherent uncertainty involved in determining the liability, it is likely that the final outcome will be different from the original liability established.

4.1.7 Reinsurance and Other Recoveries

Reinsurance and other recoveries received or receivable on paid claims and on outstanding claims (notified and not yet notified) are recognised as income in net claims incurred. All recoveries receivable on outstanding claims are measured as the present value of the expected future receipts calculated on the same basis as the outstanding claims liability. Reinsurance does not relieve the originating insurer of its liabilities to policyholders and is presented separately on the Statement of Financial Position.

4.1.8 Deferred Acquisition Costs

Acquisition costs incurred in obtaining general insurance contracts are deferred and recognised as assets where they can be reliably measured and where it is probable that they will give rise to premium revenue that will be recognised in profit or loss in subsequent reporting periods.

These costs include advertising expenses, underwriting expenses, commissions paid to agents, premium collection costs, risk assessment costs and other administrative costs.

Deferred acquisition costs at the reporting date represent the capitalised acquisition costs relating to unearned premium. Deferred acquisition costs are amortised systematically in accordance with the expected pattern of the incidence of risk under the general insurance contracts to which they relate. This pattern of amortisation corresponds to the earning pattern of the corresponding premium revenue. Risks under the Company's general insurance contracts cover a period of up to 12 months, therefore, deferred acquisition costs are amortised within 1 year.

4.2 Significant Accounting Policies Applicable to Other Activities

The accounting policies of the Company have been applied consistently in the current reporting period.

4.2.1 Investment Income

The following items are recognised in profit or loss:

- interest is recognised using the effective interest method
- realised gains and losses on investments sold
- unrealised gains and losses on Financial Assets at Fair Value through Profit or Loss (FVTPL), and
- realised and unrealised foreign exchange gains and losses on cash and cash equivalents and investments classified as FVTPL.

4.2.2 Income Tax

The following policies apply to income tax:

4.2.2.1 Current income tax

The current income tax asset or liability for the current and prior periods is measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and laws used to compute this amount are those that are enacted or substantively enacted by the reporting date.

Current tax attributable to amounts recognised directly in equity is also recognised directly in equity.

4.2.2.2 Deferred tax

Deferred tax assets and liabilities are recognised for temporary differences between the tax base of the assets and liabilities and their carrying amount, at the tax rates expected to apply when the assets are recovered or liabilities are settled.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax assets and liabilities are offset only if:

- a legally enforceable right exists to set off current tax assets and liabilities
- the deferred tax assets and liabilities relate to the same taxable entity, and
- the deferred tax assets and liabilities are with the same taxation authority.

Deferred tax balances attributable to amounts recognised directly in equity are also recognised directly in equity.

4.2.3 Goods and Services Tax (GST)

The Statement of Comprehensive Income, Statement of Changes in Equity and the Cash Flow Statement have been prepared so that all components are stated exclusive of GST. All items in the Statement of Financial Position are stated exclusive of GST with the exception of payables which include GST invoiced.

4.2.4 Financial Assets
The following policies apply to financial assets:

4.2.4.1 Financial assets backing general insurance liabilities
As part of its investment strategy the Company actively manages its investment portfolio to ensure that investments mature in accordance with the expected pattern of future cash flows arising from general insurance liabilities.

Financial assets deemed to back general insurance liabilities are designated at Fair Value through Profit or Loss. Initial recognition is at fair value in the Statement of Financial Position and subsequent measurement is at fair value with any resultant unrealised profits and losses recognised in profit or loss.

4.2.4.2 Other financial assets
Financial assets that do not back general insurance liabilities are designated in the manner appropriate to their function. Two designations used by the Company are:

- Trade receivables – These are initially recognised at cost. Subsequent measurement is at amortised cost, and
- Fair Value through Profit or Loss – These are initially recognised at fair value. Subsequent measurements are at fair value, with any unrealised gain or loss recognised through Profit or Loss. These assets are managed at fair value both for external and internal purposes and in accordance with the documented Risk Management Strategy.

Details of fair value for the different types of financial assets are listed below:

- Cash assets are carried at face value of the amounts deposited or drawn. The carrying amounts of cash assets and bank overdrafts approximate their fair value.
- Fixed interest securities are recorded at amounts based on valuations using rates of interest equivalent to the yields obtainable on comparable investments at balance date

All purchases and sales of financial assets that require delivery of the asset within the time frame established by regulation or market convention ('regular way' transactions) are recognised at trade date, being the date on which the Company commits to buy or sell the asset. In cases where the period between trade and settlement exceeds this time frame, the transaction is recognised at settlement date.

4.2.4.3 De-recognition of financial assets
A financial asset is derecognised when the Company has transferred its rights to receive cash flows from the asset, which normally occurs when the asset is sold, or the rights to receive cash flows from the asset have expired.

4.2.5 Derivative Financial Instruments
The Company enters into derivative financial instruments (forward exchange contracts) to manage its exposure to foreign currency risk. These are recorded at fair value at each reporting date. Any resultant gain or loss from the movement in market values is recognised in profit or loss.

4.2.6 Intangible Assets
Intangible assets are initially measured at cost. Subsequent measurement is at cost less accumulated amortisation and impairment. Amortisation is charged on a straight-line basis over the estimated useful life of the intangible asset.

Internally developed software is recognised as an intangible asset when it can be demonstrated that an individually identifiable asset is created. The cost of an internally developed software asset is that directly attributable to the development phase of the software project.

All software assets included in the financial statements have useful lives of between 2 and 10 periods.

Any costs relating to research are recognised as an expense in the period incurred.

4.2.7 Plant and Equipment

Plant and Equipment is initially recorded at cost, including costs that are directly attributable to the acquisition of the asset. Subsequent measurement is at cost less accumulated depreciation. Depreciation is calculated using the straight-line method to allocate their cost, net of any residual value, over their useful lives.

The estimated useful lives of the major asset classes are:

• Office Furniture and Equipment	2 to 15 years
• Motor Vehicles	3 to 5 years

All repairs and maintenance expenditure is charged to profit or loss in the period in which the expense is incurred.

An item of Plant and Equipment is de-recognised when it is disposed of, or when no future economic benefits are expected from its use or disposal. Any gain or loss on de-recognition of the asset is included in profit or loss in the period the asset is de-recognised.

4.2.8 Cash and Cash Equivalents

Cash and cash equivalents includes cash at bank, deposits on call and other short-term, highly liquid investments with original maturities of 90 days or less which are readily convertible to known amounts of cash and are subject to insignificant risk of changes in value.

4.2.9 Foreign Currency

Foreign currency transactions are translated into the functional currency of the Company, using the exchange rates prevailing at the dates of the transactions (spot exchange rate). Foreign exchange gains and losses resulting from the settlement of such transactions and from the re-measurement of monetary items at period-end exchange rates are recognised in profit or loss.

Non-monetary items measured at historical cost are translated using the exchange rates at the date of the transaction (not retranslated). Non-monetary items measured at fair value are translated using the exchange rates at the date when fair value was determined.

4.2.10 Lease Assets

Leases are classified as finance leases whenever the terms of the lease transfer substantially all of the risks and rewards of ownership to the lessee. All other leases are treated as operating leases.

Assets held under finance leases are recognised as Plant and Equipment in the Statement of Financial Position. Leased assets are initially recognised at their fair value, or if lower, the present value of the minimum lease payments.

A corresponding liability is established and each lease payment allocated between the liability and interest expense. Leased assets are depreciated on the same basis as equivalent Plant and Equipment.

The Company leases premises from external parties. Rental payments are recognised as an expense on a straight-line basis over the lease term.

4.2.11 Lease Provision

Certain operating leases for property require that the building be returned to the lessor in its original condition. However, the related operating lease payments do not include an element for this cost. The present value of the estimated future cost for the plant and equipment to be removed and the premises to be returned to the lessor in its original condition are recognised as a lease provision when the relevant alterations are made to the premises. The costs are capitalised as part of the cost of plant and equipment and then depreciated over the useful lives of the assets.

4.2.12 Provisions

A provision is recognised for a liability when the settlement amount or timing is uncertain; when there is a present legal or constructive obligation as a result of a past event; it is probable that expenditures will be required to settle the obligation; and a reliable estimate of the potential settlement can be made. Provisions are not recognised for future operating losses.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation. Provisions are discounted to their present values, where the time value of money is material.

All provisions are reviewed at each reporting date and adjusted to reflect the current best estimate.

4.2.13 Employee Benefits

The following policies apply to employee benefits:

4.2.13.1 Short-term employee benefits

Liabilities for salaries (including non-monetary benefits), annual leave and accumulated sick leave expected to be settled within 12 months of the reporting date are recognised in respect of employee services up to the reporting date. They are measured at the amount expected to be paid when the liabilities are settled.

4.2.13.2 Superannuation scheme

The Company is sponsor to an employee superannuation scheme (the Scheme). The Company contributes in accordance with the Scheme's Trust Deed and actuarial recommendations.

The Scheme has a Defined Contribution Tier and a Defined Benefit Tier.

Contributions to both tiers are expensed as incurred, when relevant employee services have been received.

The asset or liability recognised in the Statement of Financial Position in respect of the Defined Benefit Superannuation Scheme is the present value of the defined benefit obligation at the reporting date, less the fair value of the Scheme's assets as determined by an independent actuary. Actuarial gains and losses are recognised in other comprehensive income.

Management estimates the defined benefit obligation annually with the assistance of independent actuaries. The estimate of its post-retirement benefit obligations is based on standard rates of inflation, medical cost trends and mortality. It also takes into account the Company's specific anticipation of future salary increases. Discount factors are determined close to each period-end by reference to the government bond rate that have terms to maturity approximating to the terms of the related pension liability.

4.2.13.3 Employer Contributions to KiwiSaver

Where employees have elected to join a KiwiSaver Superannuation scheme, the Company complies with all applicable legislation in making employer contributions to these schemes. Obligations for contributions are recognised in profit or loss as they become payable.

4.2.14 Impairment

At each reporting date the carrying amounts of tangible and intangible assets are assessed to determine whether there is any indication that they have suffered an impairment loss. If such indications exist for an asset, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any).

Software under development (not yet available for use) is tested for impairment annually. The Company has no intangible assets with an indefinite useful life.

An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount. Impairment losses directly reduce the carrying amount of assets and are recognised in profit or loss.

The estimated recoverable amount of an asset is the greater of their fair value less costs to sell and value in use. Value in use is determined by estimating future cash flows from the use and ultimate disposal of the asset and discounting to their present value using a pre-tax discount rate that reflects current market rates and risks specific to the asset. For an asset that does not generate largely independent cash flows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

4.2.15 Share Capital
Shares are classified as equity when there is no obligation to transfer cash or other assets to the holder. Transaction costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds.

5. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES
The Company makes estimates and assumptions 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 key areas in which critical estimates and judgements are applied are described below.

5.1 The Ultimate Liability Arising from Claims Made Under Insurance Contracts
Provision is made at the period-end for the estimated cost of claims incurred but not settled at the reporting date, including the cost of claims incurred but not yet reported to the Company.

The estimated ultimate cost of claims includes direct expenses to be incurred in settling claims, gross of the expected value of salvage and other recoveries. The Company takes all reasonable steps to ensure that it has appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

The estimation of claims Incurred But Not Reported (IBNR) is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Company, where more information about the claim event is generally available.

In calculating the estimated ultimate cost of unpaid claims the Company uses an actuarial valuation carried out by an independent actuary. Refer Note 21.

5.2 Defined Benefit Superannuation Scheme
An actuarial calculation is performed by an independent actuary each period to determine the value of the asset or liability to be recognised in the Statement of Financial Position in respect of the defined benefit superannuation scheme. These are based on actuarial assumptions, as set out in Note 18.

5.3 Liability Adequacy Test
The adequacy of the unearned premium liability is assessed at reporting date by the performance of the Liability Adequacy Test (LAT). The LAT is based on prospective information, so is heavily dependent on assumptions and judgement. Refer to Note 20.

6. NET CLAIMS INCURRED

	2012 *$000*
Gross claims expense	48,169
Claim handling expenses	4,380
Other claim recovery revenue	(6,444)
Total Net Claims Incurred	**46,105**

7. OPERATING COSTS

	2012 *$000*
Employee benefit expenses	14,558
Marketing and other acquisition costs	2,058
Depreciation and amortisation	1,252
Lease and property costs	1,990
Communications	887
Legal & professional	1,040
Computer & IT	869
Audit fees	152
Other expenses	2,204
Gross Operating Costs	25,010
Less Claim handling expenses to Claims costs	(4,380)
Net Operating Costs	20,630

8. INVESTMENT INCOME & EXPENSES

	2012 *$000*
Interest income	1,705
Gains/(Losses) on Fair Value Through Profit or Loss investments	(484)
Investment Income	1,221

9. INCOME TAX

9.1 Tax Expense

	2012 *$000*
Current tax expense	-
Deferred tax expense	2,092
Total Tax Expense	2,092
Surplus before tax	7,442
Tax at applicable rate of 28%	2,084
Non-taxable/deductible items	8
Tax Expense	2,092

9.2 Deferred Tax Asset

The balance comprises temporary differences attributable to:	
Plant & equipment	192
Employee provisions and accruals	2,020
Deferred acquisition costs	(4,044)
Defined benefit obligation	2,139
Other	42
Net Deferred Tax Asset	349

Movements:	
Balance on Acquisition	1,800
Charged to the Statement of Comprehensive Income	(2,092)
Charged to other comprehensive income	641
Closing balance at 30 June	349

10. CASH INFLOWS FROM OPERATING ACTIVITIES

	2012 *$000*
Net Realised Surplus After Tax	5,350
Adjustment For Non-cash Items	
Depreciation & Amortisation	1,252
Unrealised (Gains)/Losses	10
Plant & Equipment (Gain)/Loss on Sale	(87)
Adjustment to Actuarial Movement of DB Super Scheme	57
Unrealised Foreign Exchange (Gains)/Losses	402
(Increase)/Decrease in Deferred Acquisition Costs	268
(Increase)/Decrease in Deferred Tax Benefit	1,451
Less Deferred Tax on Movements via Reserve	641
	3,994
Movement In Underwriting Provisions	
Unearned Premium	5,185
Insurance & Reinsurance Receivables	(7,285)
Reinsurance premium Payables	95,280
Deferred Reinsurance Exp	(76,448)
Outstanding Claims	77
	16,809
Movement In Working Capital	
Receivables & Tax	(1,408)
Payables	2,425
	1,017
Net Cash Inflow from Operating Activities	27,170

11. CASH AND CASH EQUIVALENTS

	2012 *$000*
Cash Held for Operational Purposes	40,198
Cash Held for Investment Purposes with IAG Asset Management Limited (IAGAML)	95,620
Total Cash and Cash Equivalents	**135,818**

Cash and cash equivalents represent cash on hand and held with banks, deposits on call and short term money held for investment at maturities of less than or equal to 90 days. Cash balances are available for use in normal operations, except for amounts collected on behalf of the New Zealand Fire Service and Earthquake Commission. Interest rates earned on cash and cash equivalents ranged from 2.5% to 4.0% during the period.

12. RECEIVABLES

	2012 *$000*
Investment Income Receivable	563
Receivable from Southern Response Earthquake Services Limited (SRESL) for professional services	1,803
Balance receivable from SRESL on purchase of insurance business	2,409
Prepayments	3,221
Total Receivables	7,996

13. INVESTMENTS

	2012 *$000*
Fixed interest securities held with IAGAML	124,297
Less, Net balance owing to IAGAML on Derivative hedging positions taken	(184)
Total Investments	124,113

14. DEFERRED ACQUISITION COSTS

	2012 *$000*
Balance on Acquisition	14,712
Acquisition costs incurred and deferred	6,651
Acquisition costs amortised in profit or loss	(6,919)
Closing balance at 30 June	**14,444**

15. PLANT AND EQUIPMENT

	Furniture & Equipment	Leasehold Improvements	Motor Vehicles	Total
	$000	*$000*	*$000*	*$000*
Opening carrying value	**0**	**0**	**0**	**0**
Balance on acquisition	3,567	1,748	2,477	7,792
Additions	205	46	169	420
Disposals – Cost	0	0	(49)	(49)
Disposals Accum. Depn.	0	0	2	2
Current period Depn	(458)	(186)	(219)	(863)
Closing carrying value	**3,314**	**1,608**	**2,380**	**7,302**
Represented by:				
Closing cost or valuation	3,772	1,794	2,597	8,163
Closing accumulated depreciation	(458)	(186)	(217)	(861)
Closing carrying value	**3,314**	**1,608**	**2,380**	**7,302**

16. INTANGIBLE ASSETS

	2012
	$000
Software	
Opening carrying value	0
Balance on acquisition	1,046
Additions	24
Current period amortisation	(389)
Closing carrying value	681
Represented by:	
Closing cost or valuation	1,070
Closing accumulated amortisation	(389)
Closing carrying value	681
Software Under Development	
Balance on acquisition	13,751
Development Expenditure incurred since acquisition	3,571
Software Development carried forward	17,322
Closing Intangible Assets	18,003

Refer Note 26 Capital Commitments.

17. SUPERANNUATION

17.1 AMI Superannuation Scheme

The Company is sponsor to an employee superannuation scheme (the Scheme). Both participating employees and the Company make contributions to the Scheme, typically as a percentage of salary. The Company contributes in accordance with the Scheme's Trust Deed and actuarial recommendations.

Note 18 details the calculation and balance of the Defined Benefit Superannuation Scheme.

	2012
	$000
Total Gross Contributions to the Superannuation Scheme (before withholding tax)	
Contributions to defined contribution plan	211
Contributions to defined benefit plan	447
Total Gross Contributions	**658**

Expected contributions to the AMI Superannuation Scheme for the next financial year are $2.4 million

17.2 KiwiSaver Superannuation Schemes

Where employees have elected to join a KiwiSaver Superannuation scheme, the Company complies with all applicable legislation in making employer contributions to the scheme. Contributions are based on a percentage of the employee's salary.

The Company has no obligations to KiwiSaver schemes other than the payment of contributions and are not exposed to the risks or rewards of the defined contribution arrangements.

	2012
	$000
Total Employer Contributions to KiwiSaver schemes	
Contributions to KiwiSaver	**93**

Expected contributions to the KiwiSaver Scheme for the next financial period are $0.4 million

18. DEFINED BENEFIT SUPERANNUATION SCHEME LIABILITY

The asset or liability recognised in the Statement of Financial Position in respect of the defined benefit superannuation scheme is the present value of the defined benefit obligation at the reporting date, less the fair value of the Scheme's assets. The asset or liability is determined annually by Robert Schoonraad, Fellow of the New Zealand Society of Actuaries, on behalf of Mercer New Zealand Limited.

The reconciliation below shows the obligation and fair value of plan assets for the entire superannuation scheme, however, the net liability of $7.640 million relates to the defined benefit portion only.

18.1 Actuarial Assumptions

The principal actuarial assumptions used in determining the financial position of the plan at 30 June 2012 and at the date the plan was acquired on 5 April 2012 include:

	30 June 2012	5 April 2012
Discount rate (gross)	3.5%	4.2%
Expected rate of return on plan assets supporting pension liabilities	4.5%	4.5%
Expected rate of return on other plan assets	4.5%	5.5%
Expected future salary increases	3.0%	3.0%

18.2 Reconciliation of Movements in the Present Value of Defined Benefit Obligation

	2012 *$000*
Opening balance	0
Acquired through business transfer	(30,587)
Current service cost	(527)
Interest cost	(269)
Contributions by plan participants	(268)
Increase in obligation arising from actuarial valuation	(1,753)
Transfers in	(745)
Benefits paid	147
Closing balance for fair value of defined benefit obligation	**(34,002)**

18.3 Reconciliation of Movements in Fair Value of Assets

Opening balance	0
Acquired through business transfer	27,040
Expected return on plan assets	317
Increase in plan assets arising from actuarial valuation	219
Contributions by Company as employer	441
Contributions by plan participants	268
Transfers in	745
Benefits paid	(147)
Closing balance for fair value of plan assets	**28,883**

18.4 Reporting Date Balances

	2012 *$000*
Defined Benefit Obligation	**(34,002)**
Fair value of Scheme assets	**28,883**
Net Defined Benefit Superannuation Scheme Asset Liability	**(5,119)**
Contribution Tax Liability	**(2,521)**
Total Defined Benefit Superannuation Scheme Liability	**(7,640)**

Expense Recognised in Profit or Loss	
Company Contributions expensed during the period	**527**
Interest Cost	**269**
Expected Return on assets	**-317**
	479

Amounts recognised in comprehensive income	
Reporting date valuation adjustment to Retained Earnings	**2,290**
	2,290

18.5 Plan Assets

The percentage invested in each asset class at 30 June:

	2012
NZ Shares	15%
Global Shares	8%
NZ Fixed Interest	50%
Property	3%
Cash	24%

The expected return on assets assumption is determined by weighting the expected long term return for each asset class by the target allocation of assets to each asset class. The returns for each asset class are net of investment tax and all expenses.

	2012 *$000*
Actual return on plan assets	536

18.6 Sensitivity

A 1% reduction in the discount rate would result in a $3.545 million increase in the present value of the defined benefit obligation. A 1% increase in the discount rate would result in a $3.545 million reduction in the defined benefit obligation.

19. EMPLOYEE ENTITLEMENTS

Employee entitlements expected to be paid within the next 12 months and those expected to be paid after 12 months are set out below.

	2012 *$000*
Employee Entitlements	
Current	6,198
Non-current	1,806
Total Employee Entitlements	8,004

The above employee entitlements include provisions for sick leave, long service leave and retirement. The discount rate used in determining the level of the long service leave and retirement provisions is the 30 June 2012 New Zealand Government Bond rate.

20. UNEARNED PREMIUM LIABILITY

	2012 *$000*
Unearned premiums acquired	197,947
Deferral of premiums on contracts written in the period	85,844
Earning of premiums written in previous periods	(80,660)
Unearned Premium Liability Closing Balance	203,131

The unearned premium liability has been assessed as adequate by a Liability Adequacy Test (LAT), performed by Colin Brigstock of Finity Consulting Pty Limited and reviewed by Christian Barrington of IAG NZ Limited, the Appointed Actuary for the Company.

The LAT has been conducted using the central estimate of the premium liabilities, together with an appropriate margin for uncertainty. The test LAT is based on prospective information, so is heavily dependent on assumptions and judgements.

The risk margin is determined based on an assessment of recent historical experience in relation to the volatility of the insurance margin.

The test has not been applied using the statistical concept of probability of adequacy, hence the risk margin applied for the purposes of the LAT has been determined using a different methodology to that used in the determination of the risk margin for the outstanding claims liability. The probability of adequacy represented by the LAT also differs from the probability of adequacy represented by the outstanding claims liability. The reason for the differences is that the former is essentially an impairment test used only to test the sufficiency of the premium liabilities, whereas the latter is a measurement accounting policy used to determine the carrying value of the outstanding claims liability on the balance sheet.

21. OUTSTANDING CLAIMS LIABILITY:

	2012
	$000
Central estimate of Outstanding claims	34,502
Plus, Risk margin	4,140
Claims handling costs	4,592
Total Reported Outstanding Claims	**43,234**

21.1. Risk Margin

The risk margin is calculated by an actuarial assessment, having regard to the inherent uncertainty of the outstanding claims liability. The risk margin is intended to provide a probability of sufficiency for the outstanding claims liability of 87.5%.

21.2 Claims Development

Claims incurred by the Company are short-tail in nature. Approximately 96% of claims are paid within one period of being reported.

Reconciliation of movement in discounted outstanding claims		2012 *$000*	
	Gross Outstanding Claims	Reinsurance and Other Recoveries	Net Outstanding Claims
Acquired as part of business transfer	43,157	(10,517)	32,640
Current period claims incurred	52,549	(6,444)	46,105
Claims Paid/Recoveries received	(52,508)	6,089	(46,419)
Movement inn discounting	0	(108)	(108)
Movement inn risk margin	36	0	36
Total Reported Outstanding Claims	**43,234**	**(10,980)**	**32,254**

21.3 Actuarial Calculation, Assumptions and Methods

The effective date of the actuarial report on the insurance liabilities is 30 June 2012. The actuarial report was prepared by Colin Brigstock and Karen Cutter (Fellows of the Institute of Actuaries of Australia) of Finity Consulting Pty Limited. Finity Consulting are satisfied with the quality of data provided for the purpose of estimating insurance liabilities. The actuarial report was reviewed by Christian Barrington of IAG NZ Limited, the appointed Actuary for the Company.

In the actuaries' opinion the insurance liabilities have been prepared in accordance with the New Zealand equivalents to International Financial Reporting Standard (*NZ IFRS 4 Insurance Contracts*) and the NZ

Society of Actuaries Professional Standard 4 governing technical liability valuations for general insurance business.

21.4 Key Actuarial Assumptions

The key assumptions used in determining net outstanding claims liabilities for the current financial period are as follows:

	2012
Inflation	Implicit
Discount Rate*	2.5%
Claims Handling Expenses	13.3%
Third Party debtors expenses	19.5%
Risk margin – Outstanding Claims Liabilities	10.6%
Average weighted term to settlement from reporting date	0.41 yrs

* *Applicable to motor non-reinsurance recoveries only*

21.5 Process to Determine Assumptions

21.5.1 Inflation

The actuarial models adopted implicitly allow for any inflationary impact which is likely to affect future claim payments.

21.5.2 Discount rate

Due to the short tail nature of the liabilities, the impact of discounting is not material other than for the motor non-reinsurance recoveries. As such, the gross liabilities are undiscounted. The motor non-reinsurance recoveries have been discounted using risk free zero coupon yields published by the New Zealand Treasury at 30 June 2012 and the payment profile of the underlying recovery payments.

21.5.3 Claims handling expenses

The estimate of outstanding claims liabilities includes allowance for the future cost of administering claims. The allowance (a percentage of gross outstanding claims) is based on analysis of historical claim related expenses.

21.5.4 Risk Margin

The risk margin was determined at a line of business level, allowing for the uncertainty of the outstanding claims estimate for each line of business. Uncertainty was analysed for each portfolio, taking into account:

- past volatility in general insurance claims
- actuarial model and parameter error
- diversification between the lines of business

The risk margin calculated at 30 June 2012 is intended to achieve an 87.5% probability of sufficiency for the outstanding claims liability.

21.5.5 Average weighted term to settlement

Expected payment patterns are used in determining the outstanding claims liability. A decrease in the average term to settlement would imply that claims are being paid sooner than previously.

21.6 Sensitivity Analysis – Impact of Changes in Key Variables

The impact of change in key assumptions on the net outstanding claims liabilities are shown in the table below for the Company. Each change has been calculated in isolation to other changes.

	Movement in Variable	Net Outstanding Claims Impact 2012 *$000*
Discount Rate	+1% p.a.	152
	-1% p.a.	(159)
Claims Handling Expense rate	+1%	379
	-1%	(379)
Risk Margin	+1%	391
	-1%	(391)

22. OVERALL RISK AND CAPITAL MANAGEMENT FRAMEWORK

In preparation for licensing under the RBNZ requirements the company formalised its risk management framework as set out below.

During the period the company has complied with all externally imposed capital requirements.

22.1 Governance framework

The primary objective of the Company's risk management framework is to protect the shareholder from events that hinder the sustainable achievement of financial performance objectives, including failing to exploit opportunities.

The Company's risk management framework recognises the unpredictability of financial markets and seeks to minimise potential adverse effects on financial performance. A key objective of the Company's risk management activities is to ensure sufficient liquidity is maintained at all times to meet obligations, particularly insurance liabilities and also to optimise investment returns.

To help the Board monitor the Company's exposure to all risks (both financial and insurance) an Audit, Risk Management and Compliance Committee meets regularly. This Committee has the responsibility of reviewing the effectiveness of risk management processes and controls. This Committee also approves the Company's risk management policies and meets regularly to approve any commercial, regulatory and organisational requirements of such policies. These policies define the Company's identification of risk and its interpretation, ensure the appropriate quality and diversification of assets, align underwriting and reinsurance strategy to the corporate goals, and specify reporting requirements.

Financial risks are generally monitored and controlled by selecting appropriate assets to back insurance liabilities.

22.2 Capital management objectives, policies and approach

The Company has established the following capital management objectives, policies and approach to managing the risks that affect its capital position:

- to allocate capital efficiently and support the development of business by ensuring that returns on capital employed meet the requirements of its capital providers and of its shareholder
- to retain financial flexibility by maintaining strong liquidity and access to a range of capital markets
- to align the profile of assets and liabilities taking account of risks inherent in the business
- to maintain financial strength to support new business growth and to satisfy the requirements of the policyholders, regulators and stakeholders, and
- to maintain strong credit ratings and healthy capital ratios in order to support its business objectives and maximise shareholder value.

22.3 Approach to capital management

The Company seeks to optimise the structure and sources of capital to ensure that it consistently maximises returns to the shareholder. The Board has delegated the review of this operation to the Asset & Liability Committee.

The Committee is responsible for:

- setting an operating range (including minimum margin) above Minimum Capital requirements of the RBNZ's Prudential Solvency Standard for Non-Life Insurance Businesses
- determining the appropriate level of return on capital to be achieved by the business
- establishing tolerance limits around the Financial Rating
- following adoption of the Annual Business Plan and updated Strategic Plan developing and performing stress test scenarios on the level of capital over a rolling 5 year period to gain a broader understanding of the risks to capital adequacy, and
- reviewing the integrity of the stress testing and developing contingency plans

The primary source of capital used by the Company is shareholder's equity.

22.4 Financial Strength Rating

At reporting date, AMI Insurance Limited had a financial strength rating from A.M. Best Co. of "A-" (Excellent). A.M. Best Co. has confirmed that this rating will be maintained with effect from 5 April 2012.

22.5 Solvency Calculation

Under the conditions of the Company's Licence to carry on insurance business in New Zealand, it is required to maintain minimum solvency capital of at least $3 million and a positive solvency margin calculated under the Reserve Bank of New Zealand's Solvency Standard for Non-Life Insurance Business.

The Solvency Calculation at 30 June 2012 is:

	$000
Total shareholders' funds per financial statements	131,302
Less Required Regulatory Adjustments	
Intangible assets	(21,364)
Deferred Tax Asset	(349)
Provision for expected dividend payment	(3,000)
Actual Solvency Capital (ASC)	**$106,589**
Capital Charges:	
Insurance risk	21,239
Catastrophe risk	10,000
Asset risk	12,470
Reinsurance recovery risk	1,529
Foreign currency	29
Interest rate	6,380
Minimum Solvency Capital (MSC) required	**$51,647**
Solvency margin	**$54,942**
Coverage of ASC to MSC (times covered)	**2.06**

23. INSURANCE CONTRACTS - RISK MANAGEMENT POLICIES AND PROCEDURES

The financial condition and operation of the Company are affected by a number of key risks including insurance risk, interest rate risk and credit risk. Risks associated with financial instruments are detailed in Note 24. The Company's objectives, policies and procedures in respect of managing these risks for insurance contracts are set out in this Note.

23.1 General insurance contracts

The Company principally issue the following types of general insurance contracts: private motor, dwelling, contents and pleasure boat.

For general insurance contracts, the most significant risks arise from weather events and natural disasters.

The above risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas in New Zealand. The variability of risks is improved by careful selection and implementation of underwriting strategies, which are designed to ensure that risks are diversified in terms of type of risk and level of insured benefits. This is largely achieved through diversification across product types and geography. Furthermore, strict claim review policies to assess all new and ongoing claims, regular detailed review of claims handling procedures and frequent investigation of possible fraudulent claims are all policies and procedures put in place to reduce the risk exposure of the Company. The Company further enforces a policy of actively managing and promptly pursuing claims, in order to reduce its exposure to unpredictable future developments that can negatively impact the business. Inflation risk is mitigated by taking expected inflation into account when estimating insurance contract liabilities.

The Company has also limited its exposure by imposing maximum claim amounts on certain contracts as well as the use of reinsurance arrangements in order to limit exposure to catastrophic events.

The purpose of these underwriting and reinsurance strategies is to limit exposure to catastrophes based on the Company's risk appetite. The Board may decide to increase or decrease the maximum tolerances based on market conditions and other factors.

The Company has reinsurance cover of up to $1.4 billion, provided by the captive reinsurer within the IAG Group. The nature and level of catastrophe events in any period cannot be predicted accurately, but can be estimated through the use of predictive models. The Company uses catastrophe risk modelling provided by the IAG Group in assessing catastrophe exposure. Based on this modelling the level of reinsurance obtained is expected to cover a 1 in 1,000 year catastrophe event.

The table below sets out the concentration of general insurance contract liabilities by type of contract:

		2012	
Insurance risk	Gross Liabilities $*000*	Non RI Recoveries $*000*	Net Liabilities $*000*
Motor	20,827	(9,526)	11,302
Contents	9,388	(467)	8,921
House	12,228	(941)	11,287
Boat	613	(42)	572
Farm	177	(5)	172
Total	43,234	(10,980)	32,254

23.2 Objectives in Managing Risks Arising from Insurance Contracts and Policies for Mitigating those Risks
The Company has an objective to manage insurance risk thus reducing the volatility of operating profits. In addition to the inherent uncertainty of insurance risk, which can lead to significant variability in the loss experience, profits from insurance business are affected by market factors, particularly competition and movements in asset values. Short-term variability is, to some extent, a feature of insurance business.

These notes identify the Company's policies and procedures, processes and controls that comprise its risk management and control systems. The systems address all material risks, financial and non-financial, likely to be faced by the Company. The Company has systems in place to ensure compliance with legislative and prudential requirements and that the Board has satisfied itself as to the compliance with the Risk Management Strategy and a Reinsurance Management Strategy.

The Company has adopted the Risk Management Strategy and Reinsurance Management Strategy, as applicable to the wider Group. Key aspects of the processes established to mitigate risks include:

- the maintenance and use of sophisticated management information systems, which provide up-to-date reliable data on the risks to which the business is exposed at any point in time
- actuarial models, using information from the management information systems, are used to calculate premiums and monitor claims patterns. Past experience and statistical methods are used as part of the process
- documented procedures are followed for underwriting and accepting insurance risks
- the Company has a programme of catastrophe and liability reinsurance to protect its insurance operations from high severity losses and catastrophic events, and
- the mix of assets in which the Company invests is driven by the nature and term of the insurance liabilities. The management of assets and liabilities is closely monitored to attempt to match the maturity dates of assets with the expected pattern of claim payments.

23.3 Terms and Conditions of Insurance Business
The terms and conditions attaching to insurance contracts affect the level of insurance risk accepted by the Company. There are no special terms and conditions in any non-standard contracts that have a material impact on the financial statements.

23.4 Concentration of Insurance Risk
The following factors significantly mitigate the Company's exposure to any concentrations of insurance risk:

- the Company's insurance portfolio covers the domestic market only and is predominantly motor vehicle, contents and house products, with short-tailed risks covering periods of up to 12 months duration
- the portfolio is well spread across New Zealand with any concentrations of insurance risk limited to metropolitan areas, and
- the Company maintains comprehensive catastrophe reinsurance cover to limit exposure from any one event.

23.5 Interest Rate Risk associated with Insurance Contracts
The underwriting of general insurance contracts creates exposure to the risk that interest rate movements may materially impact the value of the insurance liabilities. Movements in interest rates should have a minimal impact on the insurance profit due to the Company's policy of investing in assets backing insurance liabilities, principally in fixed interest securities matched to the expected payment pattern of the insurance liabilities.

23.6 Credit Risk associated with Insurance Contracts
Assets arising from insurance contracts are stated in the Statement of Financial Position at the amount that best represents the maximum credit risk exposure at reporting date.

Non-payment of premium results in lapsing or cancellation of the policy, which cancels all credit and insurance risk.

For information regarding the management of credit risk for other financial instruments, refer to Note 24.

24. FINANCIAL INSTRUMENTS - RISK MANAGEMENT POLICIES AND PROCEDURES

24.1 Financial Instrument information and Risk Management

The activities and operations of the Company expose it to financial risks such as insurance risk, interest rate risk, currency risk, liquidity risk and credit risk. The Company's objectives and policies in mitigating insurance risk are discussed in Note 23. Other risks are discussed in this section.

The Company's risk management framework recognises the unpredictability of financial markets and seeks to minimise potential adverse effects on financial performance. The key objective of the Company's financial risk management activities is to ensure sufficient liquidity is maintained at all times to meet obligations, particularly insurance liabilities and also to optimise investment returns for its shareholders.

The Board has delegated the monitoring of the Company's exposure to all risks to the Audit, Risk Management and Compliance Committee. The Committee also has the responsibility of reviewing the effectiveness of management processes and controls.

Financial risks are generally monitored and controlled by selecting appropriate assets to back insurance liabilities.

24.2 Specific Financial Risks involving Financial Instruments other than Insurance Contracts

24.2.1 Currency risk

The Company's principal business transactions are carried out in New Zealand Dollars. The Company's exposure to currency risk arises with respect to the fair value of investments denominated in foreign currencies. Fluctuation of foreign currency exchange rates will alter the returns earned and the fair value of these financial assets.

Currencies impacting on the risk are the Australian Dollar. The Company's exposure to foreign currency risk is $89.9 million, representing 17.5% of total assets. This exposure is fully hedged back to New Zealand Dollars by use of forward exchange contracts, thereby eliminating this currency risk.

24.2.2 Interest rate risk

The Company is exposed to interest rate risk on its short-term investments. Fluctuation in interest rates will alter the fair values of these financial assets.

The Company regularly monitors its exposure to interest rate risk and takes advice on likely trends in interest rates.

At 30 June, had the interest rate moved as shown in the table below, with all other variables held constant, after tax surplus and equity would have been impacted as follows:

	2012 *$000*
Impact on After Tax Surplus and Equity	Incr/(Decr)
NZD increase – 1%	(359)
NZD decrease – 1%	390

24.2.3 Credit Risk

Credit risk is the risk that a counterparty will fail to meet their contractual commitments in full and on time. Financial assets that subject the Company to credit risk principally consist of cash and fixed interest securities and receivables. Cash and fixed interest securities are placed with high quality financial institutions and the amount of credit exposure to any one financial institution is limited.

The maximum exposure to credit risk on receivables at reporting date is the carrying amounts on the statement of financial position.

24.2.4 Counterparty Risk
The Company invests in a number of financial institutions that have banking operations in New Zealand and Australia. At reporting date the Company had invested between 60% and 70% of equity with the ANZ bank which is rated AA with Standard & Poors.

Receivables represent amounts for premium and insurance claim recoveries. The recoverability of premium receivables is assessed and an appropriate provision for impairment is made based on objective evidence, having regard to past default experience.

There are no material financial assets that are past due as at the end of the reporting period but not impaired.

24.2.5 Liquidity Risk
The Company's treasury function review liquidity levels to ensure sufficient funds to cover obligations as they fall due.

Liquidity Table	Net Discounted Outstanding Claims Liability 2012 *$000*	Investments and Receivables 2012 *$000*
Cash and cash equivalents		135,818
Within 1 yr	34,566	245,724
Within 1 to 2 years	(218)	-
Within 2 to 3 years	(639)	-
Within 3 to 4 years	(527)	-
Within 4 to 5 years	(365)	-
Over 5 years	(564)	-
	32,254	381,542

24.2.6 Derivative financial instruments held for hedging purposes
The Company only use derivatives for hedging purposes in order to reduce its exposure to market risks. Only forward foreign exchanges contracts are used. The notional amount of the forward exchange contracts entered into at reporting date is $89.9 million. These all mature within one year.

24.2.7 Fair Value of investment Assets and Liabilities
The Company uses various methods to estimate the fair value of it financial assets. The methods comprise:

Level 1: fair value is calculated using quoted prices on an active market

Level 2: fair value is estimated using inputs other than quoted market prices included in level 1 that are observable for the asset, either directly or indirectly

Level 3: fair value is estimated using inputs for the asset that are not based on observable market data.

The fair value of financial assets as well as the methods used to determine the fair value are summarised in the table below:

	Level 1 *$000*	Level 2 *$000*	Level 3 *$000*	Total *$000*
Fixed interest securities	124,297	-	-	124,297
Derivatives	-	(184)	-	(184)
Total Fair Value Investments	**124,297**	**(184)**	-	**124,113**

24.2.8 Carrying value of Financial Instruments
The following describes the methodologies and assumptions used to determine fair values for those financial instruments.

24.2.8.1 Fixed rate financial instruments
Fixed rate financial assets and liabilities are carried at fair value. For quoted debt issued the fair values are determined based on quoted market prices. For those notes issued where quoted market prices are not available, a discounted cash flow model is used based on a current interest rate yield curve appropriate for the remaining term to maturity and credit spreads.

24.2.8.2 Derivatives
The only derivative products valued using a valuation technique with market observable inputs (Level 2) are forward foreign exchange contracts. These are valued using observable inputs incorporating foreign exchange spot and forward rates.

25. CAPITAL COMMITMENTS

At 30 June 2012, the Company has committed to $21.76 million of software development expenditure relating to the ongoing development of an insurance software package to be implemented in 2013 and 2014. It is planned to spend all of this amount over the next 12 months

26. OPERATING LEASES

Future expenses under non cancellable operating leases:	**2012** *$000*
Not later than 1 year	5,286
Later than 1 period, not later than 2 years	4,069
Later than 2 years, not later than 5 years	6,339
Later than 5 years	183
Total Operating Leases	**15,877**

Premises are leased under normal commercial terms, which include rights of renewal.

27. RELATED PARTY TRANSACTIONS

27.1 Related Party Balances

Related Party	Description	Balance *$000*
IAG (NZ) Holdings Ltd	Trade creditor	3,041
IAG Re Singapore Pte Ltd	Reinsurance creditor	79,929

27.2 Related Party Transactions

Related Party	Description	Transaction *$000*
Insurance Australia Ltd	Unrealised foreign exchange loss on currency contract	184
IAG (NZ) Holdings Ltd	Issue Ordinary shares	380,000
IAG New Zealand Ltd	Contract Works premiums	82

27.3 Remuneration of Key Management Personnel

Key management personnel are those Directors and Executive Managers who have authority and responsibility for planning, directing and controlling the activities of the Group.

Remuneration of Key Management Personnel	2012 *$000*
Short-term employee benefits	1,507
Termination benefits	851
Post-employment benefits and retiring allowances	118
Total Remuneration of Key Management Personnel	**2,476**

27.4 AMI Superannuation Scheme

The Company is sponsor to an employee superannuation scheme (the Scheme). Note 18 details contributions made to the Scheme. In addition to these contributions, the Company meets some of the operating costs of the Scheme, such as audit fees and actuarial valuations. These additional costs totalled $42,250.

28. SHARE CAPITAL

On 7 December 2011 - 100 ordinary shares of $1 each were issued to AMI Insurance Limited on incorporation of the Company.

On 3 April 2012 - 119,999,900 ordinary shares of $1 each were issued to AMI Insurance Limited on the same terms as existing shares

On 5 April 2012 - 380,000,000 ordinary shares of $1 each were issued to IAG (NZ) Holdings Limited on the same terms as existing shares.

On 5 April 2012 - 120,000,000 ordinary shares held by AMI Insurance Limited were repurchased and cancelled.

At 30 June 2012, share capital comprised of 380,000,000 ordinary shares of $1 each. The shares have no par value. All ordinary shares participate equally in both dividends and any surplus remaining on winding up of the Company. All ordinary shares are authorised, issued and fully paid and have the right to one vote.

29. EVENTS AFTER REPORTING DATE

There have been no significant events occurring since balance date requiring disclosure.

KPMG

KPMG

Independent auditor's report

To the shareholder of AMI Insurance Limited

Report on the financial statements

We have audited the accompanying financial statements of AMI Insurance Limited ("the Company") on pages 7 to 37. The financial statements comprise the statement of financial position as at 30 June 2012, the statements of comprehensive income, changes in equity and cash flows for the period from 7 December 2011 to 30 June 2012, and a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

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

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Company financial statements. The procedures selected depend on the auditor's 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 auditor considers internal control relevant to the Company's preparation of the 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 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.

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

Opinion

In our opinion the financial statements on pages 7 to 37:

- comply with generally accepted accounting practice in New Zealand;
- give a true and fair view of the financial position of the Company as at 30 June 2012 and of its financial performance and cash flows for the period then ended.

Report on other legal and regulatory requirements

In accordance with the requirements of sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993, we report that:

- we have obtained all the information and explanations that we have required; and
- in our opinion, proper accounting records have been kept by AMI Insurance Limited as far as appears from our examination of those records.

KPMG

13 August 2012

KPMG Christchurch

AMI Insurance Limited - Section 78 Appointed Actuaries Report as at 30 June 2012

This report has been prepared in accordance with section 78 of the Insurance Prudential Supervision Act 2010 ("Act") and details the review of the actuarial information, as defined in section 77(4), used in the preparation of AMI Insurance Limited's ("AMI") 30 June 2012 financial statements as required under section 77 of the Act ("review"). It states the following:

a. The review was carried out by Christian Barrington, AMI's Appointed Actuary.

b. The Appointed Actuary reviewed the actuarial information and financial statements.

c. The review covers actuarial information in, or used in the preparation of, financial statements. There was no limitation to the review of actuarial information carried out by the Appointed Actuary.

d. The relationships (other than that of actuary) and interests that the actuary has in AMI (or any of its subsidiaries) are as follows:
   (i) None.

e. All the information and explanations required by the Appointed Actuary were provided.

f. In the opinion of the Appointed Actuary and from an actuarial perspective:
   (i) the actuarial information contained in the financial statements has been appropriately included in those statements; and
   (ii) the actuarial information used in the preparation of the financial statements has been used appropriately.

g. In the opinion of the Appointed Actuary AMI is maintaining the solvency margin that applies under a condition imposed under section 21 (2) (b) of the Act at 30 June 2012.

This report has <u>not</u> been prepared in accordance with professional standard 9.1: Communication of Professional Advice of the New Zealand Society of Actuaries. At the date of signing a draft amended version of this professional standard was being circulated for comment. The draft amended standard clarifies the above report as a certification and exempts the actuary from its reporting requirements; but does not exempt the actuary from any other professional obligations, in particular with respect to the preparation of actuarial information.

Signed

C Barrington

Christian Barrington
Appointed Actuary
AMI Insurance Limited
Fellow of the New Zealand Society of Actuaries

Date 12 November 2012