



Registration number: 581 7931

Factory Mutual Insurance Company

New Zealand Branch

Financial Statements
For the year ended 31 December 2019



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Factory Mutual Insurance Company
New Zealand Branch
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Directors' report

The Directors present their report, together with financial statements of Factory Mutual Insurance Company (New Zealand Branch) for the year ended 31 December 2019.

Corporate Information

Factory Mutual Insurance Company, New Zealand Branch ("the Branch") is licensed by the Bank of New Zealand under the Insurance (Prudential Supervision) Act 2010.

The principal activity of the Branch is the underwriting of property insurance risks to large and medium sized clients.

The Branch is a part of Factory Mutual Insurance Company (the "Company"). The Company is incorporated in the United States of America. The registered office of the Company is 270 Central Avenue, Johnston, RI, USA.

Results

The results of the Branch's operations for the year are set out on page 6 and the financial position of the Branch at the end of the year is set out on page 8.

Review of the business

Revenue was \$29,838,492 (2018: \$23,100,528) during the year. The Branch made a post-tax profit/(loss) of \$10,556,693 (2018: (\$808,064)).

Events subsequent to reporting date

Subsequent to end of the financial year, the COVID-19 outbreak was declared a pandemic by the World Health Organization in March 2020.

The outbreak and the response of Governments in dealing with the pandemic is interfering with general activity levels within the community, the economy and the operations of our business. The scale and duration of these developments remain uncertain as at the date of this report.

It is not possible to estimate the impact of the outbreak's near-term and longer effects or Government's varying efforts to combat the outbreak and support businesses. This being the case, we do not consider it practicable to provide a quantitative or qualitative estimate of the potential impact of this outbreak on the Branch at this time.

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The financial statements have been prepared based upon conditions existing at 31 December 2019 and considering those events occurring subsequent to that date, that provide evidence of conditions that existed at the end of the reporting period. As the outbreak of COVID-19 occurred after 31 December 2019, its impact is considered an event that arose after the reporting period and accordingly, no adjustments have been made to financial statements as at 31 December 2019 for the impacts of COVID-19.

Going concern

The Directors have a reasonable expectation that the Branch has adequate resources to continue in existence for the foreseeable future. As such, they continue to adopt the going concern basis in preparing the annual financial statements.

Directors

The names of the Company's Directors in office during the year is as follows:

| <i>Director</i> | <i>Title</i> | <i>Date changed</i> |
|--------------------------|------------------------|------------------------|
| Francis Thomas Connor | Non-Executive Director | |
| Colin Richard Day | Non-Executive Director | (Ceased 11 April 2019) |
| Michel Serge Giannuzzi | Non-Executive Director | |
| Daniel Lee Knotts | Non-Executive Director | |
| Glenn Rodney Landau | Non-Executive Director | |
| Thomas Alan Lawson | Executive Director | |
| John Anderson Luke Jnr | Non-Executive Director | |
| Gracia Catherine Martore | Non-Executive Director | |
| Christine Mary McCarthy | Non-Executive Director | |
| Stuart Blain Parker | Non-Executive Director | |
| Israel Ruiz | Non-Executive Director | |
| David Thomas Walton | Non-Executive Director | |

No Directors had any interest in the shares of the Company during the year.

Insurance of Directors

Insurance is maintained for the Directors in respect of their duties as Directors of the Company.



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Disclosure of information to the auditors

So far as each person who was a Director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware.

Non-audit services

During the year, EY were not engaged to perform any services with respect to the Branch, other than their statutory duties.

On behalf of the board

Thomas Alan Lawson

Director Dated 9 Apr 2020

Gracia Catherine Martore

Director Dated 9 Apr 2020



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Independent auditor's report to the Shareholder of Factory Mutual Insurance Company

Report on the audit of the financial statements

Opinion

We have audited the financial statements of the New Zealand Branch of Factory Mutual Insurance Company (the "company") on pages 8 to 58, which comprise the statement of financial position of the New Zealand Branch of Factory Mutual Insurance Company as at 31 December 2019, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended of the New Zealand Branch of Factory Mutual Insurance Company, and the notes to the financial statements including a summary of significant accounting policies.

In our opinion, the financial statements on pages 8 to 58 present fairly, in all material respects, the financial position of the New Zealand Branch of Factory Mutual Insurance Company as at 31 December 2019 and its financial performance and cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

This report is made solely to the company's shareholder. Our audit has been undertaken so that we might state to the company's shareholders those matters we are required to state to them in an auditor's 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 shareholder, for our audit work, for this report, or for the opinions we have formed.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report.

We are independent of the New Zealand Branch of the company in accordance with Professional and Ethical Standard 1 (revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Other than in our capacity as auditor we have no relationship with, or interest in, the New Zealand Branch of the company.

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the financial statements section of the audit report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial statements.

Valuation of outstanding claims liability

| Why significant | How our audit addressed the key audit matter |
|---|--|
| <p>The estimation of the value of outstanding claims involves significant judgement and is based on an actuarial model of the expected cost of claims incurred on, or prior to, balance date. An external actuary was appointed by the New Zealand branch of the company to assist in assessing the outstanding claims liability. Assumptions included in the model can generally be categorised as either economic assumptions such as inflation and discount rates or non-economic assumptions relating to claims development and cost. Non-economic assumptions are often based on historical data relating to the volume, amount and pattern of claims settlement.</p> <p>Disclosures regarding the outstanding claims liability and the assumptions used in its calculation are included in Note 19 to the financial statements.</p> | <p>Our audit procedures over the valuation of the outstanding claims liability included:</p> <ul style="list-style-type: none"> ▶ Evaluating and testing key controls relating to the claims processes; ▶ On a sample basis validating the costs recorded for claims closed in the year; ▶ On a sample basis checking the claims data used by the appointed actuary to the underlying claims system; ▶ Using our actuarial specialists to review the outstanding claims liability valuation report prepared by the appointed actuary and evaluate the appropriateness of the methodologies and assumptions used in the valuation. Economic assumptions were considered in the context of relevant market rates and non-economic assumptions within the context of historical claims experience; ▶ Evaluating the objectivity and expertise of the appointed actuary; and ▶ Considering the adequacy of disclosures for the outstanding claims liability. |

Emphasis of Matter: Subsequent Events – Impact of the Coronavirus (COVID-19) Outbreak

We draw attention to Note 24 of the financial report which notes the World Health Organisation's declaration of the outbreak of COVID-19 as a global pandemic subsequent to 31 December 2019 and how this has been considered by the Directors in the preparation of the financial report. As set out in Note 24, no adjustments have been made to financial statements as at 31 December 2019 for the impacts of COVID-19. Our opinion is not modified in respect of this matter.

Directors' responsibilities for the financial statements

The directors are responsible, on behalf of the entity, for the preparation and fair presentation of the financial statements in accordance with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

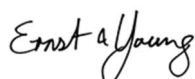
In preparing the financial statements, the directors are responsible for assessing on behalf of the entity the New Zealand Branch of the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the New Zealand Branch of the company or cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (New Zealand) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board website: <https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-2/>. This description forms part of our auditor's report.

The engagement partner on the audit resulting in this independent auditor's report is T M Dring.



Ernst & Young

Melbourne
9 April 2020

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Financial statements

Statement of profit or loss

| | Notes | 2019 \$ | 2018 \$ |
|--|-------|-------------------|-------------------|
| Gross premiums | 6 | 29,838,492 | 23,100,528 |
| Reinsurers share of premiums | 6 | (14,486,791) | (11,147,982) |
| Net premiums | | 15,351,701 | 11,952,546 |
| Gross claims paid | 7 | 4,551,977 | 40,456,938 |
| Reinsurers share of claims paid | 7 | (3,392,639) | (26,936,667) |
| Gross change in provision for outstanding claims | 7 | 610,863 | (34,154,752) |
| Reinsurers share of change in provision for outstanding claims | 7 | (1,856,262) | 29,121,547 |
| Net claims | 7 | (86,061) | 8,487,066 |
| Fees and commission income | 8 | 1,543,379 | 1,369,784 |
| Underwriting expenses | 9 | (6,424,448) | (5,643,328) |
| Underwriting Result | | 10,556,693 | (808,064) |
| Finance costs | | - | - |
| Investment income | | - | - |
| Profit before tax | | 10,556,693 | (808,064) |
| Income tax | 4(p) | - | - |
| Profit after tax | | 10,556,693 | (808,064) |

The accompanying accounting policies and explanatory notes form an integral part of the financial statements.



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Statement of other comprehensive income

| | Notes | 2019 \$ | 2018 \$ |
|---|-------|-------------------|------------------|
| Profit for the year | | 10,556,693 | (808,064) |
| Other comprehensive income to be reclassified to profit or loss in subsequent periods | | - | - |
| Other comprehensive income not to be reclassified to profit or loss in subsequent periods | | - | - |
| Other comprehensive income for the year, net of tax | | - | - |
| Total comprehensive income for the year, net of tax | | 10,556,693 | (808,064) |

The accompanying accounting policies and explanatory notes form an integral part of the financial statements.



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Statement of financial position

| | Notes | 2019 \$ | 2018 \$ |
|--|-------|-------------------|-------------------|
| Assets | | | |
| Cash and cash equivalents | 10 | 34,849,995 | 41,045,455 |
| Insurance receivables | 11 | 5,341,150 | 7,936,384 |
| Other receivables | 12 | 2,107,686 | - |
| Reinsurance assets | 14 | 6,815,576 | 4,822,671 |
| Total assets | | 49,114,407 | 53,804,510 |
| Equity and Liabilities | | | |
| Equity | | | |
| Head Office Account | | 6,000,000 | 6,000,000 |
| Retained earnings | | 8,063,657 | 7,052,422 |
| Total Equity | | 14,063,657 | 13,052,422 |
| Liabilities | | | |
| Trade and other payables | 15 | 206,350 | 9,900,890 |
| Insurance payables | 16 | 4,455,696 | 3,730,144 |
| Contract liabilities | 17 | 111,975 | 148,151 |
| Deferred commission income | 18 | 736,874 | 640,981 |
| Insurance contract liabilities | 19 | 29,539,855 | 26,331,922 |
| Total Liabilities | | 35,050,750 | 40,752,088 |
| Total Head Office Account and Liabilities | | 49,114,407 | 53,804,510 |

The accompanying accounting policies and explanatory notes form an integral part of the financial statements.

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Statement of changes in equity

For the year ended 31 December 2018

| | Head Office Account | Retained earnings | Other capital reserves | Total |
|--|---------------------------|----------------------|------------------------------|-------------------|
| | \$ | \$ | \$ | \$ |
| As at 1 January 2018 | 6,000,000 | 7,860,486 | - | 13,860,486 |
| Profit / (loss) for the year | - | (808,064) | - | (808,064) |
| Other comprehensive income | - | - | - | - |
| Total comprehensive income | 6,000,000 | 7,052,422 | - | 13,052,422 |
| Capital contributions / (repatriations) | - | - | - | - |
| As at 31 December 2018 | 6,000,000 | 7,052,422 | - | 13,052,422 |

For the year ended 31 December 2019

| | Head Office Account | Retained earnings | Other capital reserves | Total |
|--|---------------------------|----------------------|------------------------------|-------------------|
| | \$ | \$ | \$ | \$ |
| As at 1 January 2019 | 6,000,000 | 7,052,422 | - | 13,052,422 |
| Profit / (loss) for the year | - | 10,556,693 | - | 10,556,693 |
| Other comprehensive income | - | - | - | - |
| Total comprehensive income | 6,000,000 | 17,609,115 | - | 23,609,115 |
| Capital contributions / (repatriations) | - | (9,545,458) | - | (9,545,458) |
| As at 31 December 2019 | 6,000,000 | 8,063,657 | - | 14,063,657 |

The accompanying accounting policies and explanatory notes form an integral part of the financial statements.

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Statement of cashflows

| | Notes | 2019 \$ | 2018 \$ |
|---|-------|--------------------|-------------------|
| Operating activities: | | | |
| Profit / (loss) before taxation | | 10,556,693 | (808,064) |
| Adjustments to reconcile profit before tax to net cashflows: | | | |
| Impairments Losses on loans and receivables | | (8,934) | 80,667 |
| Working Capital Adjustments: | | | |
| Decrease/(increase) in Insurance Receivables | | 2,604,169 | (4,323,704) |
| Decrease/(increase) in Other Receivables | | (2,107,686) | - |
| Decrease/(increase) in Reinsurance Assets | | (1,992,905) | 28,003,641 |
| Increase/(decrease) in Trade & other payables | | (9,694,542) | 11,742,272 |
| Increase/(decrease) in Insurance payables | | 725,552 | 920,648 |
| Increase/(decrease) in contract liabilities | | (36,176) | 35,440 |
| Increase/(decrease) in Insurance contract liabilities | | 3,207,934 | (32,010,125) |
| Increase/(decrease) in Deferred commission income | | 95,893 | 65,116 |
| Cash generated from operations | | 3,349,998 | 3,705,891 |
| Interest received | | - | - |
| Net cash flows from/(used in) operating activities | | 3,349,998 | 3,705,891 |
| Investing activities | | | |
| Purchase of plant & equipment | | - | - |
| Net cash flows from/(used in) investing activities | | - | - |
| Financing activities | | | |
| Capital contributions from owner / (repatriations to owner) | | (9,545,458) | - |
| Net cash flows from/(used in) financing activities | | (9,545,458) | - |
| Net increase / (decrease) in cash and cash equivalents | | (6,195,460) | 3,705,891 |
| Cash and cash equivalents at beginning of period | | 41,045,455 | 37,339,564 |
| Cash and cash equivalents at end of period | | 34,849,955 | 41,045,455 |

The accompanying accounting policies and explanatory notes form an integral part of the financial statements.

Notes to the financial statements

Corporate and business information

1. Reporting entity

Factory Mutual Insurance Company, New Zealand Branch (the "Branch") is licensed by the Reserve Bank of New Zealand to carry on general insurance business in and from New Zealand under the Insurance (Prudential Supervision) Act 2010. The Branch was licensed on 1 January 2016.

The registered office of the Branch is :

C/-KPMG Centre
18 Viaduct Harbour Avenue
Auckland NZ 1010

The principal activity of the Branch is the underwriting of property insurance risks to large and medium sized clients.

2. Group information

The Branch is a part of Factory Mutual Insurance Company (the "Company"). The Company is incorporated in the United States of America. The registered office of the Company is 270 Central Avenue, Johnston, RI, USA.

The Company has a financial strength rating of A+ (Superior) issued by A M Best, A+ issued by S&P Global and AA (Very Strong) issued by Fitch Ratings.

3. Segment information

The whole of the Branch is considered to be an operating segment for the purposes of segment reporting.

Significant accounting policies, judgements, estimates & assumptions

4. Significant accounting policies

(a) Basis of preparation

The financial statements have been prepared in accordance with generally accepted accounting practice in New Zealand (NZ GAAP) and the requirements of the Financial Markets Conduct Act 2013.

For the purposes of complying with NZ GAAP the Branch is a for-profit entity.

The financial statements have been prepared on an historical cost basis, except for financial assets that have been initially measured at fair value and, after initial measurement, are measured at amortised cost.

The financial statements are presented in New Zealand Dollars, unless otherwise stated.

The Branch presents its statement of financial position broadly in order of liquidity on the basis that it provides information that is more reliable and relevant for the Branch.

The comparative year amounts have been re-grouped and re-classified wherever necessary in line with current year disclosure presentation.

(b) Product classification

Insurance contracts are those contracts where the Branch (the insurer) has accepted significant insurance risk from another party (the policyholders) by agreeing to compensate the policyholders if a specified uncertain future event (the insured event) adversely affects the policyholders. As a general guideline, the Branch determines whether it has significant insurance risk by comparing benefits paid with benefits payable if the insured event did not occur. Insurance contracts can also transfer financial risks.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period, unless all rights and obligations are extinguished or expire.

(c) Fair value measurement

The Branch measures certain financial instruments and non-financial assets at fair value at each balance sheet date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; OR
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Branch.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming market participants act in their economic best interest.

A fair value measurement of a non-financial asset considers a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Branch uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

(d) Foreign currency translation

The Branch's financial statements are presented in New Zealand Dollars which is also the Branch's functional currency.

Transactions in foreign currencies are initially recorded at the functional currency spot rates at the date the transaction first qualifies for recognition. Insurance revenue and expense transactions are then retranslated at the end of the month in which they are initially recorded using the monthly average rate for that month.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rate of exchange at the reporting date.

Differences arising on settlement or translation of monetary items are recognised in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. The gain or loss arising on translation of non-monetary items measured at fair value is treated in line with the recognition of the gain or loss on the change in fair value of the item (i.e., translation differences on items whose fair value gain or loss is recognised in OCI or profit or loss are also recognised in OCI or profit or loss, respectively).

(e) Revenue recognition

i. Gross premiums

Gross written premiums comprise the total premiums receivable for the whole period of cover provided by contracts entered into during the reporting period. They are recognised on the date on which the policy commences. Premiums include any adjustments arising in the reporting period for premiums receivable in respect of business written in prior accounting periods. Membership credits are deducted from gross premiums.

Unearned premiums are those proportions of premiums written in a year that relate to periods of risk after the reporting date. Unearned premiums are calculated on a pro rata basis. The proportion attributable to subsequent periods is deferred as a provision for unearned premiums.

ii. Reinsurers share of premiums

Reinsurers share of premiums comprise the total premiums payable for the whole cover provided by contracts entered into in the period and are recognised on the date on which the reinsurance policy incepts. Premiums include any adjustments arising in the accounting period in respect of reinsurance contracts incepting in prior accounting periods.

Unearned reinsurance premiums are those proportions of premiums ceded in a year that relate to periods of risk after the reporting date. Unearned reinsurance premiums are deferred over the term of the underlying direct insurance policies for risks-attaching contracts and over the term of the reinsurance contract for losses-occurring contracts, with the exception of the intercompany stop loss

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reinsurance treaty, which is recognised as a period cost for the accounting year in which cover is provided with no unearned premiums recognised at the end of the year.

iii. Fee and commission income

Revenue from contracts with customers

In certain circumstances, insurance policyholders may be separately charged for loss prevention engineering services. These fees are recognised as revenue over the period in which the related services are performed. If fees are for services provided in future periods, then they are deferred and recognised over those future periods.

Reinsurer commission income

In certain circumstances, commission income is received in respect of Reinsurers share of premiums. Commission income is recognised as revenue on the date on which the reinsurance policy incepts. Unearned commission income is deferred and recognised over the term of the related reinsurance policies.

(f) Claims and expense recognition

i. Gross claims expense

Gross claims expense includes all claims occurring during the year, whether reported or not, related to internal and external claims handling costs that are directly related to the processing and settlement of claims, a reduction for the value if salvage and other recoveries, and any adjustments to claims from previous years.

ii. Reinsurers share of claims expense

Reinsurers share of claims expense is recognised when the related gross insurance claim is recognised according to the terms of the relevant contract.

(g) Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash at banks and on hand, which are subject to an insignificant risk of changes in value.

(h) Insurance receivables

Insurance receivables are recognised when due and measured on initial recognition at the fair value of the consideration receivable. Subsequent to initial recognition, insurance receivables are measured at amortised cost, using the Effective Interest Rate ("EIR") method. The carrying value of insurance receivables is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the statement of profit or loss.

Insurance receivables are derecognised when the derecognition criteria for financial assets have been met.

(i) Deferred acquisition expenses (DAC)

Those direct costs incurred during the financial period arising from acquiring or renewing of insurance contracts are deferred to the extent that they are recoverable out of future premiums from insurance contracts. Indirect acquisition costs are recognised as an expense when incurred.

Subsequent to initial recognition, the DAC asset is amortised over twelve months, the period in which the related revenues are earned.

(j) Reinsurance ceded to reinsurance counterparties

The Branch cedes reinsurance risk in the normal course of business. Reinsurance assets represent balances due from reinsurance companies. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claim provision or settled claims associated with the reinsurer's policies and are in accordance with the related reinsurance contract.

Reinsurance assets are reviewed for impairment at each reporting date, or more frequently, when an indication of impairment arises during the reporting period. Impairment occurs when there is objective evidence because of an event that occurred after initial recognition of the reinsurance asset that the Branch may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the Branch will receive from the reinsurer. The impairment loss is recorded in the statement of profit or loss.

Ceded reinsurance arrangements do not relieve the Branch from its obligations to policy holders.

The assets are derecognised when the obligation by the reinsurer to pay expires, is discharged or is cancelled.

(k) Contracts with customers

In certain circumstances, insurance policyholders may be separately charged for loss prevention engineering services.

These fees are recognised as revenue over the period in which the related services are performed. If fees are for services provided in future periods, then they are deferred and recognised over those future periods.

A contract asset is initially recognised for revenue earned from engineering services because the receipt of consideration is conditional on successful completion of the services. Upon completion of the services, the amount recognised as contract assets is reclassified to receivables. Contract assets are subject to impairment assessment.

A receivable is recognised if an amount of consideration that is unconditional is due from the customer (i.e., only the passage of time is required before payment of the consideration is due).

A contract liability is recognised if a payment is received or a payment is due (whichever is earlier) from a customer before the Branch performs the services. Contract liabilities are recognised as revenue when the Branch performs under the contract (i.e., performs the services to the customer).

(l) Insurance contract liabilities

Insurance contract liabilities include the provision for outstanding claims, the provision for unearned premium and the provision for premium deficiency. The provision for outstanding claims is based on the estimated ultimate cost of all claims incurred but not settled at the reporting date, whether reported or not, together with related claims handling costs and a reduction for the expected value of salvage and other recoveries. Delays can be experienced in the notification and settlement of certain types of claims. Therefore, the ultimate cost of these cannot be known with certainty at the reporting date. The liability is calculated at the reporting date using a range of standard actuarial claim projection techniques, based on empirical data and current assumptions that may include a margin for adverse deviation. No provision for equalisation or catastrophe reserves is recognised. The liabilities are derecognised when the obligation to pay a claim expires, is discharged or is cancelled. The liability is discounted for the time value of money.

The provision for unearned premiums represents that portion of premiums received or receivable that relates to risks that have not yet expired at the reporting date. The provision is recognised when contracts are entered into and premiums are charged, and is brought to account as premium income over the term of the contract in accordance with the pattern of insurance service provided under the contract.

At each reporting date, the Branch reviews its unexpired risk and a liability adequacy test which is performed in accordance with NZIFRS accounting requirements to determine whether there is any overall excess of expected claims and deferred acquisition costs over unearned premiums. This calculation uses current estimates of future contractual cash flows after taking account of the investment return expected to arise on assets relating to the relevant insurance technical provisions. If these estimates show that the carrying amount of the unearned premiums (less related deferred acquisition costs) is inadequate, the deficiency is recognised in the statement of profit or loss by setting up a provision for premium deficiency.

(m) Insurance payables

Insurance payables include amounts owing to reinsurers and are recognised when due and measured on initial recognition at fair value of the consideration received less directly attributable transaction costs. Subsequent to initial recognition, they are measured at amortised cost using the EIR method.

(n) Deferred fee and commission income

Initial and other front-ended reinsurance commissions and fees received for rendering future engineering services relating to insurance contracts, are deferred and recognised as revenue when the related services are rendered.

(o) Provisions

i. General

Provisions are recognised when the Branch has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be

required to settle the obligation and a reliable estimate can be made of the amount of the obligation. When the Branch expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognised as a separate asset, but only when the reimbursement is virtually certain. The expense relating to a provision is presented in the statement of profit or loss net of any reimbursement.

If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. When discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

ii. Onerous contracts

If the Branch has a contract that is onerous, the present obligation under the contract is recognised and measured as a provision. However, before a separate provision for an onerous contract is established, the Branch recognises any impairment loss that has occurred on assets dedicated to that contract.

An onerous contract is a contract under which the unavoidable costs (i.e., the costs that the Branch cannot avoid because it has the contract) of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. The cost of fulfilling a contract comprises the costs that relate directly to the contract (i.e., both incremental costs and an allocation of costs directly related to contract activities).

(p) Taxes

The income of the Branch is taxed in Australia as the Branch is classified as non-resident for New Zealand tax purposes and therefore no income tax expense/benefit has been recognised in the financial statements of the New Zealand Branch.

(q) Financial instruments

i. Overview

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

ii. Financial assets

Initial recognition and measurement

Financial assets are recognised when, and only when, the Branch becomes party to the contractual provisions of the instruments.

The Branch's financial assets are classified as loans and receivables. They consist of cash and cash equivalents, insurance receivables and other receivables.

Financial assets are recognised initially at fair value.

Subsequent measurement

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, loans and receivables are measured at amortised cost, less allowance for impairment. Gains and losses are recognised in the statement of profit or loss when the amounts are derecognised or impaired, as well as through the amortisation process.

Derecognition

A financial asset (or, when applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- The rights to receive cash flows from the asset have expired; or
- The Branch has transferred its right to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party; and either:
(a) the Branch has transferred substantially all the risk and rewards of the asset or (b) the Branch has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

On derecognition of a financial asset, the difference between the carrying amount and the sum of the consideration received is recognised in the statement of profit or loss.

Impairment

The Branch assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, there is objective evidence of impairment as a result of one or more events that has occurred since the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

For financial assets carried at amortised cost, the Branch first assesses whether impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Branch determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for assessment of impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

The amount of any impairment loss identified is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future expected credit losses that have not yet been incurred).

The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognised in the statement of profit or loss. Loans and receivables, together with the associated allowance, are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Branch. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to finance costs in the statement of profit or loss.

iii. Financial liabilities

Initial recognition and measurement

Financial liabilities are recognised when, and only when, the Branch become party to the contractual provisions of the instruments.

All financial liabilities are recognised initially at fair value.

The Branch's financial liabilities are classified as payables (comprising trade & other payables, insurance payables and lease liabilities).

Subsequent measurement

After initial recognition, financial liabilities are subsequently measured at amortised cost using the effective interest method, unless the effect of discounting would be immaterial, in which case they are stated at cost. Gains and losses are recognised in profit or loss when liabilities are derecognised, and through the amortisation process.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. On derecognition, the difference between the carrying amounts and the consideration paid is recognised in the statement of profit or loss. When an existing financial liability is replaced by another from the same party on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the statement of profit or loss.

iv. Offsetting financial instruments

Financial assets and financial liabilities are offset, and the net amount is reported in the statement of financial position, if there is a currently enforceable legal right to offset the recognised amounts and

there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

(r) Changes in accounting policy and disclosures

The Branch has not changed any accounting policy during the reporting period.

The Branch has not applied for the first time any standards, interpretations and amendments that became effective during the reporting period.

The Branch has not early adopted any standard, interpretation or amendment that has been issued but is not yet effective.

5. Significant accounting judgements, estimates & assumptions

(a) General

The preparation of the Branch's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures, and the disclosures of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future reporting periods.

Other disclosures relating to the Branch's exposure to risks and uncertainties include:

- Capital management
- Financial risk management and policies
- Sensitivity analysis disclosures

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. The Branch based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising that are beyond the control of the Branch. Such changes are reflected in the assumptions when they occur.

(b) Valuation of insurance contract liabilities

For insurance contracts, estimates have to be made both for the expected ultimate cost of claims reported at the reporting date and for the expected ultimate cost of claims incurred, but not yet reported, at the reporting date ("IBNR").

The ultimate cost of outstanding claims is estimated by using a range of standard actuarial claims projection techniques, such as Chain Ladder and Bornheutter-Ferguson methods.

The main assumption underlying these techniques is that the Branch's past claims development experience can be used to project future claims development and hence ultimate claims costs. As

such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios. Historical claims development is mainly analysed by accident years, but can also be further analysed by significant business lines and claim types. Large claims are usually separately addressed, either by being reserved at the face value of loss adjuster estimates or separately projected in order to reflect their future development. In most cases, no explicit assumptions are made regarding future rates of claims inflation or loss ratios. Instead, the assumptions used are those implicit in the historical claims development data on which the projections are based.

Additional qualitative judgement is used to assess the extent to which past trends may not apply in future, (e.g., to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy features and claims handling procedures) in order to arrive at the estimated ultimate cost of claims that present the likely outcome from the range of possible outcomes, taking account of all the uncertainties involved.

Similar judgements, estimates and assumptions are employed in the assessment of adequacy of provisions for unearned premium.

The carrying value at the reporting date of insurance contract liabilities is \$29,539,855 (Prior Year: \$26,331,922).

(c) Fair value measurement of financial instruments

When the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be measured based on quoted prices in active markets, their fair value is measured using valuation techniques including the discounted cash flow (DCF) model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values. Judgements include considerations of inputs such as liquidity risk, credit risk and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for assets backed securities.

For discounted cash flow analysis, estimated future cash flows and discount rates are based on current market information and rates applicable to financial instruments with similar yields, credit quality and maturity characteristics. Estimated future cash flows are influenced by factors such as economic conditions (including country specific risks), concentrations in specific industries, types of instruments or currencies, market liquidity and financial conditions of counterparties. Discount rates are influenced by risk free interest rates and credit risk.

Changes in assumptions relating to these factors could affect the reported fair value of financial instruments.

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Detailed information on statement of profit or loss and OCI items

6. Net premiums

| | 2019 \$ | 2018 \$ |
|--|---------------------|---------------------|
| Gross premiums written | 31,934,272 | 25,347,595 |
| Change in provision for unearned premium | (2,095,780) | (2,247,067) |
| Gross premiums earned | 29,838,492 | 23,100,528 |
| Reinsurers share of premiums written | (14,623,433) | (12,265,888) |
| Change in reinsurers share of provision for unearned premium | 136,642 | 1,117,906 |
| Reinsurers share of premiums earned | (14,486,791) | (11,147,982) |
| Net premiums | 15,351,701 | 11,952,546 |

7. Net claims expenses

| | 2019 \$ | 2018 \$ |
|---|--------------------|---------------------|
| Claims paid | 4,261,081 | 39,081,409 |
| External loss adjustment expenses | 175,862 | 581,186 |
| Internal loss adjustment expenses | 115,034 | 794,343 |
| Salvage and other recoveries | - | - |
| Gross claims paid | 4,551,977 | 40,456,938 |
| Reinsurers share of claims paid | (2,700,605) | (26,836,359) |
| Reinsurers share of external loss adjustment expenses | (692,034) | (100,308) |
| Reinsurers share of internal loss adjustment expenses | - | - |
| Reinsurers share of claims paid | (3,392,639) | (26,936,667) |
| Gross change in provision for outstanding claims | 610,863 | (34,154,752) |
| Reinsurers share of change in provision for outstanding claims | (1,856,262) | 29,121,547 |
| Net claims | (86,061) | 8,487,066 |



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8. Fees and commission income

| | 2019 \$ | 2018 \$ |
|--|------------------|------------------|
| Engineering fee income | 237,236 | 188,380 |
| Other fee income | - | - |
| Revenue from contracts with customers | 237,236 | 188,380 |
| Commission income received | 1,402,036 | 1,246,520 |
| Change in deferred commission income | (95,893) | (65,116) |
| Commission income | 1,306,143 | 1,181,404 |
| Total Fees and commission income | 1,543,379 | 1,369,784 |

9. Underwriting expenses

| | 2019 \$ | 2018 \$ |
|--|------------------|------------------|
| Premium taxes | 856,950 | 714,540 |
| Commissions paid | 86,373 | 64,665 |
| Change in deferred acquisition costs | - | - |
| Change in unexpired risk liability | 501,290 | (102,440) |
| Net acquisition costs | 1,444,613 | 676,765 |
| Employee benefits expense | - | - |
| Impairment losses on reinsurance assets | - | - |
| Impairment losses on loans and receivables | 8,934 | (80,667) |
| Auditor's Remuneration | 23,173 | 22,863 |
| Other administration expenses | 5,240,076 | 5,840,064 |
| Administration expenses | 5,272,183 | 5,782,260 |
| Loss adjustment expense reclassification | (115,034) | (21,354) |
| Net foreign exchange (gain) / loss | (177,314) | (794,343) |
| Other expenses | (292,348) | (815,697) |
| Total underwriting expenses | 6,424,448 | 5,643,328 |



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Detailed information on statement of financial position items

10. Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise the following at 31 December:

| | 2019 \$ | 2018 \$ |
|---|-------------------|-------------------|
| Cash at banks and on hand | 34,849,995 | 41,045,455 |
| Short-term deposits including demand and term deposits) | - | - |
| Total cash and cash equivalents | 34,849,995 | 41,045,455 |

Where eligible, cash at banks earn interest at floating rates based on daily bank deposit rates.

Short-term deposits may be made for varying periods of between one day and three months, depending on the immediate cash requirements of the Branch, and earn interest at the respective short-term deposit rates.

The carrying amounts disclosed above reasonably approximate fair value at the reporting date.

11. Insurance receivables

| | 2019 \$ | 2018 \$ |
|--|------------------|------------------|
| Due from policyholders and brokers | 4,852,283 | 5,139,770 |
| Less: Allowance for expected credit losses | (62,656) | (53,722) |
| Sub-total | 4,789,627 | 5,086,048 |
| Due from reinsurers – unrelated parties | 551,523 | 6,011,933 |
| Due from reinsurers – related parties | - | (3,161,597) |
| Less: Allowance for expected credit losses | - | - |
| Sub-total | 551,523 | 2,850,336 |
| Total insurance receivables | 5,341,150 | 7,936,384 |

Insurance receivables are non-interest bearing and are generally on terms of 90 days from issue of invoice or inception of the policy, whichever is later.

The carrying amounts disclosed above approximate fair value at the reporting date.



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Set out below is the change in the provision for expected credit losses of insurance receivables, other receivables and contract assets:

| | 2019 \$ | 2018 \$ |
|--------------------------------------|---------------|----------------|
| At 1 January | 53,722 | 134,389 |
| Provision for expected credit losses | 8,934 | (80,667) |
| Write-off | - | - |
| Foreign exchange movement | - | - |
| At 31 December | 62,656 | 53,722 |

12. Other receivables

| | 2019 \$ | 2018 \$ |
|--|------------------|------------|
| Amounts due from Head Office-non-trade | 2,107,686 | - |
| Amounts due from Related parties-non-trade | - | - |
| Miscellaneous other receivables | - | - |
| Less: Allowance for expected credit losses | - | - |
| Total other receivables | 2,107,686 | - |

Other receivables are non-interest bearing and are generally on terms of 90 days.

The carrying amounts disclosed above approximate fair value at the reporting date.

13. Deferred acquisition costs (DAC)

| | 2019 \$ | 2018 \$ |
|-----------------------|------------|------------|
| At 1 January | - | - |
| Expenses deferred | 13,099 | 2,910 |
| Expenses amortised | (13,099) | (2,910) |
| At 31 December | - | - |



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14. Reinsurance assets

| | Note | 2019 \$ | 2018 \$ |
|--|------|------------------|------------------|
| Reinsurers share of provision for outstanding claims | | 2,750,274 | 894,011 |
| Reinsurers share of provision for unearned premium | | 4,065,302 | 3,928,660 |
| Reinsurance assets | | 6,815,576 | 4,822,671 |

15. Trade and other payables

| | 2019 \$ | 2018 \$ |
|---------------------------------------|----------------|------------------|
| Amounts due to related parties | - | 9,443,875 |
| Other sundry creditors | - | - |
| Accrued expenses | 71,393 | 75,256 |
| Goods and services tax (GST) payable | - | - |
| Other payables | 134,957 | 381,759 |
| Total trade and other payables | 206,350 | 9,900,890 |

Trade and other payables are unsecured and non-interest bearing. The balance has not been discounted because the effect of the time value of money is not material. Related party payables are normally settled on 90-day terms. Other payables are normally settled on 30-day terms.

The carrying amounts disclosed above approximate fair value at the reporting date.

16. Insurance payables

| | 2019 \$ | 2018 \$ |
|---------------------------------------|------------------|------------------|
| Due to policyholders and brokers | - | - |
| Due to reinsurers – unrelated parties | 2,720,279 | 2,489,971 |
| Due to reinsurers – related parties | 1,732,090 | 1,237,638 |
| Other | 3,327 | 2,535 |
| Total insurance payables | 4,455,696 | 3,730,144 |



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Insurance payables are unsecured and non-interest bearing. The balance has not been discounted because the effect of the time value of money is not material. Insurance payables to related parties are normally settled on 90-day terms. Insurance payables to third parties typically do not have credit terms and are normally settled within 30 days of being invoiced.

The carrying amounts disclosed above approximate fair value at the reporting date.

17. Liability for contracts with customers

| | 2019 \$ | 2018 \$ |
|---|----------------|----------------|
| Deferred engineering fee income | 111,975 | 148,151 |
| Total liability for contracts with customers | 111,975 | 148,151 |

18. Deferred commission income

| | 2019 \$ | 2018 \$ |
|----------------------------|----------------|----------------|
| At 1 January | 640,981 | 575,865 |
| Commission income deferred | 191,483 | 133,475 |
| Commission income earned | (95,590) | (68,359) |
| At 31 December | 736,874 | 640,981 |

19. Insurance contract liabilities

(a) Gross amount

| | 2019 \$ | 2018 \$ |
|--|-----------------------|-----------------------|
| Provision for outstanding claims | 10,265,704 | 9,654,840 |
| Provision for unearned premiums | 15,870,308 | 13,774,528 |
| Provision for premium deficiency | 3,403,843 | 2,902,554 |
| Insurance contract liabilities | 29,539,855 | 26,331,922 |



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(b) Net amount

i. Overview

For the year ended 31 December 2018

| | Gross insurance contract liabilities \$ | Reinsurance assets \$ | Net insurance contract liabilities \$ |
|---|---|-----------------------------|---|
| Provision for outstanding claims | 9,654,840 | (894,011) | 8,760,829 |
| Provision for unearned premiums | 13,774,528 | (3,928,660) | 9,845,868 |
| Provision for premium deficiency | 2,902,554 | - | 2,902,554 |
| Total insurance contract liabilities | 26,331,922 | (4,822,671) | 21,509,251 |

For the year ended 31 December 2019

| | Gross insurance contract liabilities \$ | Reinsurance assets \$ | Net insurance contract liabilities \$ |
|---|---|-----------------------------|---|
| Provision for outstanding claims | 10,265,704 | (2,750,274) | 7,515,430 |
| Provision for unearned premiums | 15,870,308 | (4,065,302) | 11,805,006 |
| Provision for premium deficiency | 3,403,843 | - | 3,403,843 |
| Total insurance contract liabilities | 29,539,855 | (6,815,576) | 22,724,279 |

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ii. Provision for outstanding claims movement

For the year ended 31 December 2018

| | Gross provision for outstanding claims \$ | Reinsurers share of provision for outstanding claims \$ | Net provision for outstanding claims \$ |
|----------------------------------|---|--|---|
| At 1 January | 43,809,592 | 30,015,558 | 13,794,034 |
| Claims incurred | 4,947,684 | (2,315,490) | 7,263,174 |
| Claims paid during the year | (39,081,409) | (26,836,359) | (12,245,050) |
| Foreign exchange rate adjustment | (21,027) | 30,302 | (51,329) |
| At 31 December | 9,654,840 | 894,011 | 8,760,829 |

For the year ended 31 December 2019

| | Gross provision for outstanding claims \$ | Reinsurers share of provision for outstanding claims \$ | Net provision for outstanding claims \$ |
|----------------------------------|---|--|---|
| At 1 January | 9,654,840 | 894,011 | 8,760,829 |
| Claims incurred | 4,735,769 | 4,667,357 | 68,412 |
| Claims paid during the year | (4,261,081) | (2,700,605) | (1,560,476) |
| Foreign exchange rate adjustment | 136,176 | (110,489) | 246,665 |
| At 31 December | 10,265,704 | 2,750,274 | 7,515,430 |

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iii. Provision for outstanding claims

For the year ended 31 December 2018

| | Gross provision for outstanding claims \$ | Reinsurers share of provision for outstanding claims \$ | Net provision for outstanding claims \$ |
|---|---|--|---|
| Provision for reported claims by policyholders | 5,776,779 | 244,246 | 5,532,533 |
| Provision for claims IBNR/IBNER | 1,484,509 | 459,651 | 1,024,858 |
| Claims administration expenses | 349,650 | - | 349,650 |
| Loss adjustment expenses | 320,803 | 31,346 | 289,457 |
| Provision for outstanding claims – undiscounted | 7,931,741 | 735,243 | 7,196,498 |
| Discount to present value | (181,010) | (17,547) | (163,463) |
| Provision for outstanding claims – discounted | 7,750,731 | 717,696 | 7,033,035 |
| Risk margin | 1,904,109 | 176,315 | 1,727,794 |
| Provision for outstanding claims – discounted, including risk margin | 9,654,840 | 894,011 | 8,760,829 |



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For the year ended 31 December 2019

| | Gross provision for outstanding claims \$ | Reinsurers share of provision for outstanding claims \$ | Net provision for outstanding claims \$ |
|---|---|--|---|
| Provision for reported claims by policyholders | 5,695,777 | 1,552,296 | 4,143,481 |
| Provision for claims IBNR/IBNER | 2,020,567 | 554,449 | 1,466,118 |
| Claims administration expenses | 153,855 | - | 153,855 |
| Loss adjustment expenses | 342,227 | 93,820 | 248,407 |
| Provision for outstanding claims – undiscounted | 8,212,426 | 2,200,565 | 6,011,861 |
| Discount to present value | (74,811) | (20,425) | (54,386) |
| Provision for outstanding claims – discounted | 8,137,615 | 2,180,140 | 5,957,475 |
| Risk margin | 2,128,089 | 570,134 | 1,557,955 |
| Provision for outstanding claims – discounted, including risk margin | 10,265,704 | 2,750,274 | 7,515,430 |



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iv. Provision for unearned premium

For the year ended 31 December 2018

| | Gross provision for unearned premiums \$ | Reinsurers share of provision for unearned premium \$ | Net provision for unearned premium \$ |
|----------------------------------|--|--|---|
| At 1 January | 11,527,461 | 2,810,754 | 8,716,707 |
| Premiums written during the year | 25,347,595 | 12,265,888 | 13,081,707 |
| Premiums earned during the year | (23,100,528) | (11,147,982) | (11,952,546) |
| At 31 December | 13,774,528 | 3,928,660 | 9,845,868 |

For the year ended 31 December 2019

| | Gross provision for unearned premiums \$ | Reinsurers share of provision for unearned premium \$ | Net provision for unearned premium \$ |
|----------------------------------|--|--|---|
| At 1 January | 13,774,528 | 3,928,660 | 9,845,868 |
| Premiums written during the year | 31,934,272 | 14,623,433 | 17,310,839 |
| Premiums earned during the year | (29,838,492) | (14,486,791) | (15,351,701) |
| At 31 December | 15,870,308 | 4,065,302 | 11,805,006 |



Factory Mutual Insurance Company
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For the year ended 31 December 2019

v. Provision for premium deficiency

| | 2019 \$ | 2018 \$ |
|---|--------------------|--------------------|
| Premium Reserve | | |
| Gross provision for unearned premium | 15,870,308 | 13,774,528 |
| Reinsurers share of provision for unearned premium | (4,065,302) | (3,928,660) |
| Net provision for unearned premium | 11,805,006 | 9,845,868 |
| Deferred acquisition costs (DAC) | (33,863) | (20,764) |
| Net provision for unearned premium less DAC | 11,771,143 | 9,825,104 |
| Premium Liability | | |
| Gross central estimate of expected future cash flows for future claims | 13,425,667 | 11,276,086 |
| Reinsurers share of expected future cash flows for future claims | (2,177,863) | (2,167,791) |
| Net central estimate of expected future cash flows for future claims | 11,247,804 | 9,108,295 |
| Risk Margin | 3,927,182 | 3,169,363 |
| Net premium liability, including risk margin | 15,174,986 | 12,727,658 |
| Net Deficiency | (3,403,843) | (2,902,554) |

Risk management and other disclosures

20. Risk management framework

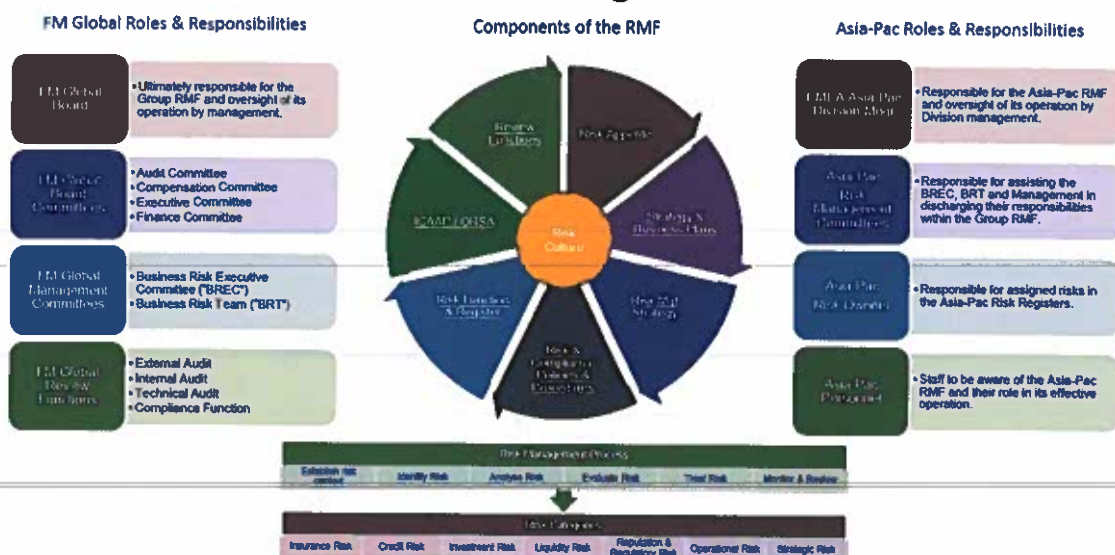
(a) Governance framework

The risk management framework enables FMIC in the Asia-Pacific region, including the Branch, to appropriately develop and implement strategies, policies, procedures and controls to manage different types of material risks. The risk management framework encompasses the systems, structures, policies, processes and people within the operations that identify, measure, monitor, report and control or mitigate all internal and external sources of material risk. Material risks are those that could have a material impact, both financial and non-financial, on operations or the interests of policyholders. The risk management framework provides reasonable assurance that each material risk to operations is being prudently and soundly managed, having regard to the size, business mix and complexity of operations.

The Asia-Pacific risk management framework covers all entities within the region and is summarised in Figure 1 below.

Figure 1

Asia-Pacific Risk Management Framework



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(b) Capital management

The Reserve Bank of New Zealand (RBNZ) is the prudential regulator of the Branch in New Zealand. The RBNZ has exempted the Branch from the need to comply with local solvency requirements described in section 55 of the Insurance (Prudential Supervision) Act 2010, in accordance with section 59 of the Act. These exemptions mean that reliance is placed on the prudential supervision, capital management practices and solvency outcomes of the Company in its home jurisdiction, rather than of the Branch.

The regulatory solvency position of the Company is as follows:

| | 2019 \$'000 | 2018 \$'000 |
|-------------------------------|-------------------|-------------------|
| Actual capital resources | 20,352,867 | 16,745,518 |
| Capital resources requirement | (2,611,964) | (2,536,203) |
| Solvency margin | 17,740,903 | 14,209,315 |
| Solvency ratio | 779% | 660% |

The solvency position reported above is converted from the Company's functional currency of USD to NZD using the spot rate published by the RBNZ as at the reporting date.

(c) Regulatory framework

A key consideration for the prudential regulator is in protecting the rights of policyholders and monitoring the activities of the Branch to ensure that the Branch is satisfactorily managing affairs for their benefit. The prudential regulator is also interested in ensuring an appropriate solvency position is maintained to meet losses arising from economic shocks or natural disasters.

(d) Asset liability management

Financial risks may arise from interest rate and currency exposures. The Branch manages these risks within an asset liability management framework by ensuring that net technical reserves are approximately matched by backing cash and investments.

21. Insurance and financial risks

(a) Insurance risk

i. Overview

The Branch issues only commercial property general insurance contracts. Risks associated with such contracts may vary in relation to the location of the risk, type of risk insured and by industry. Such risks may arise from exposures to fire or natural disasters such as windstorm, flood or earthquake.

The principal risk the Branch faces under insurance contracts is that the actual claims and benefit payments or timing thereof, differ from expectations. This is influenced by the frequency of claims, severity of claims and actual benefits paid. Therefore, an objective of the Branch is to ensure that sufficient reserves are available to cover these liabilities

The risk exposure is mitigated by careful selection and implementation of underwriting guidelines, as well as reinsurance arrangements. A key purpose of these underwriting and reinsurance strategies is to limit exposure to large losses or catastrophe event losses based on the Branch's risk appetite and tolerances. The Branch has a tolerance limit to restrict the impact of large losses or catastrophe event losses such that the combined ratio of the Branch does not exceed 125% in any given year.

Reinsurance includes participation in the Group's worldwide Excess of Loss programme, various automatic facilities, facultative reinsurance, client captive reinsurance and the Branch's intercompany stop loss reinsurance treaty with related party entity Affiliated FM Insurance Company. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts. Although the Branch has reinsurance arrangements, it is not relieved of its direct obligations to its policy holders and thus credit exposure exists with respect to ceded insurance, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements. With the exception of the intercompany stop loss reinsurance treaty, the placement of reinsurance is diversified such that it is not dependent on a single reinsurer.

Risk exposure is also mitigated by claim assessment policies for all new and ongoing claims, regular detailed review of claims handling procedures, active management of claims and prompt settlement of liabilities. Inflation risk is mitigated by taking expected inflation into account when estimating insurance contract liabilities.

ii. Process to determine outstanding claims liabilities

Future cash flows

The estimation of the outstanding claims provision is based on actuarial techniques that analyse experience, trends and other relevant factors. The actuarial claims estimate process commences with the projection of the future payments relating to claims incurred at the reporting date. The expected future payments include those in relation to claims reported but not yet paid or not yet paid in full, claims incurred but not enough reported (IBNER), claims incurred but not reported (IBNR) and the anticipated direct and indirect claims handling costs.

The Branch's claims are characterised by low frequency and high variability in claim size. Accordingly, it is not considered appropriate to rely on aggregate payment patterns to project future claims costs. Instead, estimates are based on analysis of incurred costs, and the performance of estimates, over time.

The different components of the outstanding claims provision are subject to different levels of uncertainty. The estimation of the cost of claims reported but not yet paid or not yet paid in full is made on a case by case basis by claims personnel having regard to the facts and circumstances of the claims as reported, any information available from loss adjusters/consultants and information on the cost of settling based on past experience with the accuracy of initial claims estimates. With IBNR, the estimation is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified, as no information is currently available about the claim. IBNR claims may often not be apparent until some time after the events giving rise to the claim having occurred.

Reserves are not established for catastrophes in advance of such events and so these events may cause volatility in the results for a period and in the level of the outstanding claims provision, subject to the effects of reinsurance recoveries.

The valuation of the outstanding claims provision is performed by the appointed actuary who does not have any role in the pricing function, so as to ensure that an objective and independent assessment of the outstanding claims liability is maintained.

Discounting

A projection of future claims payments both gross and net of reinsurance and other recoveries is undertaken. Projected future claims payments and associated claims handling costs are discounted to a present value as required, using appropriate risk-free discount rates.

Risk Margin

The central estimate of the outstanding claims liability is an estimate which is intended to contain no deliberate or conscious over or under estimation and is commonly described as providing the mean of the distribution. It is considered appropriate for the measurement of the claims liability to represent a higher degree of certainty regarding the sufficiency of the liability over time, and so a risk margin is added to the central estimate. The risk margin refers to the amount by which the liability recognised in the financial statements is greater than the actuarial central estimate of the liability. The risk margin added to the central estimate increases the probability that the net outstanding claims provision will ultimately prove to be adequate to 75%.

Risk margins are held to allow for uncertainty surrounding the outstanding claims provision estimation process. Potential uncertainties include those relating to the actuarial model and assumptions, the quality of the underlying data used in the model, general statistical uncertainty, and the general insurance environment.

iii. Key assumptions

The table below summarises a number of the key assumptions made by the appointed actuary in determining the outstanding claims liability.

| | 2019 % | 2018 % |
|---|-----------|-----------|
| Loss adjustment expenses rate (to net incurred claims) | 4.48% | 4.53% |
| Indirect claim management expenses rate (to gross outstanding claims provision) | 2.01% | 4.94% |
| Inflation rate | 2.47% | 2.67% |
| Discount rate (NZ only) | 0.82% | 1.99% |
| Risk margin rate (NZ only) | 26.20% | 24.57% |

Loss adjustment expenses rate

In respect of claims incurred up to the reporting date, it is known that loss adjustment expenses will be incurred in the management of claims to finalisation. An estimate of these costs is incorporated into the outstanding claims provision using the loss adjustment expense rate. The rate incorporates assumptions about the future costs to be incurred based on past experience of such costs for the business lines adopted from the liability valuation.

Indirect claim management expenses rate

In respect of claims incurred up to the reporting date, it is known that administration costs will be incurred in the management of claims to finalisation. An estimate of these costs is incorporated into the outstanding claims provision using the indirect claim management expenses rate. The rate incorporates assumptions about the future costs to be incurred based on past experience of the cost per transaction.

Inflation rate

Insurance costs are subject to inflationary pressures. Economic inflation assumptions are set by reference to current economic indicators. When making assumptions about the future claim inflation, assumptions have been made around the causative link between the type of claim and the expected growth. Fire claims may be expected, on average, to be driven by construction costs, which in turn may be expected to be driven by some factors that increase with average weekly earnings (AWE) inflation and some that increase with the consumer price index (CPI). Business interruption claims may be expected, on average, to be driven by Company profits for which the most appropriate measure is gross operating surplus (GOS) forecasts. A weighted average of all of these measures has been adopted in determining the inflation rate.

Discount rate

Because the outstanding claims provision represents payments that will be made in the future, they are discounted to reflect the time value of money, effectively recognising that the assets held to back insurance liabilities will earn a return during that period. Discount rates represent a risk free rate derived from market yields on Australian government securities.

Risk margin rate

Due to the short term nature of the provisions, and the level of reinsurance cover, the approach adopted for determining the risk inherent in the provision, involved review of statistical variation in the incremental cost movement of gross incurred costs net of facultative reinsurance recoveries, allowing for additional variation in the Excess of Loss (XoL) reinsurance recoveries, loss adjustment expenses and claims handling costs.

iv. Sensitivities

The claim liabilities are sensitive to the key assumptions in the tables below. It has not been possible to quantify the sensitivity of certain assumptions such as legislative changes or uncertainty in the estimation process. The following analysis is performed for reasonably possible movements in key assumptions with all other assumptions held constant, showing the impact on gross and net liabilities. The correlation of assumptions will have a significant effect in determining the ultimate claims liabilities, but to demonstrate the impact due to changes in assumptions, each assumption has been changed on a stand-alone basis. It should be noted that movements in these assumptions are non-linear. The movements are stated in absolute terms where the base assumption is a percentage, for example, if the base inflation rate assumption was 3.5%, a 1% increase would mean assuming a 4.5% inflation rate. All movements would be recognised directly through the Statement of Profit or Loss.

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Sensitivity of net outstanding claim liabilities for FMIC (NZ) combined to changed assumptions for the year ended 31 December 2018

| Item | Effect |
|--|---|
| Increase discount rate by 0.3% | Reduce outstanding claim liabilities by \$0.030 million (0.3% of outstanding claims central estimates) |
| Increase inflation rate by 2% | Increase outstanding claim liabilities by \$0.188 million (2.1% of outstanding claims central estimates) |
| Increase risk margin by 5% | Increase outstanding claim liabilities by \$0.352 million (4.0% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for FMG to \$2.5 million | Increase outstanding claim liabilities by \$2.513 million (28.7% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for FMG to \$0.015 million | Reduce outstanding claim liabilities by \$0.613 million (7.0% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for AFM to \$1 million | Increase outstanding claim liabilities by \$0.765 million (8.7% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for AFM to \$0.05 million | Reduce outstanding claim liabilities by \$0.419 million (4.8% of outstanding claims central estimates) |
| Approximate impact of a 25% adverse movement in exchange rates (approx 15% claims impacted) | Increase outstanding claim liabilities by \$0.329 million (3.8% of outstanding claims central estimates) |

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Sensitivity of net outstanding claim liabilities for FMIC (NZ) combined to changed assumptions for the year ended 31 December 2019

| Item | Effect |
|--|---|
| Increase discount rate by 0.3% | Reduce outstanding claim liabilities by \$0.025 million (0.3% of outstanding claims central estimates) |
| Increase inflation rate by 2% | Increase outstanding claim liabilities by \$0.173 million (2.3% of outstanding claims central estimates) |
| Increase risk margin by 5% | Increase outstanding claim liabilities by \$0.298 million (4.0% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for FMG to \$2.5 million | Increase outstanding claim liabilities by \$2.365 million (31.5% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for FMG to \$0.015 million | Reduce outstanding claim liabilities by \$0.764 million (10.2% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for AFM to \$1 million | Increase outstanding claim liabilities by \$0.805 million (10.7% of outstanding claims central estimates) |
| Change incremental incurred cost movement for development quarter 2 for AFM to \$0.05 million | Reduce outstanding claim liabilities by \$0.389 million (5.2% of outstanding claims central estimates) |
| Approximate impact of a 25% adverse movement in exchange rates (approx 15% claims impacted) | Increase outstanding claim liabilities by \$0.489 million (6.5% of outstanding claims central estimates) |

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Sensitivity of FMIC (NZ) net premium liabilities to changed assumptions for the year ended 31 December 2018

| Item | Effect |
|--------------------------------------|--|
| Increase discount rate by 0.3% | Reduce premium liabilities by \$0.038 million (0.3% of premium liability central estimates) |
| Increase inflation rate by 2% | Increase premium liabilities by \$0.251 million (2.0% of premium liability central estimates) |
| Increase risk margin by 10% | Increase premium liabilities by \$0.911 million (7.2% of premium liability central estimates) |
| Increase adopted loss ratios to 120% | Increase premium liabilities by \$6.400 million (50.3% of premium liability central estimates) |
| Decrease adopted loss ratios to 20% | Reduce premium liabilities by \$6.514 million (51.2% of premium liability central estimates) |

Sensitivity of FMIC (NZ) net premium liabilities to changed assumptions for the year ended 31 December 2019

| Item | Effect |
|--------------------------------------|--|
| Increase discount rate by 0.3% | Reduce premium liabilities by \$0.047 million (0.3% of premium liability central estimates) |
| Increase inflation rate by 2% | Increase premium liabilities by \$0.309 million (2.0% of premium liability central estimates) |
| Increase risk margin by 10% | Increase premium liabilities by \$1.125 million (7.4% of premium liability central estimates) |
| Increase adopted loss ratios to 120% | Increase premium liabilities by \$7.856 million (51.8% of premium liability central estimates) |
| Decrease adopted loss ratios to 20% | Reduce premium liabilities by \$7.470 million (49.2% of premium liability central estimates) |

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v. Claims development table

The following tables show the estimates of cumulative incurred claims, including both claims notified and IBNR for each successive accident year at each reporting date, together with cumulative payments to date.

Gross provision for outstanding claims for the year ended 31 December 2019

| | Before 2015 | 2015 | 2016 | 2017 | 2018 | 2019 | Total |
|---|----------------|--------|--------|--------|--------|--------|----------|
| Accident year | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 |
| At end of accident year | - | - | 63,402 | 4,682 | 9,436 | 5,616 | |
| One year later | - | - | 60,199 | 5,809 | 8,194 | | |
| Two years later | - | - | 61,754 | 5,807 | | | |
| Three years later | - | - | 62,099 | | | | |
| Current estimate of cumulative ultimate claims incurred | - | - | 62,099 | 5,807 | 8,194 | 5,616 | 81,716 |
| Cumulative payments to date | - | - | 62,099 | 5,807 | 5,859 | 235 | 74,000 |
| Gross provision for outstanding claims at 31 December | - | - | - | - | 2,335 | 5,381 | 7,716 |
| Total gross provision for outstanding claims per the statement of financial position | | | | | | | 10,266 |
| Current estimate of surplus / (deficiency) | | | | | | | (2,550) |
| % Surplus / (deficiency) of initial gross reserve | | | | | | | (24.84%) |

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Net provision for outstanding claims for the year ended 31 December 2019

| | Before 2015 | 2015 | 2016 | 2017 | 2018 | 2019 | Total |
|---|----------------|--------|--------|--------|--------|--------|---------|
| | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 |
| Accident year | | | | | | | |
| At end of accident year | - | - | 16,975 | 3,146 | 7,998 | 4,568 | |
| One year later | - | - | 13,728 | 2,853 | 3,863 | | |
| Two years later | - | - | 15,154 | 2,850 | | | |
| Three years later | - | - | 15,336 | | | | |
| Current estimate of cumulative ultimate claims incurred | - | - | 15,336 | 2,850 | 3,863 | 4,568 | 26,618 |
| Cumulative payments to date | - | - | 15,336 | 2,850 | 2,653 | 168 | 21,008 |
| Net provision for outstanding claims at 31 December | - | - | - | - | 1,210 | 4,400 | 5,610 |
| Total gross provision for outstanding claims per the statement of financial position | | | | | | | 7,515 |
| Current estimate of surplus / (deficiency) | | | | | | | (1,905) |
| % Surplus / (deficiency) of initial net reserve | | | | | | | (25.4%) |

(b) Financial risk

i. Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The Branch is primarily exposed to credit risk via premium receivables from policy holders, reinsurance receivables from reinsurers, receivables due from related parties and deposit accounts with financial institutions.

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Various policies and procedures are in place to prevent, minimise or mitigate exposure to credit risk, including:

- Premium receivables ageing analysis is performed regularly with overdue premiums actively pursued; and
- Reinsurance is placed with counterparties that have good credit rating and concentration of risk is avoided by following guidelines in respect of counterparty limits that are set and reviewed annually by the reinsurance committee. Reinsurance placed with client captive reinsurers, which are unrated, is subject to policy clause conditions that prevent settlement of a claim by the Branch until the client captive reinsurer has settled its share of the loss to the Branch. Reinsurance placed with related party reinsurer Affiliated FM Insurance Company, which enjoys the same rating of the parent, may give rise to concentration of risk from time to time in the event the stop loss attachment point is reached; and
- Deposit accounts are all held with highly rated financial institutions.

The tables below provide information regarding the credit risk exposure of the Branch by classifying financial assets by counterparty rating as published by rating agency Fitch. All amounts are shown before any allowance for impairment.

For the year ended 31 December 2018

| | AA \$ | AA- \$ | BBB \$ | BB \$ | Not rated \$ | Total \$ |
|---------------------------|----------------|-------------------|------------------|----------------|-----------------|-------------------|
| Cash and cash equivalents | - | 41,045,455 | - | - | - | 41,045,455 |
| Insurance receivables | (2,726) | 2,373,601 | 2,243,655 | 171,729 | 299,789 | 5,086,048 |
| Reinsurance receivables | - | 2,385,381 | - | 464,955 | - | 2,850,336 |
| Other receivables | - | - | - | - | - | - |
| Total | (2,726) | 45,804,437 | 2,243,655 | 636,684 | 299,789 | 48,981,839 |



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| | AA \$ | AA- \$ | BBB \$ | BB \$ | Not rated \$ | Total \$ |
|---------------------------|------------------|-------------------|------------------|---------------|-----------------|-------------------|
| Cash and cash equivalents | - | 34,849,995 | - | - | - | 34,849,995 |
| Insurance receivables | - | 1,513,053 | 3,140,672 | - | 135,902 | 4,789,627 |
| Reinsurance receivables | - | 515,231 | 6,356 | 29,936 | - | 551,523 |
| Other receivables | 2,107,686 | - | - | - | - | 2,107,686 |
| Total | 2,107,686 | 36,878,279 | 3,147,028 | 29,936 | 135,902 | 42,298,831 |

The tables below provide information regarding the credit risk exposure of the Branch by classifying financial assets for each material counterparty. All amounts are shown before any allowance for impairment.

For the year ended 31 December 2018

| | HSBC \$ | Bank of America \$ | ANZ \$ | FMIC US \$ | All others \$ | Total \$ |
|---------------------------|-------------------|-----------------------|-----------|--------------------|-------------------|-------------------|
| Cash and cash equivalents | 41,045,455 | - | - | - | - | 41,045,455 |
| Insurance receivables | - | - | - | - | 5,086,048 | 5,086,048 |
| Reinsurance receivables | - | - | - | (4,379,477) | 7,229,813 | 2,850,336 |
| Other receivables | - | - | - | - | - | - |
| Total | 41,045,455 | - | - | (4,379,477) | 12,315,861 | 48,981,839 |



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| | HSBC | Bank of America | ANZ | FMIC US | All others | Total |
|---------------------------|-------------------|-----------------|----------|------------------|------------------|-------------------|
| | \$ | \$ | \$ | \$ | \$ | \$ |
| Cash and cash equivalents | 34,849,995 | - | - | - | - | 34,849,995 |
| Insurance receivables | - | - | - | - | 4,789,627 | 4,789,627 |
| Reinsurance receivables | - | - | - | 6,356 | 545,167 | 551,523 |
| Other receivables | - | - | - | 2,107,686 | - | 2,107,686 |
| Total | 34,849,995 | - | - | 2,114,042 | 5,334,794 | 42,298,831 |

The tables below provide information regarding the credit risk exposure of the Branch by classifying receivables by age. All amounts are shown before any allowance for impairment.

For the year ended 31 December 2018

| | < 90 days | 90 – 180 days | >180 days | Not measured | Total |
|-------------------------|------------------|----------------|----------------|--------------|------------------|
| | \$ | \$ | \$ | | \$ |
| Insurance receivables | 4,722,658 | 313,408 | 49,982 | - | 5,086,048 |
| Reinsurance receivables | 2,443,159 | - | 407,177 | - | 2,850,336 |
| Other receivables | - | - | - | - | - |
| Total | 7,165,817 | 313,408 | 457,159 | - | 7,936,384 |

For the year ended 31 December 2019

| | < 90 days | 90 – 180 days | >180 days | Not measured | Total |
|-------------------------|------------------|----------------|----------------|--------------|------------------|
| | \$ | \$ | \$ | \$ | \$ |
| Insurance receivables | 4,515,586 | 209,693 | 64,348 | - | 4,789,627 |
| Reinsurance receivables | (131,576) | - | 683,099 | - | 551,523 |
| Other receivables | 2,107,686 | - | - | - | 2,107,686 |
| Total | 6,491,696 | 209,693 | 747,447 | - | 7,448,836 |

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The table below provides information regarding impairment allowances for insurance receivables and reinsurance receivables. No collateral is held as security for any insurance or reinsurance receivable balances.

| | 2019 \$ | 2018 \$ |
|-----------------------|---------------|----------------|
| At 1 January | 53,722 | 134,389 |
| Charge for the year | 8,934 | (80,667) |
| Amounts recovered | - | - |
| Amounts written off | - | - |
| At 31 December | 62,656 | 53,722 |

ii. Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. In respect of catastrophe claim events there is also a liquidity risk associated with the timing differences between gross cash outflows and expected reinsurance recoveries.

Various policies and procedures are in place to prevent, minimise or mitigate exposure to liquidity risk, including:

- An Asia-Pacific region liquidity risk policy. The policy includes guidelines for asset allocations and maturity profiles of assets. The policy is reviewed annually for relevance and changes in the risk environment. The policy is approved by the Risk Management Committee (RMC) and forms part of the Risk Management Framework of the region. Any liquidity risk breaches are reported to the RMC;
- The intercompany stop loss reinsurance treaty with Affiliated FM Insurance Company provides for quarterly (or more frequent) settlement in the event the combined ratio of the Branch exceeds the attachment point of 125%; and
- Contingency funding plans are in place, including access to the capital of the Company.

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| | Up to a year \$ | Total \$ |
|---------------------------|--------------------|-------------------|
| Assets | | |
| Cash and cash equivalents | 34,849,995 | 34,849,995 |
| Insurance receivables | 4,789,627 | 4,789,627 |
| Reinsurance receivables | 551,523 | 551,523 |
| | <u>40,191,145</u> | <u>40,191,145</u> |
| Liabilities | | |
| Trade and other payables | 206,350 | 206,350 |
| Insurance payables | 4,455,696 | 4,455,696 |
| | <u>4,662,046</u> | <u>4,662,046</u> |

Insurance contract liabilities and related reinsurance assets are excluded from the above analysis. Due to the nature of insurance risks assumed by the Branch, management does not believe that it is practicable to estimate reliably the timing of the future cash flows arising from these liabilities and assets. The inherent liquidity risk assumed by the Branch in this respect is mitigated by the Branch and its ability to obtain cash advance, if necessary, from its Head Office and reinsurers.

iii. Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and price risk.

Various policies and procedures are in place to prevent, minimize or mitigate exposure to market risk, including an Asia-Pacific region market and investment risk policy. The policy is reviewed annually for relevance and changes in the risk environment. The policy is approved by the RMC and forms part of the Risk Management Framework of the region. Any market risk breaches are reported to the RMC.

Currency risk

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Branch's principal transactions are carried out in New Zealand Dollar and its exposure to foreign exchange risk arise primarily with respect to the US dollar.

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In order to ensure that assets and liabilities are highly correlated with changes in currency movements, deposits with financial institutions that match technical provisions shall generally be held in the typical currency profile of the Branch's technical provisions, except where required to match specific short-term liabilities in another currency. Deposits held in excess of those required to match technical provisions may be converted into US dollars in order to limit the currency risk of the FM Global group. In doing so, it is acknowledged that the Branch may therefore be exposed to residual currency risk at a local level. This risk is tolerated subject to the ongoing requirement to ensure adequate regulatory solvency levels are maintained. The Branch does not use derivatives, hedging or other financial transactions to reduce this residual currency risk exposure at a local level.

The tables below provide information regarding the currency risk exposure of the Branch by classifying the Branch's assets and liabilities by major currencies. All amounts are unhedged. All amounts have been converted to New Zealand Dollar at the rate of exchange prevailing for the financial year ended.

For the year ended 31 December 2018

| | NZD \$ | USD \$ | Other \$ | Total (NZD) \$ |
|------------------------------|-------------------|------------------|-------------------|-------------------|
| Assets | | | | |
| Deferred tax assets | - | - | - | - |
| Plant & Equipment | - | - | - | - |
| Reinsurance assets | 3,795,001 | 814,711 | 212,959 | 4,822,671 |
| Current tax assets | - | - | - | - |
| Deferred reinsurance expense | - | - | - | - |
| Insurance receivables | 7,117,296 | 1,025,953 | (206,865) | 7,936,384 |
| Other receivables | - | - | - | - |
| Accrued income | - | - | - | - |
| Prepaid Expenses | - | - | - | - |
| Cash and short-term deposits | 21,630,438 | 8,016,237 | 11,398,780 | 41,045,455 |
| Total assets | 32,542,735 | 9,856,901 | 11,404,874 | 53,804,510 |

| | | | | |
|------------------------------------|-------------------|------------------|-------------------|-------------------|
| Liabilities | | | | |
| Deferred tax liabilities | - | - | - | - |
| Insurance Contract Liabilities | 23,522,073 | 1,693,664 | 1,116,185 | 26,331,922 |
| Deferred fee and commission income | 544,014 | 45,692 | 51,275 | 640,981 |
| Current tax liabilities | - | - | - | - |
| Insurance payables | 2,877,385 | 727,901 | 124,858 | 3,730,144 |
| Trade and other payables | 282,381 | 160,537 | 9,457,972 | 9,900,890 |
| Contract Liabilities | 96,764 | 20,058 | 31,329 | 148,151 |
| Total liabilities | 27,322,617 | 2,647,852 | 10,981,619 | 40,952,088 |

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| | NZD \$ | USD \$ | Other \$ | Total (NZD) \$ |
|------------------------------------|-------------------|-------------------|------------------|-------------------|
| Assets | | | | |
| Reinsurance assets | 4,478,785 | 1,952,147 | 384,644 | 6,815,576 |
| Insurance receivables | 3,200,534 | 1,198,014 | 942,603 | 5,341,151 |
| Other receivables | (26,581) | 583,545 | 1,550,721 | 2,107,685 |
| Cash and short-term deposits | 24,954,195 | 8,590,329 | 1,305,471 | 34,849,995 |
| Total assets | 32,606,933 | 12,324,035 | 4,183,439 | 49,114,407 |
| Liabilities | | | | |
| Insurance Contract Liabilities | 22,950,849 | 3,373,839 | 3,215,167 | 29,539,855 |
| Deferred fee and commission income | 537,107 | 116,225 | 83,542 | 736,874 |
| Insurance payables | 3,543,819 | 687,986 | 223,891 | 4,455,696 |
| Trade and other payables | 68,119 | 69,914 | 68,317 | 206,350 |
| Contract Liabilities | 82,017 | 19,085 | 10,873 | 111,975 |
| Total liabilities | 27,181,911 | 4,267,049 | 3,601,790 | 35,050,750 |

The table below demonstrates the Branch's sensitivity to reasonably possible movements in the exchange rate for USD to the functional currency of the Branch, showing the impact on profit before tax, with all other variables held constant.

| Currency | Change in ROE % | 2019 \$ | 2018 \$ |
|----------|-----------------------|------------|------------|
| USD | + 10% | (805,699) | (720,905) |
| USD | - 10% | 732,453 | 655,368 |

Interest rate risk

Interest rate risk is the risk that the fair value or future cashflows of a financial instrument will fluctuate because of changes in market interest rates. In order to ensure that assets and liabilities are highly correlated with changes in interest rate movements, deposits with financial institutions that match technical provisions shall generally be held in at call or short duration term deposits (of no more than twelve months duration), broadly consistent with the short tail settlement profile of the Branch's technical provisions.

Equity price risk

Equity price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in Equity prices (other than those arising from interest rate or foreign exchange rate risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or by factors affecting all similar financial instruments traded in the market. The Branch may not hold equities, thus avoiding Equity price risk. The Branch does not hold any financial assets and liabilities whose value fluctuate as a result of changes in market prices.

(c) Operational risks

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications or can lead to financial loss. The Branch cannot expect to eliminate all operational risks, but by maintaining a rigorous risk management and control framework and by monitoring and responding to potential risks, the Branch is able to effectively manage those risks. Controls include segregation of duties, access controls, authorisation and reconciliation procedures, staff training and assessment processes, including the use of internal audit. Business risks such as changes in environment, technology and the industry are monitored through the Branch's risk register.

22. Contingencies and commitments

(a) Legal proceedings and regulations

The Branch operates in the insurance industry and may be subject to legal proceedings in the normal course of business. There are no current contingencies associated with legal proceedings.

The Branch is also subject to Insurance solvency regulations with the prudential regulator. There are no current contingencies associated with the Branch's compliance or lack of compliance with such regulations.

(b) Commitments

The Branch has no capital commitments at the reporting date.

The Branch has no lease commitments relating to lease contracts that have not yet commenced as at year-end

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(c) Guarantees

The Branch has no guarantees at the reporting date.

(d) Contingent liabilities

The Branch has no contingent liabilities at the reporting date.

23. Related party disclosures

(a) Transactions with related parties

The Branch enters into transactions with related party entities in the normal course of business. Transactions with related parties are made on terms agreed between the parties.

Details of transactions carried out during the year with related parties are, as follows:

| | | 2019 \$ | 2018 \$ |
|--|----------------------------------|-------------------|-------------------|
| Income from related parties: | | | |
| Reinsurance recoveries | AFFILIATED FM INS. CO. | - | - |
| | RISK ENGINEERING INSURANCE | - | - |
| | COMPANY LTD. | - | - |
| | NEW PROVIDENT MUTUAL LTD. | - | - |
| Sub-Total Reinsurance recoveries | | - | - |
| Intercompany expense recoveries | FACTORY MUTUAL INSURANCE COMPANY | - | - |
| | Other related parties | - | - |
| Sub-Total Intercompany expense recoveries | | - | - |
| Total income | | - | - |
| Expenses to related parties: | | | |
| Reinsurance premiums | AFFILIATED FM INS. CO. | 4,331,139 | 3,349,428 |
| | RISK ENGINEERING INSURANCE | 893,743 | 1,110,099 |
| | COMPANY LTD. | - | - |
| | NEW PROVIDENT MUTUAL LTD. | 26,185 | 25,679 |
| Sub-Total Reinsurance premiums | | 5,251,067 | 4,485,206 |
| Intercompany expense allocation | FACTORY MUTUAL INSURANCE COMPANY | 5,163,004 | 5,736,999 |
| | Other related parties | - | - |
| Sub-Total Intercompany expense allocation | | 5,163,004 | 5,736,999 |
| Total expenses | | 10,414,071 | 10,222,205 |

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(b) Balances with related parties

Outstanding balances with related parties at the year-end are unsecured, interest free and repayable on demand, with settlement typically occurring on a quarterly basis. The carrying value of balances with related companies as at year-end approximates fair value. There have been no guarantees provided or received for any balances with related companies. No allowance for impairment has been recorded as at year-end in respect of receivables from related parties, nor has any expense been recognised for bad or doubtful debts during the period.

Details of receivables from and payables to related parties are, as follows:

| | | 2019 \$ | 2018 \$ |
|--|---|----------------|--------------------|
| Asset balances with related parties: | | | |
| Reinsurance receivables | AFFILIATED FM INS. CO. | - | (3,161,597) |
| | RISK ENGINEERING INSURANCE COMPANY LTD. | - | - |
| | NEW PROVIDENT MUTUAL LTD. | - | - |
| Sub-total Reinsurance receivables | | - | (3,161,597) |
| Reinsurance of insurance contract liabilities | AFFILIATED FM INS. CO. | - | - |
| | RISK ENGINEERING INSURANCE COMPANY LTD. | 542,325 | 456,549 |
| | NEW PROVIDENT MUTUAL LTD. | 6,879 | 5,853 |
| Sub-total Reinsurance of insurance contract liabilities | | 549,204 | 462,402 |
| Intercompany expense receivables | FACTORY MUTUAL INSURANCE COMPANY | - | - |
| | Other Group related parties | - | - |
| Sub-total Intercompany expense receivables | | - | - |
| Total asset balances | | 549,204 | (2,699,195) |

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| | | 2019 \$ | 2018 \$ |
|---|---|--------------------|---------------------|
| Liability balances with related parties: | | | |
| Reinsurance payables | AFFILIATED FM INS. CO. | (1,203,450) | (931,301) |
| | RISK ENGINEERING INSURANCE COMPANY LTD. | (447,122) | (306,336) |
| | NEW PROVIDENT MUTUAL LTD. | - | - |
| Sub-total Reinsurance payables | | (1,650,572) | (1,237,638) |
| Intercompany charges | FACTORY MUTUAL INSURANCE COMPANY | (2,313,839) | (1,786,222) |
| Intercompany expense payables | FACTORY MUTUAL INSURANCE COMPANY | 4,397,357 | (7,695,953) |
| | Other related parties | - | - |
| Sub-total Intercompany expense payables | | 2,083,518 | (9,482,175) |
| Total liability balances | | 432,946 | (10,719,813) |

24. Events after the reporting date - Impact of the Coronavirus (COVID-19) outbreak

Subsequent to end of the financial year, the COVID-19 outbreak was declared a pandemic by the World Health Organization in March 2020.

The outbreak and the response of Governments in dealing with the pandemic is interfering with general activity levels within the community, the economy and the operations of our business. The scale and duration of these developments remain uncertain as at the date of this report.

It is not possible to estimate the impact of the outbreak's near-term and longer effects or Government's varying efforts to combat the outbreak and support businesses. This being the case, we do not consider it practicable to provide a quantitative or qualitative estimate of the potential impact of this outbreak on the Branch at this time.

The financial statements have been prepared based upon conditions existing at 31 December 2019 and considering those events occurring subsequent to that date, that provide evidence of conditions that existed at the end of the reporting period. As the outbreak of COVID-19 occurred after 31 December 2019, its impact is considered an event that arose after the reporting period and accordingly, no adjustments have been made to financial statements as at 31 December 2019 for the impacts of COVID-19.

25. Standards issued but not yet effective

(a) IFRS 17 Insurance contracts

In May 2017, the IASB issued IFRS 17 Insurance Contracts (IFRS 17), a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 Insurance Contracts (IFRS 4) that was issued in 2005. IFRS 17 applies to all types of insurance contracts (i.e., life, non-life, direct insurance and re-insurance), regardless of the type of entities that issue them, as well as to certain guarantees and financial instruments with discretionary participation features. A few scope exceptions will apply. The overall objective of IFRS 17 is to provide an accounting model for insurance contracts that is more useful and consistent for insurers. In contrast to the requirements in IFRS 4, which are largely based on grandfathering previous local accounting policies, IFRS 17 provides a comprehensive model for insurance contracts, covering all relevant accounting aspects. The core of IFRS 17 is the general model, supplemented by:

- a specific adaptation for contracts with direct participation features (the variable fee approach); and
- a simplified approach (the premium allocation approach) mainly for short-duration contracts.

IFRS 17 is effective for annual reporting periods beginning on or after 1 January 2023, with comparative figures required. Early application is permitted, provided the entity also applies IFRS 9 and IFRS 15 on or before the date it first applies IFRS 17. Retrospective application is required. However, if full retrospective application for a group of insurance contracts is impracticable, then the entity is required to choose either a modified retrospective approach or a fair value approach.

The Branch is evaluating the impact of the new standard on its financial statements and related disclosures and plans to adopt the new standard on the required effective date together with IFRS 9.

(b) Amendments to IAS 1 and IAS 8: Definition of Material

In October 2018, the IASB issued amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors to align the definition of 'material' across the standards and to clarify certain aspects of the definition. The new definition states that, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.'

The amendments to the definition of material is not expected to have a significant impact on the Branch's financial statements.

Appointed actuary's report to the Directors of Factory Mutual Insurance Company – New Zealand Branch

Report in respect of a review of actuarial information in, or used in the preparation of, financial statements

This report is provided under section 78 of the *Insurance (Prudential Supervision) Act 2010* ("the Insurance Act"), and relates to a review of the actuarial information in, or used in the preparation of, the financial statements of Factory Mutual Insurance Company (New Zealand) ("FMIC (NZ)") for the year ended 31 December 2019.

The financial statements were authorised for issue by the Board of Directors of Factory Mutual Insurance Company ("FMIC (US)") on 9 April 2020 and the accompanying independent auditors' report was issued on 9 April 2020.

Name of appointed actuary conducting the review

I, Daniel Smith, of Taylor Fry Consulting Actuaries ("Taylor Fry") am a Fellow of the New Zealand Society of Actuaries. This review has been conducted by me in my role as appointed actuary to FMIC (NZ).

Other than that of actuary, I confirm that I have no relationship with, or any other interests in, FMIC (NZ).

Exemption from solvency standard

FMIC (US) has been granted a Section 59 exemption under the Insurance Act, which applies to overseas insurers of approved jurisdictions. This provides an exemption from compliance with the New Zealand Solvency Standard for Non-life Insurance Business and was dated 5 October 2015. I understand that under this exemption, the Reserve Bank of New Zealand considers the solvency of FMIC (NZ) based on the solvency requirements of FMIC (US) under the regulatory requirements of the State of Rhode Island. I have been provided with a Letter of Representation from the Chairman of FMIC (US) to the independent auditors of FMIC (US), which attests that FMIC (US) has complied with the rules and requirements of the State of Rhode Island and Providence Plantations Department of Business Regulation relating to statutory-basis financial information for the period covered by the financial statements for the year ended 31 December 2019. I have not reviewed the calculations underlying the solvency data supplied to the State of Rhode Island but have relied on the attestation of FMIC (US) and the report of the auditors as to their accuracy.

Work done in relation to actuarial information used in the financial statements

The actuarial information used in the financial statements comprises the outstanding claims liability as at 31 December 2019 shown in the statement of financial position. This amount was determined in accordance with the New Zealand Equivalent to International Financial Reporting Standard 4 ("NZ IFRS 4"), and represents the net central estimate plus a risk margin to provide a 75% probability of sufficiency. I confirm that this amount was calculated by me and advised to FMIC (NZ) in a Financial Condition Report dated 27 March 2020.

I have carried out a Liability Adequacy Test, and confirm that the unearned premium less deferred acquisition costs plus unexpired risk liability is not less than my actuarial estimate of the net premium liability.

In carrying out this review, I confirm that I have been provided with all required information and explanations from FMIC (NZ).

Opinion

In my opinion:

- » The actuarial information contained in the financial statements for FMIC (NZ) has been appropriately included in those statements, and
- » The actuarial information used in the preparation of the financial statements for FMIC (NZ) has been used appropriately.

Scope and limitations of review

This report is prepared for the Directors of FMIC (NZ), solely for the purposes set out in section 78 of the Insurance Act and for no other purpose.



Daniel Smith

Fellow of the New Zealand Society of Actuaries

9 April 2020