# CELEBRATING LIFE

ANNUAL REPORT 2013

40 YEARS

Fidelity Life

THE NEW ZEALAND LIFE COMPANY

40 YEARS

Fidelity Life

THE NEW ZEALAND LIFE COMPANY

*By providing insurance and savings solutions for New Zealanders, Fidelity Life helps keep Kiwi families strong today and tomorrow.*

### STEWARDSHIP

We make wise and prudent use of the resources entrusted to us for safe keeping

### FIDELITY

We retain our original focus to 'keep faith' in times of need

### LISTENING & RESPONDING

We engage in dialogue to create value through our relationships

ANNUAL REPORT 2013 The information in this report is current as at 30 June 2013. All amounts are in New Zealand dollars, unless otherwise specified

# FIDELITY LIFE
ANNUAL REPORT 2013

## CONTENTS


40 YEARS
Fidelity Life
THE NEW ZEALAND LIFE COMPANY
SIGNIFICANT EVENTS OF THE YEAR
Fidelity Life announces purchase of TOWER life insurance assets
Electronic underwriting system launched
Premium income exceeds $100M for the first time
40 years since first policy written
25% increase in net profit after tax

# CHAIRMAN'S REPORT

IAN BRADDOCK

## A MILESTONE YEAR FOR FIDELITY LIFE; 25% IMPROVEMENT IN PROFIT AFTER TAX AND THE ACQUISITION OF THE TOWER LIFE BUSINESS.

On behalf of the Board of Directors I am very pleased to announce total comprehensive income for the year ended 30 June 2013 of $17.5m. This is a significant improvement on the $14.1m achieved in 2012. This has also been a year of change for Fidelity Life, as we look to cement our position as a leader in the life insurance sector. Although the acquisition of the TOWER life business and the divestment of the Fidelity KiwiSaver Scheme did not complete until early in the 2014 financial year they have been a major focus for the Board and many of our staff in 2013. It is a pleasure to be able to report on the success of both transactions.

### Major Transactions

In May 2013 the Company announced that it had reached an agreement to purchase the life insurance policies of TOWER Health & Life Limited and the Group risk business of TOWER Life (N.Z.) Limited. That transaction successfully completed on 1 August 2013 and has made Fidelity Life the largest New Zealand owned life insurer and the third largest in the country. This is clearly an important milestone in the history of the Company.

The transaction signals the Board's determination to continue to grow the business through both strategic acquisition and organic means. It represents an exciting opportunity for the Board, management and staff to deliver an outcome to shareholders where the resultant combined business is greater than the sum of its individual parts. The Board has accepted that challenge and is working closely with senior management to ensure that this next phase contributes to a stronger business.

The full impact of the transaction will be reflected in next year's financial results; though $1.7m of costs incurred in relation to this are included in the current year's profit. The transaction was funded through a combination of full risk transfer reinsurance and a payment from capital reserves.

In July 2013 we announced the sale of the management of the Fidelity KiwiSaver Scheme, 64,800 members and over $300 million of managed funds, to Grosvenor Financial Services Group Limited ('Grosvenor'). This transaction completed on 23 August 2013. As part of the deal we have taken a minority shareholding in Grosvenor and will be actively working with them to build a strong relationship to benefit both organisations, advisers and all of our customers.

## Financial Results

The Company's increased profit was driven by a 10% rise in premium income; record new business production of $14.8m; and a sharp increase in investment income. Offsetting these were higher claims; higher income tax expense; and increases in management expenses, predominantly due to the transactions mentioned above.

The increase in investment income was driven by strong market conditions. Investment markets benefited from the growth in overseas markets, with market indices generally climbing over the period. This was tempered to some extent by the continuing strength of the New Zealand dollar. Although the majority of our investment income is for the benefit of policyholders, and is reflected by the increase in policyholder funds, shareholder investments contributed $6.9m to the profit (2012: $1.5m).

There were a high number of claims experienced over the course of the year. Of these claims a large number were for low-assured values, and therefore reduces the proportion recoverable from our reinsurers. Net claims increased 44% to $16.0m.

New life assurance tax rules, which came into effect in 2010, reduced the level of tax relief that New Zealand life assurance companies previously benefitted from. We are now in the third year of a five year transition period, which resulted in our overall tax charge increasing by $3.3m in the year. Tax credits attributable to shareholders decreased by $1.4m; whilst the tax expense attributable to policyholders increased by $1.9m, due to improved investment returns. It is worth noting that the Company's profit before tax attributable to shareholders increased by 46% in the year.

Total assets grew by 9% to $588m as investment valuations improved, contributions increased and policyholder surrenders and withdrawals fell. This figure excludes the funds under management in the Fidelity KiwiSaver Scheme. Shareholders' funds grew from $140m to $155m, and policyholder liabilities from $281m to $308m. Shareholders' funds as a percentage of policyholders' funds are consistent with last year at 50%, reflecting our continued focus on risk business.

## Dividend and Solvency

Despite a challenging operating environment the Company has recorded a strong profit result for the period and an improved solvency position. The Board has therefore authorised an ordinary base dividend of $2.42 per share, compared to $2.20 in 2012. However, as signalled in last year's Annual Report and in the interim results announcement in March 2013, we are unable to continue to impute dividends in the near term. This change in policy arises due to the new tax regime and the Company being unable to generate imputation credits for shareholders.

In addition to the $2.42 ordinary dividend, we will also pay shareholders a special dividend of $0.58 per share in recognition of the improved profitability and the success of the transactions we have undertaken. This special dividend will also not be imputed. This means the total dividend for the year will be $3.00 gross, with 33% resident withholding tax to be deducted from this.

The Board's revised dividend policy now is to maintain real increases in the dividend rate year on year; targeting a 10% per annum compound increase on the base dividend over a five year rolling period. Our ability to meet this expectation is subject to profit levels and maintaining prudent solvency margins; the Board having adopted a target solvency ratio of 130%. Our solvency margin as at 30 June 2013 is $30.1m compared to $22.2m in 2012, in line with the Board's objective.

In January A.M. Best reaffirmed our A- (Excellent) financial strength rating for the 17th consecutive year. As typically happens following a major transaction this rating is currently under review. It is therefore imperative that we continue to demonstrate to AM Best that Fidelity Life is prudently managed and well positioned for the smooth integration of the new business.

*continued on page 6*


"Believe you can
and you're halfway there."
- Theodore Roosevelt

## Full Insurance License Granted

Under the Insurance (Prudential Supervision) Act 2010 all insurers carrying on insurance business in New Zealand were required to be fully licensed and supervised by the Reserve Bank of New Zealand ('RBNZ') by 7 September 2013. On 2 August 2013 the Company was granted its full insurance license by the RBNZ to operate as a life insurer. Insurance licencing is aimed at ensuring that insurers are adequately capitalised and prudently managed. The RBNZ licensing requirements are wide ranging, covering aspects such as corporate governance, risk management and financial strength. As with the year under review, we expect that going forward licencing will require significant input from the Board and senior management.

## Outlook

The Board acknowledges that there is hard work ahead, not least of which is the successful integration of the TOWER business over the coming years. It is important to recognise that this transaction provides us with both leverage and scale. It also presents a huge opportunity to cement a position as a leading insurance provider in the New Zealand market. The Board has every confidence that the management and structures now in place will result in a very positive long-term outcome for shareholders.

The challenge will be to continue to successfully grow the business and deliver acceptable returns to shareholders; against a backdrop of a fast changing legal, regulatory and tax environment. We look forward to 2014 with enthusiasm, and believe we are well positioned to meet these challenges.

## Acknowledgements

I would like to express my appreciation to our policyholders, Fidelity KiwiSaver Scheme members and to the large network of financial advisers for their loyalty and commitment to the Fidelity Life brand. I would also like to thank our other business partners including fund managers, trustees and reinsurers that continue to support us.

In particular I would like to thank Milton Jennings for his effective leadership of the Company during the year. I also extend my thanks to his management team and the rest of the Fidelity Life staff, who at times were put under significant pressure this year and who again responded with their usual hard work and dedication.

Finally, I thank my fellow directors for their contribution and ongoing commitment to Fidelity Life.

Ian Braddock

IAN BRADDOCK
CHAIRMAN

## UNEXPECTED COVER IN A TIME OF NEED

### MARCUS WAS INVOLVED IN A DELIBERATE HIT AND RUN INCIDENT WHICH RESULTED IN MULTIPLE INJURIES THAT LEFT HIM UNABLE TO WORK.

Marcus was 42 years old and had his own furniture restoration business. He is the father of three, who at the time of the incident were school-aged.

Marcus also led a very active lifestyle. His hobbies included dirt bike riding, scuba diving and he also had a single figure golf handicap.

Marcus' injuries left him with impaired vision, speech difficulties, on-going migraines and fatigue. Marcus suffered memory loss and even now he cannot clearly recall any events for the 12 months following the incident, including moving into his new home. He will never drive a car again, is not able to ride a bicycle and has been told that he will never return to full time employment. Even part time employment will be difficult for him.

Fortunately, Marcus had taken out a Fidelity Life Mortgage Protector Policy, with Income Protection, Accelerated Critical Care and Waiver of Premium benefits. He saw the need to have insurance protection to meet mortgage commitments if he became unable to work.

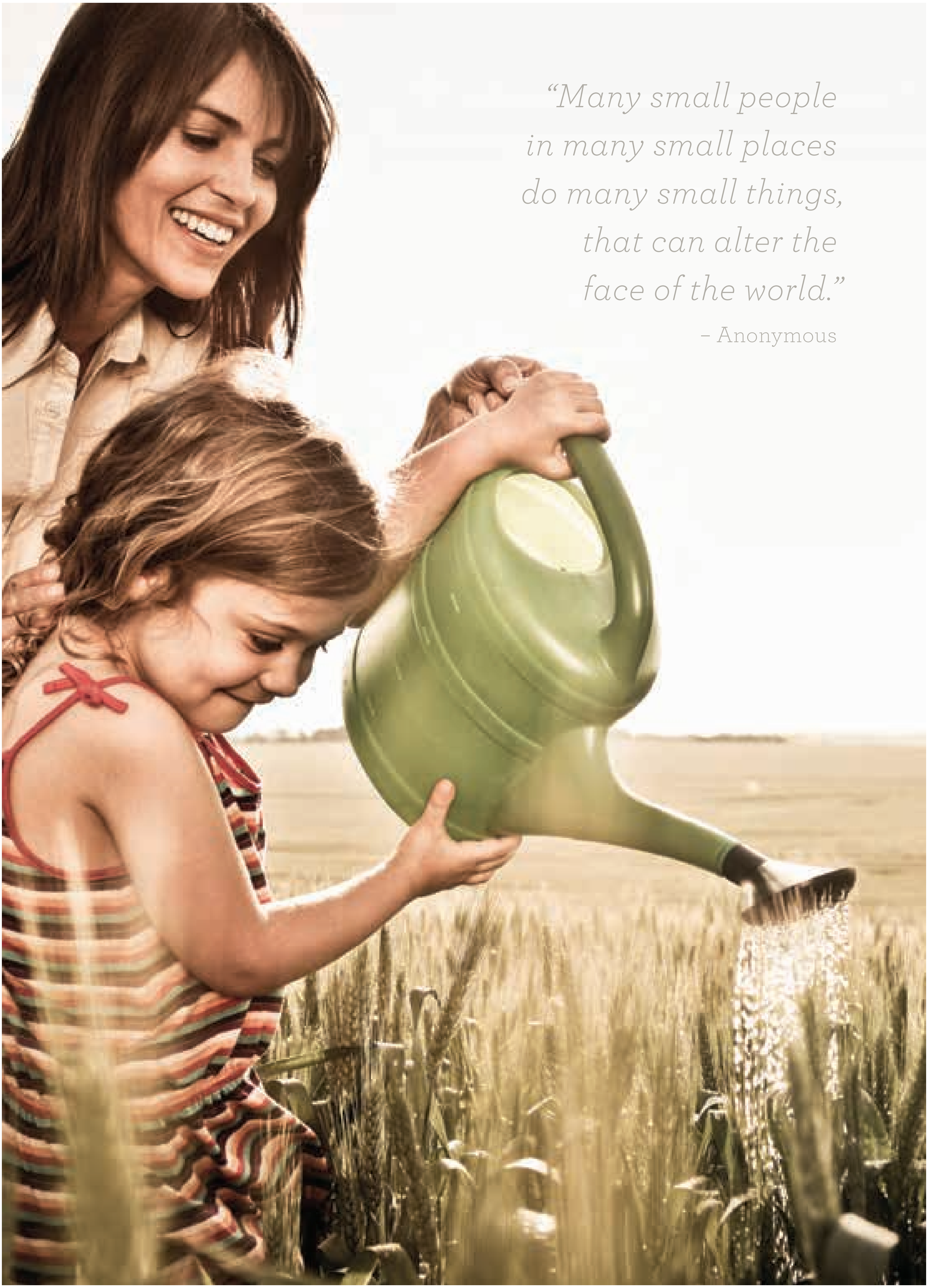
The Income Protection benefit on the policy provides Marcus with a specified income for five years; and the Waiver of Premium benefit also ensures that as long as Marcus is unable to work in his own occupation, his insurance payments are covered. Finally, Marcus' Accelerated Critical Care benefit provided a lump sum payment for permanent disability. This lump sum was enough to pay the remaining mortgage off on his new home.

Marcus' story is one of great sadness but Marcus agrees wholeheartedly that having insurance with Fidelity Life took the financial burden away from a situation that has impacted him both mentally and physically. "It meant there was no panic. I had complete peace of mind financially and was able to concentrate on dealing with everything else going on."

Three years on, Marcus is still undergoing rehabilitation. He has moved house so that he and his children are within walking distance of town. He has since done a tandem skydive and is back playing golf despite impaired vision. His upbeat and his tenacious attitude remains. Although he tires easily and is often in bed by 7:30pm at night, Marcus' goal is to one day return to part time work.

In the short term, he is looking forward to a Pacific Island cruise with his new partner, his first holiday since the accident. He has spotted a climbing wall on-board the ship and looks forward to giving it a go!

**This is a real life claim, but names and personal information have been changed to protect privacy.**


*"Many small people
in many small places
do many small things,
that can alter the
face of the world."*
– Anonymous

# CEO'S REVIEW

MILTON JENNINGS

## IN FUTURE YEARS, 2013 WILL BE REGARDED AS A KEY PHASE IN THE DEVELOPMENT AND GROWTH OF FIDELITY LIFE.

2013 was one of the most eventful periods in the 40 year history of Fidelity Life. It was a year in which we advanced our growth strategy by laying the groundwork to purchase the TOWER life business. We also spent time finding a strategic partner who could take over management of the Fidelity KiwiSaver Scheme. But most significantly, it was the year in which we demonstrated to the New Zealand market that Fidelity Life is a major force in the local financial services industry.

### Financial Result

Whilst we always strive for greater profitability, on the macro side we have a low interest rate environment, greater taxation from the new regime, increased compliance costs and strong competition in the life insurance market.

It was especially pleasing that we were able to grow our premium income by 9%, thanks to record new business of $14.8m. This was supplemented by a very good investment year with an average return across the invested assets of 9%. However, much of this goes to policyholders, as reflected by the increase in policyholder liabilities. Shareholders' funds tend to be conservatively invested to maximise solvency, but we still achieved an average return on largely fixed interest type investments of about 6%.

Increases in claims and management expenses adversely affected profits this year. For the three years prior to 2013 death claims had been falling but that trend reversed in the year with a 43% increase in gross death claims. In addition, critical care claims were up 8% over last year. These spikes in claims are consistent with our historical experience and the nature of the industry we operate in. If we take out transaction costs then management expenses increased 16%. This included a number of non-recurring one off costs as well as extra expenditure in marketing to boost new business sales. Our major expense, employment costs, was well controlled and only rose by 8%. New business premium per sales and marketing staff increased 40% in the last year.

We have a strong base of planned margins on our risk products. Along with close cost control and assuming a normal claims experience, we are confident of producing an improved result for 2014.

### TOWER Life Purchase

While the TOWER transaction completed in the 2014 financial year it consumed a huge amount of time and resources during most of the year under review. I gratefully acknowledge the tremendous amount of determination and sacrifice that was shown by the Fidelity Life staff involved in putting this deal together. In particular, I would like to highlight the hard work of Ed Eadie, John Smith, Richard Horton and their teams, plus all our external consultants.

With the transaction now complete, Fidelity Life has total in-force annualised premium in excess of $190m and another 47,000 policyholders. TOWER had a strong presence in the group risk market with over $20m of in-force premium and the acquisition takes us to number three in that market. I strongly believe that this transaction will propel the Company forward as one of the leading risk insurers in the New Zealand market. We have put together an experienced integration team to ensure that the transition is successfully managed and that the projected added value for shareholders is achieved.

## Fidelity KiwiSaver Scheme

As a result of the Company's strategic focus on core profitability, in 2013 we decided to divest our KiwiSaver business but maintain our niche non-KiwiSaver investment interests. The resultant search for a business partner who was willing to form a strategic alliance with us led to Grosvenor Financial Services Group Limited ('Grosvenor'). Fidelity Life has had a long standing and very positive relationship with Grosvenor for many years. The firm shares a lot of our values, particularly in their support for financial advisers, so was an obvious strategic fit.

The agreement that we have now completed for the transfer of the Fidelity KiwiSaver Scheme management rights sees us take a minority equity position in Grosvenor. We will work closely with them to ensure that advisers continue to have a quality New Zealand managed KiwiSaver offering. In turn we will provide risk products to their clients.

## Distribution

Our key distribution channel remains our loyal network of advisers, who continue to show us strong support and commitment. In order to continue to fully support advisers, we have extended our network of Business Development Managers from 10 to 13. They are invaluable to our strategy in developing and nurturing relationships with advisers as well as acting as an intermediary with our other departments.

We continue to receive strong support for our spread commission model, which we see as the way forward. This differentiates us from other companies in the market and reduces the impact of competing on high initial commissions. Spread commission helps advisers build the value of their business by creating a significant asset for the future. Furthermore, it results in a higher level of renewal income, providing the right type of incentive and allowing good client service in a regulated world. Our sales and marketing strategies of relationship building and IT enhancements, as well as the spread commission on offer, are the key reasons for achieving our record new business production this year. We again thank advisers for their loyal support and their belief in what we are trying to achieve at Fidelity Life.

## People

The TOWER transaction has recently added another 69 people to our overall headcount. This takes the total number of staff to over 250, clearly demonstrating that the Company has now become a major employer in the local financial services industry.

The general calibre of Fidelity Life staff is high, and all have worked determinedly and tirelessly with management to maintain the business and not let standards slip while these major transactions were negotiated. I remain particularly proud of the positive culture at the Company – the resulting 88% retention rate enables us to maintain continuity over longer periods than the industry average, while also bringing in new blood and new ideas.

Recognising the changing needs of a growing business, we strengthened our Sales and Marketing areas with some recent key senior appointments. Peter Mensah stepped across into the role of National Sales Manager; Mark Nalder has joined us from TOWER as Head of Corporate Distribution; and Ian Moody takes on the role of Chief Marketing Officer. These three have extensive financial services backgrounds and bring a wealth of experience to the senior leadership team.

## Technology

Keeping up with developments in information technology and utilising its capabilities to improve the efficiency of our operations continues to be an important part of our business strategy. On-going investment in this area is necessary to enhance Fidelity Life's complex computer systems to be more efficient and to meet the needs of our ever changing environment.

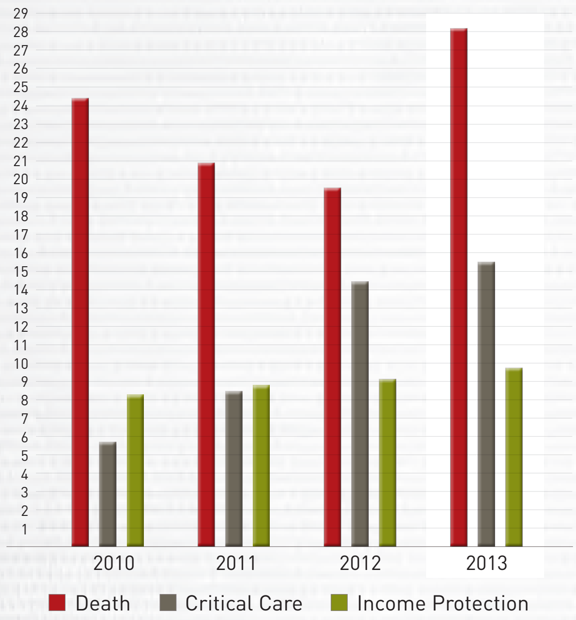
The take-up of our web-based electronic application process (E-App) has been very encouraging, with over 3,000 lives underwritten in this period. We see the online area as a key opportunity to differentiate ourselves and we continue to be innovators in this space. Also during the year our quotation software, Apollo, went web-based; we were able to link Apollo to advisers' CRM systems to make their processes even more efficient; and we launched a new credit card system. Recent projects have started in relation to reinsurance and finance, and there will be some new product developments launching in the new financial year.

*continued on page 12*

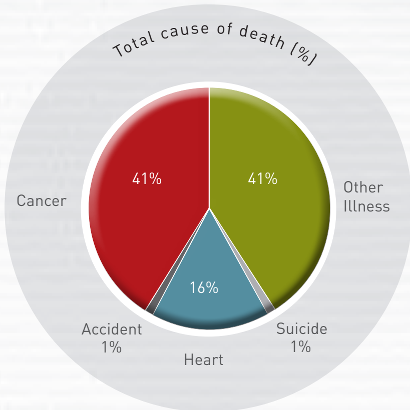
# 2013 CLAIM STATISTICS

for the year ended 30 June 2013

## CLAIMS PROFILE ($MILLIONS) 2010-2013

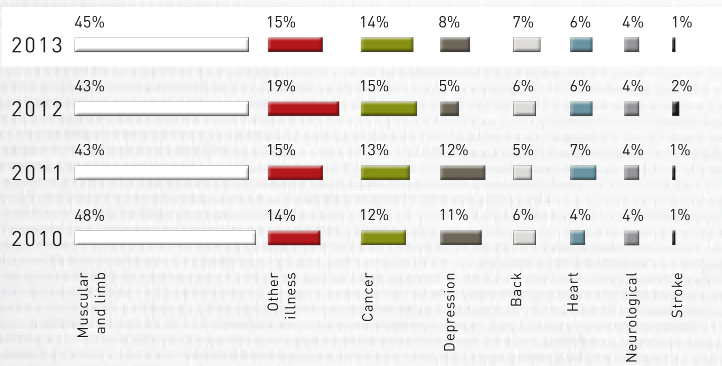


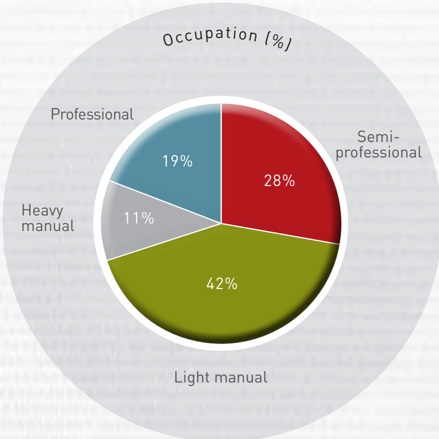

## DEATH AND TERMINAL ILLNESS CLAIMS 2013




- 344 Death and Terminal Illness claims totalling $28,150,647
- Reinsurance recoveries of $20,676,205
- Youngest claimant: 13
- Oldest claimant: 92
- Average age of claimant: 61

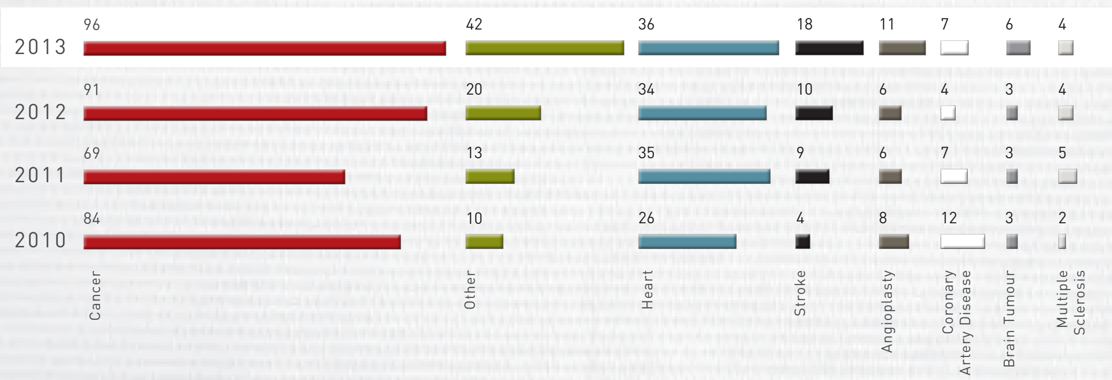
## INCOME PROTECTION CLAIMS 2010-2013




- Claims due to illness: 56%
  Claims due to accident: 44%
- Gross income protection claims totalling $9,823,199
- Reinsurance recoveries of $7,258,768
- Average insured monthly benefit $3,596

## CRITICAL CARE CLAIMS 2010-2013




- 218 Critical Care claims totalling $15,568,336
- Reinsurance recoveries of $9,518,575
- Youngest claimant: 28
- Oldest claimant: 69
- Average age of claimant: 50

## Community

Fidelity Life has always seen itself as being a part of the wider community of New Zealand. Therefore an important part of our business culture is our continued support of a number of charities. The main charity that we support is Leukaemia & Blood Cancer New Zealand and this year staff members were active in participating in a number of their fundraisers. This included Shave for a Cure, the Golf Marrowthon 100 Hole Challenge and the Sky Tower Challenge.

We continue to support the Multiple Sclerosis Society and several staff members continue to provide mentoring support to the Foundation for Youth Development.

## Looking ahead

Our major focus this year will be following through on the success of the transactions with TOWER and Grosvenor. Following the TOWER deal there has already been significant work undertaken to gain efficiencies and this will continue for some time yet. Within the next 12 months we will be bringing all Auckland staff together under one roof.

We will continue to work hard to attract and retain quality financial advisers who value our offering of product quality, modern technology, a track record of consistent support and dedicated, friendly staff. We performed extremely well in this year's Beaton Adviser Satisfaction Survey, particularly in the key areas of underwriting speed, claims servicing and adviser support. Fidelity Life was rated four stars and had the second highest overall satisfaction rating.

An improving operating environment, combined with a renewed focus on profitability and efficiencies, gives me every confidence that Fidelity Life will continue to grow and succeed into the future. I would like to thank the Board, my senior management team and staff, advisers and shareholders for the support they have been shown to the Company over this period. This is an exciting time for the Company and I am confident that 2014 will be another successful year.

MILTON JENNINGS
CHIEF EXECUTIVE OFFICER

# FINANCIAL SUMMARY

for the years ended 30 June

| Dollars in thousands | 2013 | 2012 | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|
| Ordinary risk premium * | 104,134 | 95,048 | 86,746 | 80,716 | 75,417 |
| Investment income **/*** | 39,407 | 3,391 | 45,128 | 54,398 | 2,590 |
| Claims expense *** | 54,671 | 44,649 | 39,549 | 38,534 | 40,233 |
| Net profit after taxation | 17,075 | 13,644 | 18,314 | 16,916 | 10,350 |
| Ordinary dividend per share | $2.42 | $2.20 | $1.70 | $1.32 | $1.00 |
| Special dividend per share | $0.58 | - | $0.30 | $0.15 | - |
| Earnings per share (year-end) | $11.86 | $9.48 | $12.73 | $11.76 | $7.19 |
| Shareholders' equity | 154,712 | 140,401 | 129,089 | 112,661 | 96,845 |
| Policyholder liabilities | 307,619 | 281,895 | 289,851 | 290,377 | 272,575 |
| Total assets ** | 588,499 | 540,293 | 531,130 | 529,948 | 493,345 |
| Shares on issue | 1,439 | 1,439 | 1,439 | 1,439 | 1,439 |

* 2009 has been adjusted from published financial statements to reflect a reclassification of a portion of premium from risk to savings.

** In 2011 to 2013 amounts relating to Fidelity Capital Guaranteed Bond Limited and consolidated in the Group have been prepared on a realisable value basis.

*** In 2011 to 2013 the Financial Summary includes discontinued activities which are disclosed separately within the Statements of Comprehensive Income.

*"Alone we can do so little; together we can do so much."*

– Helen Keller

# STATUTORY AND OTHER DISCLOSURES

for the years ended 30 June 2013

| Director | Direct shareholdings | | Indirect beneficial shareholdings | | Total remuneration and other benefits |
|---|---|---|---|---|---|
| | As at 30 June 2013 | Increase/ (decrease) during the year | As at 30 June 2013 | Increase/ (decrease) during the year | |
| **Ian Braddock** Chairman | 531 | – | 9,933 | – | 149,403 |
| **Colin Wise** Director | 500 | – | 8,354 | – | 74,701 |
| **Jeff Meltzer** Director | 517 | – | 10,342 | – | 74,701 |
| **Carole Durbin** Director | 3,750 | – | – | – | 74,701 |
| **Anne Blackburn** Director | 500 | – | – | – | 74,701 |

## Information on directors of the parent company

In accordance with the Company's constitution, Ian Braddock and Anne Blackburn retire by rotation at the AGM and being eligible, offer themselves for re-election.

Jeff Meltzer is a trustee of the Fidelity Family Trust, which holds 788,370 (2012: 788,370) shares in Fidelity Life.

Ian Braddock is a trustee of the Fidelity Life Employee Share Purchase Scheme which holds 20,900 (2012: 29,383) shares in Fidelity Life.

## Director's insurance

In accordance with the constitution, Fidelity Life Assurance Company Limited and its subsidiaries have arranged policies of directors' and employees' liability insurance which, together with a deed of indemnity, ensure that directors will incur no monetary loss as a result of actions undertaken by them as directors provided they operate within the law. The directors certified that the premium was fair and reasonable to the Company.

## Subsidiary Company Directors

| | Ian Braddock | Colin Wise | Jeff Meltzer |
|---|---|---|---|
| Fidelity Fund Management Limited | | • | • |
| Fidelity Capital Guaranteed Bond Limited | • | • | • |
| Fidelity Securities Limited* | • | | • |

* Fidelity Securities Limited was sold to Grosvenor Investment Management Limited on 23 August 2013. Ian Braddock and Jeff Meltzer resigned as directors on that date.

No subsidiary company director received in his capacity as such, directors' fees nor other such benefits.

## Employee remuneration

Details of total remuneration packages including grossed-up benefits for employees of the parent company are set out below.

| Remuneration ranges | Number of employees in each band | |
|---|---|---|
| | 2013 | 2012 |
| $460,000-$470,000 | 1 | 0 |
| $440,000-$450,000 | 1 | 0 |
| $420,000-$430,000 | 0 | 1 |
| $370,000-$380,000 | 0 | 1 |
| $320,000-$330,000 | 1 | 0 |
| $280,000-$290,000 | 1 | 0 |
| $270,000-$280,000 | 1 | 1 |
| $250,000-$260,000 | 1 | 0 |
| $240,000 $250,000 | 4 | 1 |
| $220,000-$230,000 | 3 | 0 |
| $210,000-$220,000 | 0 | 1 |
| $200,000-$210,000 | 0 | 2 |
| $190,000-$200,000 | 2 | 1 |
| $180,000-$190,000 | 4 | 2 |
| $170,000-$180,000 | 4 | 3 |
| $160,000-$170,000 | 3 | 1 |
| $150,000-$160,000 | 1 | 4 |
| $140,000-$150,000 | 1 | 5 |
| $130,000-$140,000 | 5 | 4 |
| $120,000-$130,000 | 8 | 6 |
| $110,000-$120,000 | 6 | 6 |
| $100,000-$110,000 | 9 | 9 |

## Auditors

PricewaterhouseCoopers have indicated their willingness to continue as auditors of the Group.

## Use of company information

No notices were received from directors regarding the use of company information that would not have been available to them other than in their capacity as directors.

## Events after balance date

The directors are not aware of any matter or circumstance since the end of the financial year, not otherwise dealt with in this report nor the attached financial statements that has significantly affected the operations of Fidelity Life Assurance Company Limited.

## Shareholders

The following table shows the names and holdings of the ten largest shareholders of the Company as at 30 June 2013.

| Shareholders | Shares held |
|---|---|
| 1. Whale M J & Meltzer J P | 788,370 |
| 2. Burgess G A J & Burgess M S | 258,914 |
| 3. Farmers' Mutual Group | 166,185 |
| 4. Trotter K & Childs P & Hughes C | 23,996 |
| 5. Braddock I L & Jennings M J | 20,900 |
| 6. Alison D J & Alison K H | 13,636 |
| 7. Meltzer J P & Porus J L | 10,342 |
| 8. Alison K H & Alison D J & Webber J E | 9,958 |
| 9. Braddock I L & Braddock F M | 9,933 |
| 10. Hamilton Y D & Vanderwee J C & Hamilton R B & Hamilton G R | 9,471 |

# STATEMENT OF CORPORATE GOVERNANCE

for the years ended 30 June 2013

THE DIRECTORS ARE ELECTED BY THE SHAREHOLDERS AND ARE ACCOUNTABLE FOR THE PERFORMANCE OF THE GROUP AND COMPLIANCE BY THE GROUP WITH LAWS AND STANDARDS.

## The board

The board of directors controls and monitors the business of Fidelity Life Assurance Company Limited and subsidiary companies on behalf of the shareholders. The directors are elected by the shareholders and are accountable for the performance of the Group and compliance by the Group with laws and standards. The board has adopted the Financial Markets Authority "Principles and Guidelines of Corporate Governance" as a framework against which the board monitors and reviews its corporate governance.

## Board membership

At 30 June 2013 the board comprised five non-executive directors, including a non-executive chairman. Their qualifications and experience are set out at the end of this report.

## Board attendance

Attendance at the scheduled and unscheduled formal meetings of the Board and its committees for the period 1 July 2012 to 30 June 2013 was as follows:

| | Board | | Audit & Risk | | Remuneration | Nomination |
|---|---|---|---|---|---|---|
| | Scheduled | Unscheduled | Scheduled | Unscheduled | Scheduled | Scheduled |
| Meetings | 11 | 8 | 5 | 2 | 2 | 1 |
| Ian Braddock | 11 | 8 | 5 | 2 | 2 | 1 |
| Colin Wise | 11 | 8 | n/a | n/a | 2 | 1 |
| Jeff Meltzer | 11 | 8 | 4 | 2 | n/a | 1 |
| Carole Durbin | 11 | 8 | 5 | 2 | n/a | 1 |
| Anne Blackburn* | 11 | 7 | 5 | 1 | 2 | 1 |

* Anne Blackburn was appointed to the Audit & Risk Committee on 14 September 2012

Board members also attended a number of informal meetings during the year.

## Committees

The board has formally constituted three board committees: the Audit & Risk Committee, the Remuneration Committee and the Nomination Committee.

**Audit & Risk Committee:** Established as a link between the board and external auditors. Provides independent oversight of the effectiveness of the Company's financial reporting and risk management processes. Committee membership is reviewed annually.

**Members:** Anne Blackburn (Chair), Ian Braddock, Jeff Meltzer and Carole Durbin.

**Remuneration Committee**: Established to assist the board with the remuneration structures for the Company's Chief Executive Officer and senior executives.

**Members:** Colin Wise (Chair), Ian Braddock and Anne Blackburn.

**Nomination Committee:** Established to assist in the planning of the board's composition and the appointment of new directors.

**Members:** all directors.

## Directors' shareholdings

Directors are required to hold at least 500 shares. They must refrain from dealing in the Company's shares for their personal benefit except for the periods from the announcement of annual results to 30 November, and the announcement of half year results to 30 April; and must refrain from trading at any time if they have market sensitive information. The same restrictions are imposed upon senior management.

## Directors' fees

The level of non-executive directors' fees was last approved at the shareholders meeting on 9 November 2012 as $65,000 per director and $130,000 for the chairman.

No additional fees are paid for attendance at board committee meetings.

## Non-executive directors' superannuation fund

In accordance with the Company's constitution, it is the Company's policy to pay a sum into a superannuation fund for each director's retirement. This amount is equal to 10% of that director's fees after the deduction of all taxes payable, as settled by the Company. Distribution of the proceeds is at the discretion of the trustees of the fund.

## Ethics

The board has adopted the Code of Proper Practice for Directors of the New Zealand Institute of Directors. The board acknowledges the need for the continued maintenance of a high standard of corporate governance practices and ethical conduct by all directors and employees of Fidelity Life Assurance Company Limited.

## Delegational framework

The board has formally delegated to the Chief Executive Officer the day-to-day management of the Group. The Chief Executive Officer recommends to the board changes in the business, performance, goals, strategies and plans of the Group.

Comprehensive formal delegations of financial authority to management are in place, as are agreed policy frameworks with respect to the principal operational aspects of the Group.

Annual budgets and longer term strategic financial plans are agreed by the board, which in turn monitors management's performance relative to the goals and plans.

## Internal controls

The Group has in place an integrated framework of controls designed to safeguard the Group's assets and interests and to ensure the integrity of its reporting. The overall framework has been developed and guidelines formulated for risk management structures and processes in areas additional to financial risk.

## Business risks

All committee duties have been developed to allow the board to identify and manage the various business risks faced by the Group. In order to ensure that procedures are current and comprehensive, the responsibilities of each committee are reviewed annually.

# THE BOARDROOM

CHAIRMAN

IAN BRADDOCK BCom CA MInstD

DIRECTOR

COLIN WISE

DIRECTOR

JEFF MELTZER JP BCom FCA MInstD AAMINZ

DIRECTOR

CAROLE DURBIN BCom LLB(Hons)FInstD

DIRECTOR

ANNE BLACKBURN MA

CHIEF EXECUTIVE OFFICER

MILTON JENNINGS BCom CA

APPOINTED ACTUARY

JOHN SMITH MSc FNZSA FIAA

CHIEF FINANCIAL OFFICER

ED EADIE BSc (Hons)

# FINANCIAL STATEMENTS

## Contents

## STATEMENTS OF COMPREHENSIVE INCOME

for the year ended 30 June 2013

| | Note | Group 2013 $'000 | Group 2012 $'000 | Parent 2013 $'000 | Parent 2012 $'000 |
|---|---|---|---|---|---|
| **INSURANCE BUSINESS** | | | | | |
| **Revenue** | | | | | |
| Insurance premium revenue | | 104,134 | 95,048 | 104,134 | 95,048 |
| Insurance premium ceded to reinsurers | 8 | (35,191) | (33,787) | (35,191) | (33,787) |
| Fee and commission income | 9 | 891 | 475 | 891 | 475 |
| Investment income | 10 | 39,406 | 3,388 | 39,406 | 3,388 |
| Investment property income | 11 | 1,284 | 1,285 | 1,284 | 1,285 |
| Other income | 12 | 65 | 6,603 | 65 | 6,603 |
| **Total insurance revenue** | | 110,589 | 73,012 | 110,589 | 73,012 |
| **Expenses** | | | | | |
| Claims expense | 13 | 54,671 | 44,636 | 54,671 | 44,636 |
| Reinsurance recoveries | 14 | (38,685) | (33,550) | (38,685) | (33,550) |
| Net change in life insurance contract liabilities | 31 | (13,142) | 842 | (13,142) | 842 |
| Net change in life investment contract liabilities | 32 | 23,378 | (7,053) | 23,378 | (7,053) |
| Commission and management expenses | 15 | 64,640 | 54,619 | 64,640 | 54,619 |
| **Total insurance expenses** | | 90,862 | 59,494 | 90,862 | 59,494 |
| **Net insurance income before tax** | | 19,727 | 13,518 | 19,727 | 13,518 |
| Income tax expense | 16 | 3,280 | 43 | 3,280 | 43 |
| **Net insurance income after tax** | | 16,447 | 13,475 | 16,447 | 13,475 |
| **Net discontinued operations income after tax** | 17 | 628 | 169 | 628 | 169 |
| **Profit for the year attributable to the owners of the Company and Group** | 7 | 17,075 | 13,644 | 17,075 | 13,644 |
| **OTHER COMPREHENSIVE INCOME** | | | | | |
| **Items that will not be reclassified to profit or loss:** | | | | | |
| Revaluations movement, net of tax | 34 | 400 | 397 | 400 | 397 |
| Employee share purchase plan | 33 | 59 | 71 | 59 | 71 |
| Other comprehensive income for the year, net of tax | | 459 | 468 | 459 | 468 |
| **TOTAL COMPREHENSIVE INCOME FOR THE YEAR ATTRIBUTABLE TO THE OWNERS OF THE COMPANY AND GROUP** | | 17,534 | 14,112 | 17,534 | 14,112 |
| **BASIC AND DILUTED EARNINGS PER SHARE** | | | | | |
| From continuing operations | 36 | 11.43 | 9.36 | | |
| From discontinued operations | 36 | 0.43 | 0.12 | | |

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

# STATEMENTS OF FINANCIAL POSITION

as at 30 June 2013

| | | Group | | Parent | |
|---|---|---|---|---|---|
| | Note | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| **ASSETS** | | | | | |
| Cash and cash equivalents | 18 | **12,984** | 15,543 | **12,790** | 15,296 |
| Assets arising from reinsurance contracts | 19 | **12,091** | 10,347 | **12,091** | 10,347 |
| Financial assets at fair value through profit or loss | 20 | **485,463** | 437,228 | **419,850** | 373,734 |
| Derivative financial instruments | 21 | **857** | 2,721 | **857** | 2,721 |
| Loans and other receivables | 22 | **31,520** | 32,446 | **31,520** | 32,446 |
| Investment property | 23 | **10,203** | 9,275 | **10,203** | 9,275 |
| Property, plant and equipment | 24 | **10,121** | 9,282 | **10,121** | 9,282 |
| Investment in subsidiaries | 25 | **-** | - | **8** | 8 |
| Income tax asset | 16 | **3,881** | 2,560 | **3,881** | 2,560 |
| Deferred tax assets | 26 | **17,090** | 15,102 | **17,090** | 15,102 |
| Deferred acquisition costs – investment | 27 | **6** | 867 | **6** | 867 |
| Intangible assets | 28 | **4,283** | 4,922 | **4,283** | 4,922 |
| **TOTAL ASSETS** | | **588,499** | 540,293 | **522,700** | 476,560 |
| **LIABILITIES** | | | | | |
| Payables and other financial liabilities | 29 | **30,541** | 30,652 | **30,520** | 30,579 |
| Current tax liabilities | | **428** | - | **428** | - |
| Derivative financial instruments | 21 | **2,557** | 173 | **2,557** | 173 |
| Deferred tax liabilities | 26 | **26,864** | 23,512 | **26,864** | 23,512 |
| Interest bearing liabilities | 30 | **65,778** | 63,660 | **-** | - |
| Life insurance contract liabilities | 31 | **(30,595)** | (17,054) | **(30,595)** | (17,054) |
| Life investment contract liabilities | 32 | **338,214** | 298,949 | **338,214** | 298,949 |
| **TOTAL LIABILITIES** | | **433,787** | 399,892 | **367,988** | 336,159 |
| **NET ASSETS** | | **154,712** | 140,401 | **154,712** | 140,401 |
| **EQUITY** | | | | | |
| Share capital | 33 | **13,186** | 12,946 | **13,186** | 12,946 |
| Retained earnings | 34 | **140,357** | 126,686 | **140,357** | 126,686 |
| Revaluation reserve | 34 | **1,169** | 769 | **1,169** | 769 |
| **TOTAL EQUITY** | | **154,712** | 140,401 | **154,712** | 140,401 |

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

For and on behalf of the board

5 September 2013

Ian Braddock
**Chairman**

Anne Blackburn
**Director**

## STATEMENTS OF CHANGES IN EQUITY

for the year ended 30 June 2013

| | Note | Share capital $'000 | Retained earnings $'000 | Reserves $'000 | Total $'000 |
|---|---|---|---|---|---|
| **GROUP AND PARENT** | | | | | |
| **Balance at 1 July 2011** | | 12,581 | 116,136 | 372 | 129,089 |
| **Profit for the year** | | - | 13,644 | - | 13,644 |
| **Other comprehensive income** | | | | | |
| **Items that will not be reclassified to profit or loss:** | | | | | |
| Revaluations, net of tax | 34 | - | - | 397 | 397 |
| Employee share purchase plan | 33 | 71 | - | - | 71 |
| **Total other comprehensive income for the year** | | 71 | - | 397 | 468 |
| **Total comprehensive income for the year** | | 71 | 13,644 | 397 | 14,112 |
| **Transactions with owners** | | | | | |
| Ordinary shares issued | 33 | 45 | - | - | 45 |
| Share capital vested from Trust | 33 | 249 | - | - | 249 |
| Dividends | 35 | - | (3,094) | - | (3,094) |
| **Total transactions with owners** | | 294 | (3,094) | - | (2,800) |
| **BALANCE AT 30 JUNE 2012** | | 12,946 | 126,686 | 769 | 140,401 |
| **Balance at 1 July 2012** | | 12,946 | 126,686 | 769 | 140,401 |
| **Profit for the year** | | - | 17,075 | - | 17,075 |
| **Other comprehensive income** | | | | | |
| **Items that will not be reclassified to profit or loss:** | | | | | |
| Revaluations, net of tax | 34 | - | - | 400 | 400 |
| Employee share purchase plan | 33 | 59 | - | - | 59 |
| **Total other comprehensive income for the year** | | 59 | - | 400 | 459 |
| **Total comprehensive income for the year** | | 59 | 17,075 | 400 | 17,534 |
| **Transactions with owners** | | | | | |
| Share capital vested from Trust | 33 | 181 | - | - | 181 |
| Dividends | 35 | - | (3,404) | - | (3,404) |
| **Total transactions with owners** | | 181 | (3,404) | - | (3,223) |
| **BALANCE AT 30 JUNE 2013** | | 13,186 | 140,357 | 1,169 | 154,712 |

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

| | | Group | | Parent | |
|---|---|---|---|---|---|
| | Note | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | | | |
| Premiums from life insurance contracts | | 104,214 | 97,678 | 104,214 | 97,678 |
| Deposits from life investment contracts | | 55,560 | 43,795 | 55,560 | 43,795 |
| Reinsurance received | | 36,942 | 30,186 | 36,942 | 30,186 |
| Interest received | | 8,387 | 7,121 | 8,386 | 7,118 |
| Dividends received | | 37 | 175 | 37 | 175 |
| Distributions from unitised investments | | 6,639 | 8,442 | 6,639 | 8,442 |
| Other investment income | | 17,168 | 9,797 | 17,168 | 9,797 |
| Proceeds from reinsurance treaty recapture | | - | 6,500 | - | 6,500 |
| Benefits paid under life insurance contracts | | (54,329) | (40,375) | (54,329) | (40,375) |
| Benefits paid under life investment contracts | | (39,675) | (45,457) | (39,675) | (45,457) |
| Reinsurance premiums paid | | (34,744) | (33,787) | (34,744) | (33,787) |
| Commission paid | | (34,961) | (29,253) | (34,961) | (29,253) |
| Payments to suppliers and employees | | (29,032) | (24,791) | (28,978) | (24,067) |
| Income tax paid | | (3,051) | (1,200) | (3,051) | (1,200) |
| **NET CASH INFLOWS FROM OPERATING ACTIVITIES** | 37 | 33,155 | 28,831 | 33,208 | 29,552 |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | | | |
| Purchases of intangible assets | | (928) | (1,455) | (928) | (1,455) |
| Purchases of financial assets | | (234,119) | (342,783) | (234,119) | (342,783) |
| Purchases of property, plant and equipment | | (938) | (390) | (938) | (390) |
| Deposit paid on acquisition | 22 | (2,000) | - | (2,000) | - |
| Proceeds from sale of financial assets | | 207,517 | 304,015 | 207,517 | 304,015 |
| Proceeds (to)/from related companies | 40 | (1,887) | 1,913 | (1,887) | 1,913 |
| Proceeds on sale of property, plant and equipment | | 45 | 25 | 45 | 25 |
| **NET CASH OUTFLOWS FROM INVESTING ACTIVITIES** | | (32,310) | (38,675) | (32,310) | (38,675) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | | | |
| Proceeds from issue of ordinary shares, net of transaction costs | | - | 45 | - | 45 |
| Interest paid on borrowings | | - | (3,469) | - | - |
| Ordinary dividends paid | | (3,404) | (3,094) | (3,404) | (3,094) |
| **NET CASH OUTFLOWS FROM FINANCING ACTIVITIES** | | (3,404) | (6,518) | (3,404) | (3,049) |
| **Net decrease in cash and cash equivalents** | | (2,559) | (16,362) | (2,506) | (12,172) |
| Cash and cash equivalents at 1 July | | 15,543 | 31,905 | 15,296 | 27,468 |
| **CASH AND CASH EQUIVALENTS AT 30 JUNE** | 18 | 12,984 | 15,543 | 12,790 | 15,296 |

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

## 1. GENERAL INFORMATION

Fidelity Life Assurance Company Limited ('Fidelity Life') (the 'Company' or 'Parent') and its subsidiaries (together called the 'Group') are financial services companies that provide insurance and investment management services. The Company and its subsidiaries are profit oriented entities.

The Company is a limited liability company incorporated and domiciled in New Zealand. The address of its registered office is Level 1, 81 Carlton Gore Road, Newmarket, Auckland, New Zealand.

These consolidated financial statements have been approved for issue by the Board of Directors on 5 September 2013. The Company's owners do not have the power to amend these financial statements after issue.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### (A) BASIS OF PREPARATION

The financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice ('NZ GAAP'). They comply fully with New Zealand Equivalents to International Financial Reporting Standards ('NZ IFRS'), as appropriate for profit oriented entities, and comply with International Financial Reporting Standards ('IFRS').

#### ENTITIES REPORTING

The financial statements include separate financial statements for Fidelity Life Assurance Company Limited, a separate legal entity (the 'Parent'); and the consolidated entity (the 'Group'), consisting of the Company and its subsidiaries.

#### STATUTORY BASE

The Company is registered under the Companies Act 1993 and is an issuer in terms of the Securities Act 1978. The financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 1993 and the Companies Act 1993.

#### HISTORICAL COST CONVENTION

With the exception of the information relating to the Parent's 100% owned subsidiary Fidelity Capital Guaranteed Bond Limited ('FCGBL') these financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain assets and liabilities as stated in specific accounting policies below.

Due to the events occurring in August 2011, detailed in note 17(b), the financial statements of FCGBL have been prepared, and consolidated into the Group accounts, on a realisable value basis.

### (B) PRINCIPLES OF CONSOLIDATION

#### SUBSIDIARIES

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of the Company as at 30 June 2013 and the results of all subsidiaries for the year then ended. The Company and its subsidiaries together are referred to in these financial statements as the Group or the consolidated entity.

Subsidiaries are all those entities over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given and equity instruments issued and liabilities incurred or assumed at the date of exchange. Acquisition related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the profit and loss component of the statements of comprehensive income.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (B) PRINCIPLES OF CONSOLIDATION (CONTINUED)

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

### (C) FOREIGN CURRENCY TRANSLATION

#### FUNCTIONAL AND PRESENTATION CURRENCY

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated and parent financial statements are presented in New Zealand dollars, which is the Company's functional currency and the Group's presentation currency.

#### TRANSACTIONS AND BALANCES

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit and loss component of the statements of comprehensive income.

### (D) SEGMENT REPORTING

An operating segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different to those of other operating segments. Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker ('CODM') who reviews the operating results on a regular basis and makes decisions on resource allocation and assessing performance.

### (E) PREMIUM REVENUE

#### LIFE INSURANCE CONTRACTS

Premiums on life insurance contracts are recognised on an accruals basis except where a policy provides for payment on a specific date, then such premiums are recognised as revenue when due. Unpaid premiums on policies that have deemed to have lapsed at balance date are not recognised as revenue.

#### LIFE INVESTMENT CONTRACTS

Amounts received under life investment contracts are separated into their fee and deposit components. The fee component is recognised as income on an accruals basis and the deposit component is recognised as an increase in the liability for investment contracts.

### (F) INVESTMENT INCOME

#### INTEREST INCOME

Interest income is recognised using the effective interest method.

#### DIVIDEND AND DISTRIBUTIONS

Revenue is recognised when the right to receive payment is established. Dividends from equity securities are recorded as revenue on the ex-dividend date.

#### FAIR VALUE GAINS AND LOSSES

Fair value gains and losses on financial assets at fair value are recognised through the profit and loss component of the statements of comprehensive income.

### (G) FEE AND COMMISSION INCOME

Fee revenue on investment contracts is recognised when the service is provided. To the extent that the service will be provided in future periods, this amount is deferred to the liability for investment contracts and amortised as the services are provided. Commission revenue for which no future service is required is recognised on trade date.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (H) CLAIMS EXPENSE

#### LIFE INSURANCE CONTRACTS

Claims are recognised when the liability to a policyholder has been established or upon notification of the insured event.

#### LIFE INVESTMENT CONTRACTS

Claims under life investment contracts represent withdrawals and surrenders of investment deposits and are recognised as a reduction in the liability for investment contracts.

### (I) EXPENSES

All operating expenses in respect of life insurance or life investment contracts have been apportioned between policy acquisitions, policy maintenance and investment management expenses with regard to the objective when incurring the expense and the outcome achieved.

### (J) POLICY ACQUISITION COSTS

Policy acquisition costs comprise the costs of acquiring new business, including commission, advertising, policy issue and underwriting costs, agency expenses and other sales costs.

#### ACQUISITION COSTS – LIFE INSURANCE CONTRACTS

Where overall product profitability of new business written during the year is expected to support the recovery of acquisition costs incurred in that year, these costs are effectively deferred as an element of life insurance contract liabilities and amortised over the life of the policies written. Unamortised acquisition costs are a component of life insurance contract liabilities. Amortisation of acquisition costs is recognised in the profit and loss component of the statements of comprehensive income as a component of net change in life insurance contract liabilities at the same time as policy margins are released.

#### ACQUISITION COSTS – LIFE INVESTMENT CONTRACTS

Commission that varies with and is directly related to securing new contracts is capitalised as a deferred acquisition cost asset along with an administration and marketing allowance. All other acquisition costs are recognised as expenses in the profit and loss component of the statements of comprehensive income when incurred. The deferred acquisition cost asset is subsequently amortised over the life of the contracts and is recognised in the profit and loss component of the statements of comprehensive income. Unamortised acquisition costs are recorded in deferred acquisition costs on the statements of financial position.

#### MAINTENANCE AND INVESTMENT MANAGEMENT EXPENSES

Maintenance costs are the fixed and variable costs of administering policies subsequent to sale. These include general growth and development costs. Maintenance costs include all operating costs other than acquisition and investment management costs.

Investment management costs are the fixed and variable costs of managing investment funds. Maintenance and investment management costs are recognised in the profit and loss component of the statements of comprehensive income on an accrual basis.

### (K) OUTWARDS REINSURANCE

Premiums ceded to reinsurers under reinsurance contracts are recorded as an outwards reinsurance expense and are recognised over the period of indemnity of the reinsurance contract.

### (L) REINSURANCE RECOVERIES

Reinsurance assets consist of amounts receivable in respect of ceded insurance liabilities and are recognised as revenue. Amounts recoverable from reinsurers are estimated in accordance with the relevant reinsurance contract and in a manner consistent with the outstanding claims.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (M) LIFE INSURANCE BUSINESS

#### CLASSIFICATION

Life insurance contracts are those contracts that transfer significant insurance risk. Life investment contracts are those contracts with no significant insurance risk, but which give rise to a financial asset and/or liability.

A contract with a discretionary participation feature is unbundled where possible so that the deposit component of the contract is treated as a life investment contract and the insurance component of the contract is treated as an insurance contract.

#### LIFE INSURANCE CONTRACT LIABILITIES

Life insurance liabilities ('policyholder liabilities') in the statements of financial position and the increase or decrease in policyholder liabilities in the profit and loss component of the statements of comprehensive income have been calculated in accordance with the New Zealand Society of Actuaries Professional Standard No 3 – Determination of Life Insurance Policy Liabilities ('PS3') which prescribes the Margin on Services ('MoS') basis.

MoS is designed to recognise profits on life insurance policies as services are provided to policyholders and income is received. Profits are deferred and amortised over the life of the policy, whereas losses are recognised immediately. Policy services provided over the lifetime of a contract include the costs of expected claims, maintaining policies and investment management. Profit margins relating to the expected income from providing policy services for each of the major product groupings are used to defer and amortise the profit over the life of the policies. Typically renewal premiums are used as a 'profit carrier' to release profits as services are provided. Policy liabilities are generally determined as the present value of all future expected payments, expenses, taxes and profit margins reduced by the present value of all future expected premiums, except in the case of some investment business where policyholder liabilities are determined as the accumulated benefits to policyholders. Profit margins for participating business are set in relation to the value of supporting assets.

#### MOS PROFIT COMPRISES THE FOLLOWING COMPONENTS:

#### PLANNED MARGINS OF REVENUES OVER EXPENSES

At the time of writing a policy and at each balance date, best estimate assumptions are used to determine all expected future payments and premiums.

#### THE DIFFERENCE BETWEEN ACTUAL AND ASSUMED EXPERIENCE

Where actual experience replicates best estimate assumptions, the expected profit margin will be released to profit over the life of the policy. Experience profits or losses are realised where actual experience differs from best estimate assumptions. Instances giving rise to experience profits or losses include variations in claims, expenses, mortality, discontinuance and investment returns. For example, an experience profit will emerge when the expenses of maintaining all in-force business in a year are lower than the best estimate assumption in respect of those expenses.

#### CHANGES TO UNDERLYING ASSUMPTIONS

Assumptions used for measuring policy liabilities are reviewed each year. Where the review leads to a change in assumptions, the change is deemed to have occurred from the end of the year, except for changes in discount rates which are recognised in the year that the rates are changed. The financial effect of all other changes to the assumptions underlying the measurement of policyholder liabilities made during the reporting period, is recognised in the profit and loss component of the statements of comprehensive income over the future reporting periods during which services are provided to policyholders.

#### LOSS RECOGNITION ON GROUPS OF RELATED PRODUCTS

If, based on best estimate assumptions, written business for a group of related products is expected to be unprofitable, the total expected loss for that related product group is recognised in the profit and loss component of the statements of comprehensive income immediately. When loss making business becomes profitable previously recognised losses are reversed.

#### INVESTMENT EARNINGS ON ASSETS IN EXCESS OF POLICY LIABILITIES

Profits are generated from investment assets which are in excess of those required to meet policyholder liabilities. Investment earnings are directly influenced by market conditions and as such this component of MoS profit will vary from year to year.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (M) LIFE INSURANCE BUSINESS (CONTINUED)

#### PARTICIPATING POLICIES

Policyholder liabilities attributable to participating policies include the value of future planned shareholder profit margins and an allowance for future supportable bonuses. The value of supportable bonuses and planned shareholder profit margins account for all profit on a policy based on best estimate assumptions. Under MoS methodology, the value of supportable bonuses and the shareholder profit margin relating to a reporting year will emerge as expected profit in that year.

#### LIFE INVESTMENT CONTRACT LIABILITIES

Life investment contracts are determined to be either participating or non-participating. A participating contract is eligible for a share of the profits of the returns of the underlying funds invested in.

#### PARTICIPATING

A small amount of life investment contract liabilities are participating investment contracts. The Group establishes a liability equal to the future benefit entitlement to be paid out to the contract holders.

#### NON PARTICIPATING

Life investment contracts that are non-participating are unit-linked and are measured at fair value. The fair value of a unit linked contract is determined using the current unit values that reflect the fair value of the financial assets backing the contract, multiplied by the number of units attributed to the contract holder.

There are a small amount of non-participating contracts that are non-linked and are measured at amortised cost. This is calculated by determining the present value of future expected cash flows payable discounted at the risk free rate of return appropriate to the contract.

### (N) INVESTMENT PROPERTY

Investment property is property that is held for long-term rental yields and is not occupied by the Group. These properties are partly accounted for as property, plant and equipment where partly occupied by the Group (refer to property and equipment policy below). Investment property is carried at its fair value, which is supported by market evidence, as assessed by qualified external valuers. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. Changes in fair values are recorded in the profit and loss component of the statements of comprehensive income in other income.

### (O) PROPERTY AND EQUIPMENT

Owner-occupied properties are held by the Group for use in the supply of services or for its own administrative purposes. These properties are partly accounted for as investment property, to the extent they are occupied by third parties (refer to investment property policy above).

Owner-occupied land and buildings are carried at fair value, based on periodic, but at least triennial, valuations by external independent valuers, less annual subsequent depreciation for buildings. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset, and the net amount is restated to the revalued amount of the asset.

Increases in the carrying amount arising on revaluation of land are credited to revaluation reserves in other comprehensive income. Decreases that offset previous increases of the same asset are charged against revaluation reserves directly in other comprehensive income; all other decreases are charged to the profit and loss component of the statements of comprehensive income. Each year the difference between depreciation based on the revalued carrying amount of the asset charged to the profit and loss component of the statements of comprehensive income and depreciation based on the asset's original cost is transferred from revaluation reserves to retained earnings.

All other items classed as property and equipment within the statements of financial position are carried at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

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

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (O) PROPERTY AND EQUIPMENT (CONTINUED)

Depreciation is calculated on the straight-line method to write down the cost of other assets to their residual values over their estimated useful lives as follows:

| | |
|---|---|
| • Properties building component | 50 years |
| • Building fit out | 8 years |
| • Leasehold improvements | 8 years |
| • Motor vehicles | 5 years |
| • Computer equipment | 4 years |
| • Furniture and office equipment | 5 years |

Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal of property and equipment are determined by comparing the proceeds with the carrying amount and are recognised within other income. Repairs and maintenance are charged to the profit and loss component of the statements of comprehensive income during the financial period in which they are incurred.

### (P) INTANGIBLE ASSETS

#### (i) GOODWILL

Goodwill represents the excess of the cost of an acquisition over the fair value of the Company's share of the net identifiable assets of the acquired business or associate at the date of acquisition. Goodwill on acquisitions of businesses is included in intangible assets. Goodwill acquired in business combinations is not amortised. Instead, goodwill is tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired, and is carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

#### (ii) SOFTWARE

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Employee and contractor costs associated with developing significant, identifiable and unique software products controlled and utilised by the Company and Group are capitalised and treated as intangible assets. These costs are amortised over their estimated useful lives (three to five years).

The amortisation expense, costs associated with minor software development and costs associated with or maintaining computer software programmes are recognised as an expense in the profit and loss component of the statements of comprehensive income as incurred.

#### (iii) ACQUIRED VALUE OF IN-FORCE BUSINESS ('AVIF')

The present value of future profits on a portfolio of life insurance and investment contracts, acquired either directly or through the purchase of a subsidiary, is recognised as an asset. In most cases, this is classified as AVIF but, for non-participating investment contracts, it is included within intangibles. In all cases, the AVIF is amortised over the useful lifetime of the related contracts in the portfolio on a systematic basis. The rate of amortisation is chosen by considering the profile of the additional value of in-force business acquired and the expected depletion in its value. The value of the acquired in-force long-term business is reviewed annually for any impairment in value and any reductions are charged as expenses in the profit and loss component of the statements of comprehensive income. Details of the methodology and assumptions are included in note 28.

### (Q) IMPAIRMENT OF NON-FINANCIAL ASSETS

Assets with definite useful lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment irrespective of whether any circumstances identifying a possible impairment have been identified. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units).

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (R) CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash at banks and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments with less than 90 days' maturity from the date of acquisition. For the purposes of the statements of cash flows, cash and cash equivalents also include bank overdrafts, which are included in payables and other financial liabilities on the statements of financial position.

#### STATEMENT OF CASH FLOWS

The following are the definitions of the terms used in the statements of cash flows:

(i) Operating activities include all transactions and other events that are not investing or financing activities.

(ii) Investing activities are those activities relating to the acquisition, holding and disposal of property, plant and equipment and of investments.

(iii) Financing activities are those activities relating to changes in the equity and debt structure of the Group.

### (S) LEASES

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the profit and loss component of the statements of comprehensive income on a straight line basis over the period of the lease.

### (T) FINANCIAL INSTRUMENTS

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss; and loans and other receivables, covered in note 2(z). The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its investments at initial recognition and re-evaluates this designation at each reporting date.

#### (i) FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss on initial recognition. A financial asset is classified as held for trading if acquired principally for the purpose of selling in the short term. Derivatives are also categorised as held for trading. Assets are designated at fair value through profit or loss if a group of financial assets is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented investment strategy, and information about the group of assets is provided internally on that basis to key management personnel. Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance date.

Purchases and sales of financial assets are recognised on trade date, the date on which the Group commits to purchase or sell the asset. Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all the risks and rewards of ownership.

#### (ii) FAIR VALUES OF FINANCIAL INSTRUMENTS

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes.

The fair values of financial instruments traded in active markets (such as publicly traded derivatives, and trading securities) are based on quoted market prices at the balance date. The quoted market price used for financial assets held by the Company is the current bid price; the appropriate quoted market price for financial liabilities is the current ask price.

If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include reference to the fair values of recent arms length transactions, involving the same instruments or other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

Realised and unrealised gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss category, interest and dividends are included in the profit and loss component of the statements of comprehensive income in the period in which they arise.

The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (T) FINANCIAL INSTRUMENTS (CONTINUED)

#### (iii) DERIVATIVES

Derivative financial instruments include foreign exchange contracts, interest rate futures, currency and interest rate swaps, and currency and interest rate options.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value.

Fair values are obtained from quoted market prices or, if these are not available, by using valuation techniques such as discounted cash flow models or option pricing models.

Changes in the fair value of any derivative instrument are recognised in the profit and loss component of the statements of comprehensive income.

#### (iv) IMPAIRMENT

The Group assesses at each balance date whether there is objective evidence that a financial asset or group of financial assets is impaired.

If the carrying value of an investment is greater than the recoverable amount, the carrying value is reduced through a charge to the profit and loss component of the statements of comprehensive income in the period of impairment.

### (U) PROVISIONS

A provision is recognised in the statements of financial position when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow or resources will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

### (V) CONTINGENT LIABILITY

The Group discloses a contingent liability when it has a possible obligation arising from past events, that will be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the Group's control. A contingent liability is disclosed when a present obligation is not recognised because it is not probable that an outflow of resources will be required to settle an obligation, or the amount of the obligation cannot be measured with sufficient reliability.

### (W) EMPLOYEE BENEFITS

#### (i) WAGES AND SALARIES, ANNUAL LEAVE AND SICK LEAVE

Liabilities for wages and salaries, including non monetary benefits, annual leave and accumulating sick leave expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and measured at the rates paid or payable.

#### (ii) SUPERANNUATION OBLIGATIONS

The Group pays contributions into administered superannuation funds including KiwiSaver. Once the contributions have been paid, the Group, as employer, has no further payment obligations. The Group's contributions are charged to the profit and loss component of the statements of comprehensive income in the year to which they relate and are included in employee benefit expenses.

#### (iii) EMPLOYEE SHARE OWNERSHIP SCHEME

Historically the Group operated an equity-settled share based compensation plan in which the Group offered employees the right to purchase shares at a discount in return for employee services. The discount granted to employees is recognised as an expense over the vesting period with a corresponding increase in equity. At any time during the vesting period the employee has an option to require the Group to repurchase the shares at the lower of cost or fair value. Therefore, the Group recognises a liability at balance date for the amount that the Group can be required to pay to repurchase the shares. Once the vesting period is complete the Group extinguishes the liability and recognises a corresponding increase in equity.

### (X) SHARE CAPITAL

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (Y) DIVIDENDS

Provision is made for the amount of any dividend declared on or before the end of the financial year but not distributed at balance date.

### (Z) LOANS AND OTHER RECEIVABLES

Loans and other receivables are non derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of selling the receivable. The Group's loans and other receivables comprise receivables and cash and cash equivalents in the statements of financial position.

Loans and other receivables are recognised initially at fair value and subsequently measured at amortised cost, less provision for doubtful debts.

A provision for impairment of loans and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of a bad debt provision account, and the amount of the loss is recognised in the profit and loss component of the statements of comprehensive income within other expenses. When a receivable is uncollectible, it is written off against the provision.

#### RESTRUCTURED FINANCIAL ASSETS

Where concessionary terms and conditions on an asset have been formally granted to a customer because of the customer's financial difficulties, and the return on the asset following restructuring is such that a loss is not expected to be incurred, then the asset is to be regarded as a restructured asset.

### (AA) INCOME TAX

The income tax expense comprises both current and deferred tax. Income tax expense is recognised in the profit and loss component of the statements of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to the tax payable in respect of previous years. Deferred tax is recognised using the statements of financial position method, providing for temporary differences between the carrying amounts of assets and liabilities in a transaction that is not a business combination and that affects neither accounting or taxable profit, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date.

A deferred tax asset is recognised for the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised.

Deferred tax assets are set-off against deferred tax liabilities to the extent they relate to income taxes which are legally able to be set-off against each other.

#### LIFE INSURANCE TAX

A new income tax regime was introduced for Life Insurers from 1 July 2010. Tax is payable on investment income allocated to policyholders and on shareholder cash flows (investment income, premiums less claims, less expenses). For the first five years of the new tax regime (1 July 2010 – 30 June 2015) there are concessions which allow most legacy policies to continue being taxed similar to that incurred under the old regime as explained below.

Prior to 1 July 2010 Life Insurers were subject to a special tax regime. Two tax bases were maintained; the life insurer base where tax is calculated on investment income less expenses plus underwriting income, and the policyholder base which seeks to tax benefits as they accrue to policyholders under the policies in the form of claim, surrender and maturity payments and increments in the value of policies. The life insurer paid tax on the higher of the two bases at the company tax rate of 30%. As the life insurer was taxed as proxy for the policyholder, returns to policyholders were tax exempt.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (AB) TRADE AND OTHER PAYABLES

These amounts represent liabilities for goods and services provided to the Group prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

### (AC) BORROWINGS

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the profit and loss component of the statements of comprehensive income over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance date.

### (AD) BORROWING COSTS

Borrowing costs are expensed as incurred.

### (AE) FIDUCIARY ACTIVITIES

Assets and income arising from fiduciary activities, together with related undertakings to return such assets to customers, are excluded from these financial statements where the Group has no contractual rights in the assets.

### (AF) DERECOGNITION AND OFFSET OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

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

- The rights to receive cash flows from the asset have expired;
- The Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third-party under a "pass-through" arrangement; or
- The Group has transferred its rights to receive cash flows from the asset and has either transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Financial assets and liabilities are offset and the net amount reported in the statements of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

### (AG) EARLY ADOPTION OF NEW ZEALAND EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Group has not early adopted any New Zealand Equivalents to International Financial Reporting Standards.

### (AH) STANDARDS, AMENDMENTS AND INTERPRETATIONS ADOPTED DURING YEAR

The following new accounting standards and amendments to standards relevant to the Group have been adopted from 1 July 2012 and have been applied in the preparation of these financial statements. Adoption of the standards has not resulted in any changes to the Groups' reported profit or financial position.

- NZ IAS 1 **Presentation of financial statements** – The amendment requires entities to separate items presented in other comprehensive income into two groups, based on whether they may be recycled to profit or loss in the future. The adoption of this amendment has not affected the measurement of any of the items recognised in the statements of financial position or the profit or loss, however, it has altered the disclosure of these items in the statement of comprehensive income by identifying which items in other comprehensive income may, and which may not, be recycled to profit or loss in the future.
- NZ IAS 12 **Income taxes** – The amendments provide a practical approach for measuring deferred tax liabilities and deferred tax assets when investment property is measured using the fair value model. IAS 12 requires the measurement of deferred tax assets or liabilities to reflect the tax consequences that would follow from the way management expects to recover or settle the carrying of the relevant assets or liabilities, that is through use or through sale. The amendment introduced a rebuttable presumption that investment property which is measured at fair value is recovered entirely by sale. The adoption of this standard has not resulted in any additional disclosures or impacted on the Company's or Groups' reported result or financial position.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### (AI) STANDARDS, AMENDMENTS AND INTERPRETATIONS TO EXISTING STANDARDS THAT ARE NOT YET EFFECTIVE

The following new accounting standards and amendments to standards relevant to the Group are not yet effective and have not yet been applied in preparing the financial standards.

- NZ IFRS 9 **Financial instruments** replaces part of NZ IAS 39 Financial instruments and will be mandatory for the Group's financial statements for the year beginning 1 July 2015. It establishes two primary measurement categories for financial assets: amortised cost and fair value, with classification depending on an entity's business model and the contractual cash flow characteristics of the financial asset. The impact of this standard on the financial statements of the Group has not yet been determined.

  A further amendment to the standard was issued in October 2010 and is mandatory for the Group's financial statements for the year beginning 1 July 2015. The amendment provides an additional presentational requirement for liabilities designated at fair value through profit or loss. Where such a designation is made, the liability will be recorded on the statements of financial position at its full value. However, the fair value movement taken to the profit and loss component of the statements of comprehensive income excludes the effect of credit risk; this is recorded in other comprehensive income (unless recognising own credit in other comprehensive income creates an accounting mismatch). There will be no subsequent reclassification of the amounts in other comprehensive income to profit or loss. The impact of this amendment on the financial statements of the Group has not yet been determined.

- NZ IFRS 10 **Consolidated financial statements** – This standard was issued in May 2011 and replaces all of the guidance on control and consolidation in NZ IAS 27 Consolidated and separate financial statements, and NZ SIC-12 Consolidation – special purpose entities. The standard will be mandatory for the Group's financial statements for the year beginning 1 July 2013. The core principle that a consolidated entity presents a parent and its subsidiaries as if they are a single economic entity remains unchanged, as do the mechanics of consolidation. However, the standard introduces a single definition of control that applies to all entities. It focuses on the need to have both power and rights or exposure to variable returns before control is present. Power is the current ability to direct the activities that significantly influence returns. Returns must vary and can be positive, negative or both. There is also new guidance on participating and protective rights and on agent/principal relationships. While the Group does not expect the new standard to have a significant impact on its composition, it has yet to perform a detailed analysis of the new guidance in the context of its various investees that may or may not be controlled under the new rules.

- NZ IFRS 12 **Disclosure of interests in other entities** – The standard was issued in May 2011 and sets out the required disclosures for entities reporting under the two new standards, IFRS 10 Consolidated Financial Statements and IFRS 11 Joint Arrangements, and replaces the disclosure requirements currently found in IAS 28. The standard will be mandatory for the Group's financial statements for the year beginning 1 July 2013. Application of this standard by the Group will not affect any of the amounts recognised in the financial statements, but may impact the type of information disclosed in relation to the Group's investments.

- NZ IFRS 13 **Fair value measurement** – The standard was released in May 2011 and explains how to measure fair value and aims to enhance fair value disclosures. The Group has yet to determine which, if any, of its current measurement techniques will have to change as a result of the new guidance. It is, therefore, not possible to state the impact, if any, of the new rules on any of the amounts recognised in the financial statements. However, application of the new standard will impact the type of information disclosed in the notes to the financial statements. The Group does not intend to adopt the new standard before its operative date, which means that it would be first applied in the annual reporting period beginning 1 July 2013.

### (AJ) COMPARATIVE INFORMATION

Comparative information has been reclassified in relation to the discontinued operations. For further information refer to note 17.

## 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities and profit within the next financial year are discussed below.

### (A) INSURANCE LIABILITIES – EFFECT OF CHANGES AND ASSUMPTIONS

Policy liabilities arising from life insurance and life investment contracts are calculated at each reporting date using mathematical and statistical models. The valuations are prepared by experienced Fellows of the New Zealand Society of Actuaries on the basis of actuarial methods set out in Professional Standards issued by the New Zealand Society of Actuaries, a full member of the International Actuarial Association. The methodology takes into account the risks and uncertainties of the particular classes of business written.

The key factors that affect the estimation of these liabilities are:

- The cost of providing benefits and administering these contracts;
- Mortality and morbidity experience on life insurance products;
- Persistency experience, which affects the entity's ability to recover the cost of acquiring new business over the lives of the contracts; and
- Other factors such as regulation, competition, interest rates, the performance of the capital markets and general economic conditions affect the level of these liabilities.

The uncertainties surrounding these assumptions means that it is likely that the actual observed claims incidence will vary from the liability estimated at the reporting date.

Refer to note 4 for more detail on the valuation of the policy liabilities and the assumptions applied.

### (B) ACQUIRED VALUE OF IN-FORCE BUSINESS

The balance of acquired value of in-force business ('AVIF') is reviewed for impairment at each reporting period by the Appointed Actuary.

The key factors that affect the estimation of the valuation are:

- The life expectancy of the outstanding life insurance contracts;
- The value of planned profit margins, discounted at a risk adjusted rate of return; and
- The discount rate to use for assessing the value of economic capital.

Where the outcome of the valuation differs adversely against the book value of the AVIF there is an impact to the profit and loss component of the statements of comprehensive income and the AVIF intangible balance recognised on the statements of financial position.

### (C) DEFERRED TAX

Significant judgements relating to the calculation of policyholder liabilities (note 3(a)) also impact the Group and Company's deferred tax assets and liabilities. The Group and Company has taken an assessment of anticipated tax assets and liabilities based on estimates of when additional taxes will be due and benefits will arise.

Where the expected tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the reported profit or loss and current and deferred tax amounts in the period in which such determination is made.

## 4. ACTUARIAL METHODS AND POLICIES

The actuarial reports on policyholder liabilities and solvency reserves for the years ended 30 June 2012 and 30 June 2013 were prepared by the Appointed Actuary, John Smith MSc FNZSA FIAA, and peer reviewed by the Consulting Actuary, Peter Davies BBusSc FNZSA FIAA of Davies Financial and Actuarial Limited.

The results incorporate legacy direct mail policies based on data supplied by a third-party administrator and accounting information maintained by the Company.

The value of the policyholder liabilities has been determined in accordance with PS3 and NZ IFRS 4 Insurance Contracts.

The actuaries have examined the information used for the determination of the liabilities and have satisfied themselves as to the accuracy of the data from which the policyholder liabilities have been determined, and that all policies have been valued accurately.

The accumulation method to determine liabilities has been used for all investment contracts (Gold Medal type policies, group superannuation deposits, Power Saver and bonds). There is no allowance in the policyholder liabilities for deferred acquisition charges on investment contracts. A prospective reserve is held for the potential shortfall if the market value of assets backing Gold Medal policies is insufficient to cover guaranteed maturity benefits.

Assurances, annuities, disability claims in payment and risk contracts have been valued using the projection method as in previous years.

The value of supporting assets for participating policies issued by Farmers Mutual Life Limited is the fund value transferred on 28 February 2007 rolled up with subsequent cash flow and interest, adjusted by any difference between the actual and MoS supportable bonuses at each year end.

The valuation assumptions are based on best estimates for each component in terms of PS3. To determine the best estimates, the actuaries examined observable market data and recent experience of the Company and appropriateness of assuming that the current experience continues.

**Discount Rates:** The 10 year NZ Government bond rate at 30 June 2013 was 4.13% (2012: 3.4%). For the year ended 30 June 2013 a gross discount rate of 4.13% was used (2012: 3.4%).

A gross interest rate of 4.13% was used to value discounted cash flows on renewable risk plans where the policy reserve is negative and level premium risk plans where the policy reserve is positive (2012: 3.4%).

A net rate of interest of 2.97% was used to value non-participating assurances (2012: 2.5%).

A gross rate of interest of 4.13% was used to value claim reserves and provisions for investment guarantees (2012: 3.4%).

Annuities were valued at 2.97% net of tax (2012: 2.5%).

For former Farmers Mutual Life Limited ('FMLL') participating plans, a valuation rate of 3.75% was used (2012: 4.0%). This is derived from expected after-tax return on the assets backing the participating fund.

The solvency reserves are valued in accordance with the Solvency Standard for Life Insurance Business issued by the Reserve Bank of New Zealand in August 2011. The discount rate for the insurance risk capital requirement was 4.13% (before tax) and 2.97% (after tax). Participating plans were valued using the risk free rate of 2.97% (not a higher expected after-tax return on assets). All contracts except annuities, participating business and traditional assurances were valued on a gross basis, assuming no tax charge would arise if the prescribed adverse yield applied. Annuities, participating business and traditional assurances were valued on a net basis.

**Taxation:** Tax is payable on investment income allocated to policyholders and on shareholder cash flows (investment income, premiums less claims, less expenses). This change has been incorporated into the valuation methodology for annuities and participating contracts which were valued on a net basis (2012: net basis). The assumed long-run rate is 28% (2012: 28%).

**Asset Mix:** The current asset mix was assumed to continue into the future.

**Inflation rates:** A rate of 2.5% was used where applicable (2012: 2.5%).

**Profit carriers** (where valued on the projection method)**:**

- Interest earnings for traditional policies
- Claims for mortgage repayment insurance
- Premiums for other policies.

## 4. ACTUARIAL METHODS AND POLICIES (CONTINUED)

**Investment and maintenance expenses:** The maintenance expenses of policies are based on an analysis of existing and projected costs and product margins. Where those expenses relate to life insurance, trauma and disability insurance it has been assumed that those expenses increase at the same rate that premiums increase – according to age rather than the inflation rate.

**Mortality:** Mortality was based on the net reinsurance rates. A selection rebate of 100% (2012: 100%) was assumed in accordance with the actual selection rebate set out in reinsurance treaties. Standard mortality is the reinsurance rates for underwritten business.

For guaranteed acceptance plans mortality is assumed to be 500% of standard mortality for the first five years, falling to 200% of standard from the 10th year (unchanged from 2012).

For former FMLL plans the mortality assumptions were unchanged from 2012:

- 100% of NZ97(5) select for participating business;
- 65% of NZ97(5) select for term insurance; and
- Adjusted reinsurance valuation table for direct mail business.

For limited premium guaranteed acceptance plans mortality is assumed to be 200% of standard throughout (unchanged from 2012).

**Annuitant mortality:** The mortality of annuitants is assumed to follow the IMA92C20 and IFA92C20 standard tables with a reduction in attained age of 5 up to age 55 falling by 1 year for every 10 years of age to nil from age 95 (2012: age reduction 5 years to age 55, falling 1 year every 10 years of age to nil from age 95).

**Morbidity:** Morbidity was based on the net reinsurance rates. A selection rebate of 100% (2012: 100%) was assumed in accordance with the actual selection rebate agreed with reinsurers.

**Rates of discontinuance:** The ultimate discontinuance rates used for life and accelerated critical care and accelerated TPD was 11.5% for policies from year 6 onwards (2012: 11.0%). The assumed discontinuance rate in the first year was 7.0% or 11.5% depending on the level of compulsory spreading. The discontinuance rate during years 2 to 5 of the policy life time is assumed to be 11.0% to 12.0% or 15.5% depending on the minimum proportion of initial commission that is spread (2012: 11.0% to 15.5%).

The ultimate discontinuance rate for stand-alone critical care and stand-alone total and permanent disability ('TPD') was 13.5% for policies in force from year 6 onwards (2012: 13.0%). The assumed discontinuance rate in the first year is 7.5% or 12.0% depending on the level of compulsory spreading. The discontinuance rate during years 2 to 5 of the policy life time is assumed to be 13.0% to 14.5% or 17.5% depending on the minimum proportion of initial commission that is spread (unchanged from 2012).

The ultimate discontinuance rate for income protection was 15.5% for policies in force from year six onwards (2012: 15.0%). The assumed discontinuance rate in the first year was 8.5% or 13.0% depending on the level of compulsory spreading. The discontinuance rate during years 2 to 5 of the policy life time is assumed to be 13.5% to 16.0% or 19.0% to 19.5% depending on the minimum proportion of initial commission that is spread (2012: 14.0% to 19.5%).

The discontinuance rate for traditional whole of life and endowment assurances was assumed to be 5.0%, the same as last year.

Discontinuance rates for the former FMLL plans were based on a recent experience study. Those rates vary by product and duration in force.

**Surrender values:** The surrender value of whole of life and endowment assurances, issued by the former FMLL, is 90% of the net premium reserve with double Zillmer calculated using NZ97(5) mortality table discounted at 4.8%, ignoring any terminal bonus (2012: 4.8%). For legacy assurances issued by Fidelity Life the surrender value is based on the A49/52 ultimate mortality table discounted at 4.5% (same as last year).

There is no exit charge on bonds and power saver (same as last year).

The exit charge on Gold Medal is 5.0%, reducing by 1.0% each year from the policy anniversary four years preceding maturity (same as last year). Policies issued after July 2009 do not have an exit charge.

**Participating business:** For Fidelity Life with-profit assurances it was assumed that the current bonus allocation will continue indefinitely. The bonus is equal to conservative portfolio return on cash deposits plus a cash bonus of 10% of premiums paid.

For former FMLL plans the supportable bonus rate is 0.74% of the sum assured and reversionary bonus (2012: 0.57%). The current bonus declaration was 0.75% (2012: 0.57%).

It is assumed that the policyholder's share of the surplus on the participating pool is 83.3% (2012: 83.3%), which matches the value of supportable assets at date of transfer from Farmers Mutual Group Limited to Fidelity Life.

## 4. ACTUARIAL METHODS AND POLICIES (CONTINUED)

**Profit Margins:** Profit Margins have been incorporated for existing product categories to release those profits arising in the future which are not in relation to the provision of the original acquisition cost as and when those profits are released.

Profit margins were adjusted to ensure that there was no capitalisation of future profits arising from changes to demographic assumptions and rates used in the projection. However, changes to economic and financial assumptions are capitalised.

**Impact of actuarial changes in assumptions:** Under MoS, for life insurance contracts valuations using the projection method, changes in actuarial assumptions are recognised by adjusting the value of future profit margins in life insurance contract liabilities. Future profit margins are released over future periods.

The impact of the assumption changes in the current period on future profit margins in respect of life insurance contracts (excluding new business contracts which are measured using assumptions at the valuation date) are shown below:

### GROUP AND PARENT

| | Effect on Future Profit Margins | Effect on Life Insurance Contract Liabilities | Effect on Future Profit Margins | Effect on Life Insurance Contract Liabilities |
|---|---|---|---|---|
| | 2013 $'000 | 2013 $'000 | 2012 $'000 | 2012 $'000 |
| **ASSUMPTION CHANGE** | | | | |
| Discontinuance rates | (5,133) | - | 7,232 | - |
| Premium rates | (655) | - | (2,975) | - |
| Renewal expenses | (7,831) | - | 202 | - |
| Mortality/Morbidity rates | 7,911 | - | - | - |
| Other modelling changes | 9,224 | - | - | - |
| Discount rate | (10,442) | (2,327) | 17,857 | (4,837) |

During the financial year the software used for the projection of future cash flows was upgraded to a new platform. During the upgrade process implicit historic assumptions were revised to align closer to current business processes.

### SENSITIVITY ANALYSIS OF LIFE INVESTMENT CONTRACTS

The following table shows the changes in the value of future margins, policy liability and profit at 30 June if actuarial assumptions change as follows:

### GROUP AND PARENT

2013

| | Change in Assumption | Effect on Future Margins | Effect on Policy Liability | Effect on Profit (before tax) |
|---|---|---|---|---|
| | | $'000 | $'000 | $'000 |
| Lapses | Decrease by 10% | - | - | (80) |
| Expenses | Increase by $1 million | - | - | (1,000) |

2012

| | Change in Assumption | Effect on Future Margins | Effect on Policy Liability | Effect on Profit (before tax) |
|---|---|---|---|---|
| | | $'000 | $'000 | $'000 |
| Lapses | Decrease by 10% | - | - | (52) |
| Expenses | Increase by $1 million | - | - | (1,000) |

## 4. ACTUARIAL METHODS AND POLICIES (CONTINUED)

### SENSITIVITY ANALYSIS OF LIFE INSURANCE CONTRACTS

Refer to note 5(B) for sensitivity analysis for life insurance contracts.

### ASSETS BACKING LIFE INSURANCE AND LIFE INVESTMENT BUSINESS

All assets in wholesale unit trusts and segregated mandates are marked to market by external wholesale fund managers that primarily invest in investment grade listed securities.

Directly held investments comprise Property, Mortgages and subordinated debt issued by Fidelity Capital Guaranteed Bond Limited. Property is valued annually by an independent chartered surveyor. Mortgages are valued at outstanding balance less provision for bad debts. At 30 June 2013 the value of the subordinated debt issued by FCGBL on a realisable basis is $nil (2012: $nil).

The carrying value of the assets backing life insurance and life investment contracts is as follows:

**GROUP AND PARENT**

| | Life Investment | | Life Insurance | |
|---|---|---|---|---|
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Loans | 18,242 | 17,794 | 7,819 | 11,606 |
| Debt securities | 100,404 | 90,369 | 11,524 | 12,780 |
| Equity securities | 109,409 | 93,830 | 2,010 | - |
| Other investments | 87,798 | 75,931 | 109,562 | 103,545 |
| Investment property | 9,083 | 8,531 | 1,120 | 744 |
| Property, plant and equipment | 8,055 | 6,728 | 2,066 | 2,554 |
| Cash and cash equivalents | 5,223 | 5,766 | 7,567 | 9,530 |
| Other receivables | - | - | 5,459 | 3,046 |
| Assets arising from reinsurance recoveries | - | - | 12,091 | 10,347 |
| Investment in subsidiaries | - | - | 8 | 8 |
| Income tax asset | - | - | 3,881 | 2,560 |
| Deferred tax assets | - | - | 17,090 | 15,102 |
| Deferred acquisition costs – investment | - | - | 6 | 867 |
| Intangible assets | - | - | 4,283 | 4,922 |
| **Total assets backing** | 338,214 | 298,949 | 184,486 | 177,611 |

The asset portfolios linked to life investment contracts are determined by policyholders, who stipulate the respective portfolio funds to invest in at the time of investment, and subsequent transfers between portfolios.

The assets of FCGBL do not back the life investment and life insurance business, and as such are not included in this analysis.

## 5. RISK MANAGEMENT

### RISK MANAGEMENT FRAMEWORK

The Board of Directors (the 'Board') acknowledges the need for the continued maintenance of a high standard of corporate governance practices and ethical conduct by all directors and employees of Fidelity Life.

The Board of Directors has adopted the Financial Markets Authority (formally Securities Commission) 'Corporate Governance in New Zealand Principles and Guidelines' as a framework against which the Board monitors and reviews its corporate governance. The Board has also adopted the Code of Proper Practice for Directors of the New Zealand Institute of Directors.

The Board has formally delegated to the Chief Executive Officer the day to day management of the Group. The Chief Executive Officer recommends to the Board changes in the business, performance, goals, strategies and plans of the Group.

The Board has in place an integrated framework of controls designed to safeguard the Group's assets and interests and to ensure the integrity of its reporting.

The Board has established a number of standing committees that focus on specific areas of the Board's responsibilities. The committees currently constituted are:

- **Audit & Risk Committee** – established as a link between the Board and external auditors. Provides independent oversight of the effectiveness of the Company's financial reporting and risk management processes.
- **Nomination Committee** – established to assist in the planning the Board's composition and the appointment of new directors.
- **Remuneration Committee** – established to assist the Board with the remuneration structures for the Company's Chief Executive Officer and senior executives.

The Board's committees operate under the same rules of conduct and procedure as the Board and provide a framework for efficient decision making. The Board's committees are subordinate to the Board which retains overall responsibility for decision making.

Under Reserve Bank of New Zealand ('RBNZ') requirements, all insurers who wish to continue to operate in New Zealand are required to have a full licence prior to 7 September 2013. Fidelity Life was granted a full licence on 2 August 2013. The Company has an A- (Excellent) credit rating from A.M. Best, an approved credit rating agency.

Fidelity Life has a formalised risk management programme. The Company's risk management programme is supported by four key components:

(i) The risk management policy states the objectives of the risk management framework and strategy; and identifies who is responsible for the various risk management activities, including oversight, implementation and assessment of effectiveness.

(ii) The risk management framework details how the company ensures effective risk management is real and reflected in the operational activities of the Company.

(iii) The risk management strategy forms part of the annual strategic and business planning documents, identifying the key risks to achieving strategic objectives and the risk management initiatives that need to be planned and budgeted for. The risk management strategy is updated annually, ensuring that the Company continues to focus on relevant and current risks.

(iv) The risk register allows Board and senior management to critically evaluate if the risk management process is effectively identifying and addressing exposures. The risk register continuously evolves as risks are identified, monitored and treated.

The risk management programme is periodically reviewed to ensure the effectiveness of the overall risk management programme.

The business risk assessment estimates the consequences from adverse events and the likelihood that such adverse events might occur. The effectiveness of measures to mitigate the impact of adverse events or reduce the chance of adverse events is assessed against market norms and best practice. The controls for all identified risks are deemed to be at least adequate.

The Board has also appointed an Investment Committee to oversee the investments in line with the Statement of Investment Policy and Objectives ('SIPO') that is approved by the Board.

The Appointed Actuary submits an annual Financial Condition Report ('FCR') to the Board that encompasses the items specified in section 6.3 of the Reserve Bank of New Zealand's 'Solvency Standard for Life Insurance Business' as well as the New Zealand Society of Actuaries Professional Standards. The FCR examines all matters material to the financial condition of the Company and makes recommendations to maintain and enhance the Company's financial strength. The Board reviews the FCR and as appropriate approves and implements the recommendations of the Appointed Actuary. The Appointed Actuary submits an update at half year.

## 5. RISK MANAGEMENT (CONTINUED)

Distributors need to be Authorised Financial Advisers to provide personalised advice on investment products. Distributors need to be Registered Financial Advisers or Authorised Financial Advisers to provide advice on insurance products. Fidelity Life does not accept business that is submitted via advisers who are not permitted to provide such advice under the legislation. The Company is a member of the Insurance & Savings Ombudsman Scheme Inc. (ISO) dispute resolution scheme.

Risk is categorised as follows:

- Market
- Insurance
- Liquidity
- Credit
- Fair values
- Capital management

### A. MARKET RISK

Market risk is the risk of changes in the fair value of financial instruments from fluctuations in foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (price risk), whether such a change in price is caused by factors specific to an individual financial instrument or to its issuer, or to factors affecting all financial instruments traded in a market.

For each of the major components of market risk, the Company has put in place procedures to set out how each risk should be managed and monitored, and the approach to setting an appropriate risk appetite. The management of market risk is undertaken by the Investment Committee which is responsible for managing market risk, and a number of investment related risks.

Most investment contracts are linked to the underlying performance of asset portfolios. The Investment Committee oversees the selection of wholesale managers, construction of wholesale mandates and asset allocation within the permitted guidelines of the SIPO. The financial impact from changes in market risk is managed by the fund managers, however, market risk is borne by the policyholder.

There is a maturity guarantee provided under the Gold Medal range of policies. The Company is liable to make good any shortfall between the market value of assets and the minimum rate of return at maturity. The solvency reserve allows for a one-off shock to asset values (consistent with credit, equity and property ('CEP') risk capital charges defined in the RBNZ solvency standard) and long-term risk-free yield.

The assets that are not required to meet linked liabilities are invested defensively. However, each investment portfolio has a small proportion of non-linked funds to provide immediate liquidity for any policyholder that wishes to withdraw or switch. Prescribed asset risk capital charges are maintained to meet currency, interest rate and price risks defined in the RBNZ solvency standard for life insurance business.

#### (i) CURRENCY RISK

Currency risk is the risk of changes in the fair value of financial instruments from fluctuations in exchange rates. Foreign currency risk arises as the parent and its subsidiaries have assets invested in foreign currencies.

The Group's SIPO policy requires that the fund managers maintain sufficient assets to meet currency liabilities. Therefore, the Group limits its exposures regardless of foreign currency movements.

The Investment Committee meets with the currency adviser every quarter to determine the appropriate levels of forward currency contracts to enter into. These contracts are implemented by the Bank of New Zealand ('BNZ').

The forward foreign currency contracts are accounted for at fair value through profit or loss as the Group does not apply hedge accounting.

## 5. RISK MANAGEMENT (CONTINUED)

### A. MARKET RISK (CONTINUED)

**Concentrations**

The following table shows the assets of the Group (policyholder and shareholder) denominated in foreign currency:

| | Group | | Parent | |
|---|---|---|---|---|
| | 2013 NZ$'000 | 2012 NZ$'000 | 2013 NZ$'000 | 2012 NZ$'000 |
| NON-MONETARY ASSETS | | | | |
| AUD | 134,896 | 108,355 | 134,896 | 108,355 |
| GBP | 28,847 | 17,034 | 28,847 | 17,034 |
| USD | 4,012 | 15,696 | 4,012 | 15,696 |
| TOTAL ASSETS IN FOREIGN CURRENCY | 167,755 | 141,085 | 167,755 | 141,085 |
| PERCENTAGE OF TOTAL ASSETS | 28.5% | 26.1% | 32.1% | 29.6% |

The Group also holds forward exchange contracts as detailed in note 21.

**Sensitivity analysis**

The following table, which includes only shareholder investments, shows the change in profit after tax and the effect on equity if there was an increase/decrease in the foreign exchange rates of 10% with all other variables assumed unchanged:

**Group and Parent**

| | +10% change in foreign exchange rates | | | | -10% change in foreign exchange rates | | | |
|---|---|---|---|---|---|---|---|---|
| | Impact on post tax profit | | Impact on equity | | Impact on post tax profit | | Impact on equity | |
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| AUD | 14 | 204 | 14 | 204 | (11) | (167) | (11) | (167) |
| GBP | 123 | 75 | 123 | 75 | (100) | (61) | (100) | (61) |
| USD | 14 | 99 | 14 | 99 | (11) | (81) | (11) | (81) |
| | 151 | 378 | 151 | 378 | (122) | (309) | (122) | (309) |

**(ii) PRICE RISK**

Price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices.

Price risk is incurred for directly held securities and exchange traded funds. Price risk also exists for wholesale unit-trusts, common trust funds and wholesale investment mandates or Portfolio Investment Entities ('PIE') based on movements in the underlying securities within the wholesale vehicles.

The Investment Committee delegates active monitoring of its investments owned directly by the Company. Concentrations of specific holdings are also managed and monitored by the Company's fund managers.

Most price risk is borne by policyholders who have selected the investment portfolio that invests in a particular mix of assets. The unit-price of investment portfolios includes the full and immediate change in market values of underlying investments.

Shareholders' funds provide security to meet adverse fluctuations in insurance risks rather than investment market risks. Thus, shareholders' funds are invested defensively to minimise price risk.

## 5. RISK MANAGEMENT (CONTINUED)

### A. MARKET RISK (CONTINUED)

**Sensitivity analysis**

The following table shows the change in profit after tax and the effect on equity if there was an increase/decrease in the market value of investments of +/- 10% with all other variables assumed unchanged:

**Group and Parent**

| | +10% change in price variable | | | | -10% change in price variable | | | |
|---|---|---|---|---|---|---|---|---|
| | Impact on post tax profit | | Impact on equity | | Impact on post tax profit | | Impact on equity | |
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Change in the Market Value of: | | | | | | | | |
| New Zealand and Australian Shares | 142 | 184 | 142 | 184 | (142) | (184) | (142) | (184) |
| International Shares | 47 | 237 | 47 | 237 | (47) | (237) | (47) | (237) |
| New Zealand Property | 34 | 139 | 34 | 139 | (34) | (139) | (34) | (139) |
| Bond Options (Derivatives) | 67 | 375 | 67 | 375 | (67) | (375) | (67) | (375) |
| | 290 | 935 | 290 | 935 | (290) | (935) | (290) | (935) |

### (iii) INTEREST RATE RISK

Interest rate risk is the risk of loss to the Group arising from adverse changes in interest rates.

**Fair value interest rate risk**

Fair value interest rate risk arises from the potential for a change in interest rates to cause a fluctuation in the fair value of financial instruments and life insurance contract liabilities.

**Cash flow interest rate risk**

Cash flow interest rate risk is the potential for a change in interest rates to change interest expense and interest income in future periods.

The Group's investments that are subject to fair value interest rate risk includes fixed interest securities and put and call options that are taken out against overseas interest rates.

Investments held in mortgages and policy loans are subject to cash flow interest rate risk.

Most interest rate risk is borne by policyholders who have selected the investment portfolio that invests in a particular mix of assets. The unit-price of investment portfolios includes the full and immediate change in market values of underlying investments.

Shareholders' funds provide security to meet adverse fluctuations in insurance risks rather than investment market risks. Thus, shareholders' funds are invested defensively to minimise interest rate risk.

## 5. RISK MANAGEMENT (CONTINUED)

### A. MARKET RISK (CONTINUED)

**Sensitivity analysis**

The following table shows the change in profit and the effect on equity if there was an increase/decrease in interest rates of 1% with all other variables assumed unchanged:

**Group**

| | +1% change in interest rates | | | | -1% change in interest rates | | | |
|---|---|---|---|---|---|---|---|---|
| | Impact on post tax profit | | Impact on equity | | Impact on post tax profit | | Impact on equity | |
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Cash and Cash Equivalents | 56 | 70 | 56 | 70 | (56) | (70) | (56) | (70) |
| Loans | 56 | 84 | 56 | 84 | (56) | (84) | (56) | (84) |
| NZ Debt Securities | (5,656) | (1,705) | (5,656) | (1,705) | 5,799 | 1,853 | 5,799 | 1,853 |
| International Debt Securities | (17) | (369) | (17) | (369) | 19 | 393 | 19 | 393 |
| | (5,561) | (1,920) | (5,561) | (1,920) | 5,706 | 2,092 | 5,706 | 2,092 |

**Parent**

| | +1% change in interest rates | | | | -1% change in interest rates | | | |
|---|---|---|---|---|---|---|---|---|
| | Impact on post tax profit | | Impact on equity | | Impact on post tax profit | | Impact on equity | |
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Cash and Cash Equivalents | 54 | 68 | 54 | 68 | (54) | (68) | (54) | (68) |
| Loans | 56 | 84 | 56 | 84 | (56) | (84) | (56) | (84) |
| NZ Debt Securities | (5,656) | (1,705) | (5,656) | (1,705) | 5,799 | 1,853 | 5,799 | 1,853 |
| International Debt Securities | (17) | (369) | (17) | (369) | 19 | 393 | 19 | 393 |
| | (5,563) | (1,922) | (5,563) | (1,922) | 5,708 | 2,094 | 5,708 | 2,094 |

### B. INSURANCE RISK

Insurance exists to provide peace of mind to people who will be compensated for part or all of a financial loss that is relatively infrequent, strikes at random and is potentially devastating for an individual or their family.

The Company pools the risks of tens of thousands of policyholders, each of whom pays a relatively modest premium for their insurance cover. The relatively few claims are met from the many premiums paid into the insurance pool.

The Appointed Actuary sets premium rates based on the expected incidence of claims, costs of running the insurance pool (including commission to sales intermediaries) and contingency margin to cover the variability risk and cost of capital that provides solvency support for the insurance pool.

The exposure of the Company to variation in the incidence of claims and concentration of risk is controlled through the use of reinsurance that caps the total amount payable on each claim to a predefined amount of risk retained on each individual person.

The Company actively manages its exposure under its retention agreements with its reinsurers. Levels of retained risk are increased or decreased to reflect changes in the Company's retention risk appetite.

## 5. RISK MANAGEMENT (CONTINUED)

### B. INSURANCE RISK (CONTINUED)

The exposure of the Company to mis-estimation of the expected incidence of claims is controlled by setting rates based on actuarial research undertaken by international reinsurance companies to derive pure risk premium rates.

Most premium rates are adjustable every year so any systemic strain can be rectified. Premium rates are not adjusted for random fluctuations.

The analysis of recent experience for each component in the insurance premiums is included in the annual FCR and half-yearly actuarial valuation reports. Profitability is estimated from monthly management accounts.

**Sensitivity analysis**

The analysis assumes that the value of liabilities will not be affected by changes in demographic assumptions.

The following table shows the changes in the value of future planned margins (assuming no compensating changes in future premiums), policy liability (including future profit margins) and surplus at 30 June if actuarial assumptions change as follows:

2013

| | | Future Margins | Policy Liability | Profit |
|---|---|---|---|---|
| | | $'000 | $'000 | $'000 |
| Discount rate/inflation rate | Increase by 0.25% | (2,249) | (552) | 358 |
| | Decrease by 0.25% | 2,334 | 629 | (429) |
| Mortality/Morbidity | Increase by 10% | (57,247) | 120 | (487) |
| | Decrease by 10% | 14,905 | (110) | 526 |
| Lapses | Increase by 10% | (22,521) | - | - |
| | Decrease by 10% | 27,732 | - | - |
| Expenses | Increase by 10% | (21,325) | 5 | - |
| | Decrease by 10% | 21,325 | (5) | - |
| Terminations | Increase by 10% | - | (312) | 312 |
| | Decrease by 10% | - | 329 | (329) |

2012

| | | Future Margins | Policy Liability | Profit |
|---|---|---|---|---|
| | | $'000 | $'000 | $'000 |
| Discount rate/inflation rate | Increase by 0.25% | (3,301) | (471) | 249 |
| | Decrease by 0.25% | 3,435 | 548 | (318) |
| Mortality/Morbidity | Increase by 10% | (56,210) | 105 | (483) |
| | Decrease by 10% | 14,554 | (90) | 518 |
| Lapses | Increase by 10% | (27,193) | - | - |
| | Decrease by 10% | 33,741 | - | - |
| Expenses | Increase by 10% | (20,101) | 6 | - |
| | Decrease by 10% | 20,101 | (6) | - |
| Terminations | Increase by 10% | - | (333) | 333 |
| | Decrease by 10% | - | 352 | (352) |

## 5. RISK MANAGEMENT (CONTINUED)

### B. INSURANCE RISK (CONTINUED)

| Variable | Impact of a movement in the underlying variable |
|---|---|
| **Mortality risk** | For insurance contracts providing death benefits, greater mortality rates would lead to higher levels of claims, increasing associated claims cost and therefore reducing profit and shareholders' equity. |
| **Morbidity risk** | The cost of claims related to health depends on both the incidence of policyholders being diagnosed with a critical illness or becoming temporarily or permanently disabled and the duration which they remain temporarily or permanently disabled. Higher than expected incidence and duration would be likely to increase claim costs, reducing profit and shareholders' equity. |
| **Expense risk** | An increase in the level or inflationary growth of expenses over assumed levels will decrease profit and shareholders' equity. |
| **Termination risk** | The impact of the termination rate assumption depends on a range of factors including the type of contract, the surrender value basis (where applicable) and the duration in force. |

### C. LIQUIDITY RISK

Management of liquidity risk is designed to ensure that the Group and Company have the ability to meet their financial obligations as they fall due at a reasonable cost.

The Group is exposed to daily calls on its available cash resources from maturing policies, policy claims, surrenders and cashing in or switching between investment portfolios.

Through the application of a liquidity management policy the Group seeks to maintain sufficient resources to meet its obligations as they fall due.

Investment durations are matched with the expected timeframes of liabilities to ensure that liabilities are adequately covered.

Each investment portfolio has a small proportion of non-linked funds to provide immediate liquidity for any policyholder that wishes to withdraw funds or switch portfolios.

**Maturity analysis**

The table below shows the maturity of the contractual undiscounted cash flows of the Group and Company's financial assets and liabilities. Where the counterparty has discretion in requesting payment, liabilities have been classified according to the earliest time period in which the Group may be required to pay. Cash flows on derivative financial instruments are analysed on a gross basis, unless they are settled net.

In relation to FCGBL (included in Group figures) the inputs have been prepared on the basis of expected cash flow maturities post the Close Out of Fund.

## 5. RISK MANAGEMENT (CONTINUED)

### C. LIQUIDITY RISK (CONTINUED)

**Group 2013**

| | Less than 1 year | Between 1 & 2 years | Between 2 & 5 years | Over 5 years | Total | Carrying amount |
|---|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 |
| **Financial assets:** | | | | | | |
| Cash and cash equivalents | 12,984 | - | - | - | 12,984 | 12,984 |
| Loans and other receivables | 7,307 | 4,672 | 6,939 | 24,601 | 43,519 | 28,188 |
| Financial assets at fair value through profit or loss | 380,439 | 18,406 | 59,529 | 42,959 | 501,333 | 485,463 |
| Derivative financial instruments | 1,310 | 560 | 347 | 722 | 2,939 | 857 |
| Assets arising from reinsurance contracts | 12,091 | - | - | - | 12,091 | 12,091 |
| | 414,131 | 23,638 | 66,815 | 68,282 | 572,866 | 539,583 |
| **Financial liabilities:** | | | | | | |
| Policyholder liabilities – investment (non-participating) contracts | 146,810 | 11,969 | 32,012 | 147,423 | 338,214 | 338,214 |
| Policyholder liabilities – insurance contracts | 936 | 826 | 2,023 | 8,167 | 11,952 | (30,595) |
| Payables and other financial liabilities | 26,978 | - | - | - | 26,978 | 26,978 |
| Derivative financial instruments | 2,557 | - | - | - | 2,557 | 2,557 |
| Interest bearing liabilities | 65,865 | - | - | - | 65,865 | 65,778 |
| | 243,146 | 12,795 | 34,035 | 155,590 | 445,566 | 402,932 |

**Group 2012**

| | Less than 1 year | Between 1 & 2 years | Between 2 & 5 years | Over 5 years | Total | Carrying amount |
|---|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 |
| **Financial assets:** | | | | | | |
| Cash and cash equivalents | 15,543 | - | - | - | 15,543 | 15,543 |
| Loans and other receivables | 7,207 | 2,697 | 10,798 | 29,332 | 50,034 | 31,435 |
| Financial assets at fair value through profit or loss | 284,570 | 84,652 | 62,766 | 26,529 | 458,517 | 437,228 |
| Derivative financial instruments | 2,721 | - | - | - | 2,721 | 2,721 |
| Assets arising from reinsurance contracts | 10,347 | - | - | - | 10,347 | 10,347 |
| | 320,388 | 87,349 | 73,564 | 55,861 | 537,162 | 497,274 |
| **Financial liabilities:** | | | | | | |
| Policyholder liabilities – investment (non-participating) contracts | 119,011 | 12,373 | 28,911 | 138,654 | 298,949 | 298,949 |
| Policyholder liabilities – insurance contracts | 6,344 | 2,538 | 4,328 | 12,309 | 25,519 | (17,054) |
| Payables and other financial liabilities | 27,708 | 17 | - | - | 27,725 | 27,714 |
| Derivative financial instruments | 173 | - | - | - | 173 | 173 |
| Interest bearing liabilities | - | 65,865 | - | - | 65,865 | 63,660 |
| | 153,236 | 80,793 | 33,239 | 150,963 | 418,231 | 373,442 |

## 5. RISK MANAGEMENT (CONTINUED)

### C. LIQUIDITY RISK (CONTINUED)

Parent 2013

| | Less than 1 year | Between 1 & 2 years | Between 2 & 5 years | Over 5 years | Total | Carrying amount |
|---|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 |
| **Financial assets:** | | | | | | |
| Cash and cash equivalents | 12,790 | - | - | - | 12,790 | 12,790 |
| Loans and other receivables | 7,307 | 4,672 | 6,939 | 24,601 | 43,519 | 28,188 |
| Financial assets at fair value through profit or loss | 314,739 | 18,406 | 59,529 | 42,959 | 435,633 | 419,850 |
| Derivative financial instruments | 1,310 | 560 | 347 | 722 | 2,939 | 857 |
| Assets arising from reinsurance contracts | 12,091 | - | - | - | 12,091 | 12,091 |
| | 348,237 | 23,638 | 66,815 | 68,282 | 506,972 | 473,776 |
| **Financial liabilities:** | | | | | | |
| Policyholder liabilities – investment (non-participating) contracts | 146,810 | 11,969 | 32,012 | 147,423 | 338,214 | 338,214 |
| Policyholder liabilities – insurance contracts | 936 | 826 | 2,023 | 8,167 | 11,952 | (30,595) |
| Payables and other financial liabilities | 26,957 | - | - | - | 26,957 | 26,957 |
| Derivative financial instruments | 2,557 | - | - | - | 2,557 | 2,557 |
| | 177,260 | 12,795 | 34,035 | 155,590 | 379,680 | 337,133 |

Parent 2012

| | Less than 1 year | Between 1 & 2 years | Between 2 & 5 years | Over 5 years | Total | Carrying amount |
|---|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 |
| **Financial assets:** | | | | | | |
| Cash and cash equivalents | 15,296 | - | - | - | 15,296 | 15,296 |
| Loans and other receivables | 7,207 | 2,697 | 10,798 | 29,332 | 50,034 | 31,435 |
| Financial assets at fair value through profit or loss | 284,570 | 18,952 | 62,766 | 26,529 | 392,817 | 373,734 |
| Derivative financial instruments | 2,721 | - | - | - | 2,721 | 2,721 |
| Assets arising from reinsurance contracts | 10,347 | - | - | - | 10,347 | 10,347 |
| | 320,141 | 21,649 | 73,564 | 55,861 | 471,215 | 433,533 |
| **Financial liabilities:** | | | | | | |
| Policyholder liabilities – investment (non-participating) contracts | 119,011 | 12,373 | 28,911 | 138,654 | 298,949 | 298,949 |
| Policyholder liabilities – insurance contracts | 6,344 | 2,538 | 4,328 | 12,309 | 25,519 | (17,054) |
| Payables and other financial liabilities | 27,643 | - | - | - | 27,643 | 27,643 |
| Derivative financial instruments | 173 | - | - | - | 173 | 173 |
| | 153,171 | 14,911 | 33,239 | 150,963 | 352,284 | 309,711 |

## 5. RISK MANAGEMENT (CONTINUED)

### D. CREDIT RISK

Credit risk is the risk of loss in the value of financial assets due to counterparties failing to meet all or part of their obligations.

In respect of Group assets, the Group manages credit risk by monitoring exposures entered into by the fund managers and assets held directly by the Group. Financial assets are not to fall outside of a preset range.

The following table provides information regarding the aggregated credit risk exposure for financial assets with external credit ratings. Other financial asset categories are unrated.

**Group 2013**

| | AAA+ to A- | BBB+ to BBB- | BB+ to B- | Unrated | Total |
|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 |
| Cash and cash equivalents | 12,984 | - | - | - | 12,984 |
| Assets arising from reinsurance contracts | 12,091 | - | - | - | 12,091 |
| Debt securities | 142,137 | 27,982 | 775 | 6,647 | 177,541 |
| Derivatives | 857 | - | - | - | 857 |
| Loans | - | - | - | 26,984 | 26,984 |
| | 168,069 | 27,982 | 775 | 33,631 | 230,457 |

**Group 2012**

| | AAA+ to A- | BBB+ to BBB- | BB+ to B- | Unrated | Total |
|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 |
| Cash and cash equivalents | 15,543 | - | - | - | 15,543 |
| Assets arising from reinsurance contracts | 10,347 | - | - | - | 10,347 |
| Debt securities | 131,036 | 22,998 | 1,275 | 11,334 | 166,643 |
| Derivatives | 2,721 | - | - | - | 2,721 |
| Loans | - | - | - | 30,174 | 30,174 |
| | 159,647 | 22,998 | 1,275 | 41,508 | 225,428 |

Included in the statement of financial position are unitised funds of $196,503,000 (2012: $176,755,000). Unitised products are invested within the guidelines of the Group's SIPO. The SIPO requires investments to be well diversified, outlines minimum credit rating applicable dependent on type of asset and the maximum exposure to class of investment.

## 5. RISK MANAGEMENT (CONTINUED)

### D. CREDIT RISK (CONTINUED)

**Parent 2013**

| | AAA+ to A- | BBB+ to BBB- | BB+ to B- | Unrated | Total |
|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 |
| Cash and cash equivalents | 12,790 | - | - | - | 12,790 |
| Assets arising from reinsurance contracts | 12,091 | - | - | - | 12,091 |
| Debt securities | 76,524 | 27,982 | 775 | 6,647 | 111,928 |
| Derivatives | 857 | - | - | - | 857 |
| Loans | - | - | - | 26,984 | 26,984 |
| | 102,262 | 27,982 | 775 | 33,631 | 164,650 |

**Parent 2012**

| | AAA+ to A- | BBB+ to BBB- | BB+ to B- | Unrated | Total |
|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 |
| Cash and cash equivalents | 15,296 | - | - | - | 15,296 |
| Assets arising from reinsurance contracts | 10,347 | - | - | - | 10,347 |
| Debt securities | 67,542 | 22,998 | 1,275 | 11,334 | 103,149 |
| Derivatives | 2,721 | - | - | - | 2,721 |
| Loans | - | - | - | 30,174 | 30,174 |
| | 95,906 | 22,998 | 1,275 | 41,508 | 161,687 |

Included in the statement of financial position are unitised funds of $196,503,000 (2012: $176,755,000). Unitised products are invested within the guidelines of the Group's SIPO. The SIPO requires investments to be well diversified, outlines minimum credit rating applicable dependent on type of asset and the maximum exposure to class of investment.

#### CONCENTRATION OF CREDIT RISK

Concentration of credit risk exists if a number of counterparties are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic conditions.

The concentration of credit risk on financial assets is generally the carrying amount, net of any provisions for doubtful debts. The Group does not expect any investment or reinsurance counterparties to fail to meet their obligations given their high credit ratings.

#### ASSET QUALITY

An ageing analysis of loans receivable is shown below. All loans are deemed not to be impaired unless specifically disclosed as such:

| | Group and Parent | |
|---|---|---|
| | 2013<br>$'000 | 2012<br>$'000 |
| Current | 16,537 | 17,933 |
| Less than three months | 4,234 | 3,917 |
| Between three and six months | 1,821 | 2,933 |
| Greater than six months past due | 2,006 | 2,253 |
| Impaired | 2,386 | 3,138 |
| **Total due** | 26,984 | 30,174 |

As at 30 June 2013 $1.0 million (2012: $2.8 million) of loans receivable would have been past due at balance date, however their terms were re-negotiated.

## 5. RISK MANAGEMENT (CONTINUED)

### D. CREDIT RISK (CONTINUED)

**Maximum exposure to credit risk**

The maximum exposure relating to each class of financial asset is its carrying value.

**Collateral held as security**

Loans are secured in a variety of ways, including mortgages over property, life insurance cover, a charge over future business income, a personal guarantee or a charge over other assets. For mortgages, which comprise 83% of the loans portfolio, the Company policy is for a maximum loan to value ratio of less than 75%. In the event of a default, the Group is able to sell or repledge the mortgage collateral held. In the case of policy loans, the loan is secured by the underlying policy. If the outstanding loan exceeds the level of security held it is actively managed to reduce the Group's exposure. At present the fair value of all security across the entire portfolio is not calculated.

**Collateral taken possession of**

The Group did not hold any collateral which it was permitted to sell or repledge in the absence of default, at the end of either 2013 or 2012.

**Provision for impairment of receivables**

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Carrying amount at the beginning of the year | 774 | 536 |
| Provisions recognised during the year | 366 | 353 |
| Balances written off during the year | - | (31) |
| Unused amounts reversed | (217) | (84) |
| **Carrying amount at the end of the year** | 923 | 774 |

The provisions above are all made against specific loans and receivables where it is considered there have been events making full repayment unlikely. There have been no collective provisions included (2012: nil).

The creation and release of the provision for impaired receivables has been included in other expenses in the profit and loss component of the statements of comprehensive income. Amounts charged to the allowance account are generally written off when there is no expectation of recovering additional cash.

### E. FAIR VALUES

The Group classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

(i) Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1).

(ii) Inputs other than quoted prices included within level 1 that are observable for the assets or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2).

(iii) Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The level in the fair value hierarchy within which the fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. For this purpose, the significance of an input is assessed against the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a level 3 measurement. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgement, considering factors specific to the asset or liability.

As at 30 June 2013, the Group's financial instruments held at fair value through profit or loss (refer notes 20 and 21) have been classified as level 2 (2012: level 2) in the fair value hierarchy, apart from specific instruments relating to the Company's 100% owned subsidiary, FCGBL, as disclosed below. These instruments comprise debt securities, unitised funds, equities of corporate New Zealand and non-New Zealand entities and derivative financial instruments comprising forward exchange contracts and interest rate swaps. These financial instruments are priced daily with reference to active market pricing.

## 5. RISK MANAGEMENT (CONTINUED)

### E. FAIR VALUES (CONTINUED)

As at 30 June 2013, FCGBL's financial assets held at fair value through profit or loss have been classified as level 3 (2012: level 3) in the fair value hierarchy. These assets comprise a zero coupon bond debt security issued by a New Zealand registered bank. The discount on the face value of the bond of $65.7 million (2012: $65.7 million) was amortised on a market yield basis to maturity on 15 July 2013.

The fair value of the Capital Guaranteed Bonds has been classified as level 3 in the fair value hierarchy. The fair value of the Capital Guaranteed Bonds at 30 June 2013 was $65,778,000 (2012: $63,660,000). The fair value of the Capital Guaranteed Bonds are the estimated realisable values being the outstanding principal owed on the Senior Bonds adjusted for the shortfall of total recognised assets compared to total recognised liabilities held by FCGBL at 30 June.

The fair value of the Subordinated Bonds has been classified as level 3 in the fair value hierarchy. The fair value was derived from a re-estimation of future expected cash flows by FCGBL management discounted by the original effective interest rate of 12.35%. At 30 June 2013 fair value was $nil (2012: $nil).

The carrying value of cash, receivables and other financial assets and payables and other financial liabilities are assumed to approximate their fair value due to their short term nature. The fair value of loans on mortgage and policy loans is the outstanding loan balance and accrued interest.

### F. CAPITAL MANAGEMENT

Capital Risk is managed by the Board with reference to the FCR presented by the Appointed Actuary which includes projections of the solvency margin over the next 5 years for a central basis and various scenarios that would create a bigger solvency strain than the central basis.

On the basis of the projections, the Appointed Actuary makes recommendations on items that may have a bearing on future solvency or maintenance of the Company's credit rating.

Prior to receipt of a Close Out Notice (refer note 17(b)), funds held by FCGBL were invested within the Active Portfolio which were used to generate investment income and used as collateral to generate option income as set out in FCGBL's Investment Statement and Supplemental Trust Deed. At 30 June 2013 and 30 June 2012 all assets were held with the Capital Guarantor.

#### PRIORITY OF CREDITORS CLAIMS

Following the receipt of a Close Out Notice on 11 August 2011 by FCGBL (refer note 17(b)), and the investment of the Fund in a Fixed Portfolio, the Fund was in a deficit position. As there was no Surplus on Close Out of the Fund, suspended and future interest payable was discharged and cancelled. As a result there was no payments to bondholders other than settlement by the Trustee of the senior bondholder principal amount of $75 million on the Maturity Date of 15 July 2013.

FCGBL has a bank account for Ongoing Expenses which will be used to meet contemplated expenses for auditor fees, legal fees, registrar's fees, listing fees and trustee's fees. It is anticipated that there will be no surplus on this account, any shortfall will be met by Fidelity Life as Parent.

#### GUARANTEES

FCGBL entered in to a Reimbursement Agreement dated 7 February 2007 with Westpac Banking Corporation, New Zealand Branch who have guaranteed payment of the Principal Amount at maturity of the Capital Guaranteed Bonds to the extent that the Principal Amount is not paid in full by FCGBL from the Liquidated Proceeds of the Fund. The Capital Guaranteed Bond matured on 15 July 2013, refer to note 46 for further information.

## 5. RISK MANAGEMENT (CONTINUED)

### F. CAPITAL MANAGEMENT (CONTINUED)

#### SOLVENCY

The Company's capital management goals are to maintain a strong capital base to protect policyholders; to maintain an excellent credit rating; and to support its dividend policy.

From 1 December 2011, the Company has operated under a provisional licence issued by the RBNZ, under the provisions of the IPSA. Fidelity Life was granted a full licence by the RBNZ on 2 August 2013.

One of the ongoing licensing requirements is to comply with the Solvency Standard for Life Insurance Business issued by RBNZ (the 'Solvency Standard'). It is a requirement that the actual solvency capital must at all times exceed the higher of $5 million and the minimum solvency capital.

During the year ended 30 June 2013, the Company complied with all capital and other licensing requirements. The Appointed Actuary continuously monitors the capital position of the Company and updates the Board of Directors of the solvency position on a monthly basis.

The Audit and Risk Committee reviews the annual and interim financial statements and receives an actuarial review by independent consulting actuary. From 30 June 2012, the Company has been required to obtain a report from the auditor on the solvency return.

The Board of Directors considers an annual FCR prepared by the Appointed Actuary in accordance with both professional standards issued by the New Zealand Society of Actuaries and the Solvency Standard. The FCR identifies and describes all material risks (of which it is reasonable to expect the Appointed Actuary to be aware) and steps taken or proposed to address such risks. The FCR includes consideration of: related entities; assets, investment policy and matching; investment guarantees; tax; bonuses; dividend policy and capital requirements; risk assessment, controls and operational risk; unit-pricing; persistency; counter-party risks; product pricing, cost of sales and planned growth; and compliance with new and proposed legislation.

The Company manages its capital by considering the return on capital reported under NZ IFRS and projections of solvency margin. Regulatory capital is made up of two components, actual solvency capital and minimum solvency capital. This is calculated as follows for Fidelity Life as the Life Insurer of the Group:

| | Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Actual solvency capital | **126,700** | 118,747 |
| Minimum solvency capital | **96,605** | 96,592 |
| **Solvency margin** | **30,095** | 22,155 |
| **Solvency ratio** | **131.2%** | 122.9% |

## 6. SEGMENT INFORMATION

The operating segments reflect the reporting provided to the Board of Directors (Chief Operating Decision Maker 'CODM'). They reflect the key sectors that the Group operates in and earns revenue from.

Operating segments reported to the CODM for decision making purposes are the Life Insurance segment and the Capital Guaranteed Bond (discontinued operation). Life insurance includes all insurance and investment management services, and includes receipts from fiduciary activities. Operations are conducted in, and revenues derived from, New Zealand. Capital Guaranteed Bond (discontinued operation) relates to investment, all investments are held in New Zealand. Other contains reclassifications of items to reconcile the Board reporting to the statutory financial statements.

The Group does not rely on a major customer for its revenue basis.

**2013**

| | Life Insurance Segment | Capital Guaranteed Bond Segment (Discontinued operation) | Other | Group |
|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 |
| **Revenue** | | | | |
| Insurance premium revenue | 104,134 | - | - | 104,134 |
| Insurance premium ceded to reinsurers | (35,191) | - | - | (35,191) |
| Interest revenue | 8,386 | 1 | (1) | 8,386 |
| Other investment income | 31,020 | - | - | 31,020 |
| Investment property income | 1,961 | - | (677) | 1,284 |
| Other income | 4,709 | - | (3,753) | 956 |
| **Total segment revenue** | 115,019 | 1 | (4,431) | 110,589 |
| **Expenses** | | | | |
| Claims expense | 54,671 | - | - | 54,671 |
| Reinsurance revenue | (38,685) | - | - | (38,685) |
| Commission and other management expenses | 66,566 | 1 | (4,113) | 62,454 |
| Depreciation | 619 | - | - | 619 |
| Amortisation | 979 | - | - | 979 |
| Impairment | 588 | - | - | 588 |
| **Total segment expenses** | 84,738 | 1 | (4,113) | 80,626 |
| Net change in policyholder liabilities – expense | 9,837 | - | 399 | 10,236 |
| **Net profit before taxation** | 20,444 | - | (717) | 19,727 |
| Income tax expense/(credit) | 3,369 | - | (89) | 3,280 |
| **Net insurance income after tax** | 17,075 | - | (628) | 16,447 |
| **Net discontinued operations income after tax** | - | - | 628 | 628 |
| **PROFIT FOR THE YEAR ATTRIBUTABLE TO THE OWNERS OF THE COMPANY AND GROUP** | 17,075 | - | - | 17,075 |
| **Total assets** | 522,700 | 65,807 | (8) | 588,499 |

As per note 17(b) the instrument related to FCGBL has been measured on a realisable value basis (2012: realisable value basis).

## 6. SEGMENT INFORMATION (CONTINUED)

2012

| | Life Insurance Segment | Capital Guaranteed Bond Segment (Discontinued operation) | Other | Group |
|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 |
| **Revenue** | | | | |
| Insurance premium revenue | 95,048 | - | - | 95,048 |
| Insurance premium ceded to reinsurers | (33,787) | - | - | (33,787) |
| Interest revenue | 9,103 | 3 | (3) | 9,103 |
| Other investment income | (5,715) | - | - | (5,715) |
| Investment property income | 1,962 | - | (677) | 1,285 |
| Other income | 10,766 | - | (3,688) | 7,078 |
| **Total segment revenue** | 77,377 | 3 | (4,368) | 73,012 |
| **Expenses** | | | | |
| Claims expense | 44,649 | - | (13) | 44,636 |
| Reinsurance revenue | (33,550) | - | - | (33,550) |
| Commission and other management expenses | 56,818 | 3 | (4,236) | 52,585 |
| Depreciation | 626 | - | - | 626 |
| Amortisation | 744 | - | - | 744 |
| Impairment | 664 | - | - | 664 |
| **Total segment expenses** | 69,951 | 3 | (4,249) | 65,705 |
| Net change in policyholder liabilities - credit | (6,294) | - | 83 | (6,211) |
| **Net profit before taxation** | 13,720 | - | (202) | 13,518 |
| Income tax expense/(credit) | 76 | - | (33) | 43 |
| **Net insurance income after tax** | 13,644 | - | (169) | 13,475 |
| **Net discontinued operations income after tax** | - | - | 169 | 169 |
| **PROFIT FOR THE YEAR ATTRIBUTABLE TO THE OWNERS OF THE COMPANY AND GROUP** | 13,644 | - | - | 13,644 |
| **Total assets** | 476,560 | 63,741 | (8) | 540,293 |

### (B) REVENUES ATTRIBUTABLE TO FOREIGN COUNTRIES:

All revenues received by the life insurance segment are attributable to New Zealand. Subsequent to the Close Out notice (refer note 17(b)) all revenues received by the Capital Guaranteed Bond segment are attributable to New Zealand.

As per note 17(b) the instrument related to FCGBL has been measured on a realisable value basis (2012: realisable value basis).

### (C) NON-CURRENT ASSETS

All non current (non financial instrument) assets held in the Life Insurance segment are located in New Zealand.

All assets under the Capital Guaranteed Bond segment are deemed to be current in nature.

## 7. PROFIT AFTER TAXATION

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Profit after taxation arose from | | |
| **Life insurance contracts** | | |
| Planned margins of revenues over expenses | 9,657 | 9,761 |
| Difference between actual and assumed experience | (3,113) | 2,568 |
| Effects of changes in underlying assumptions | (289) | (3,749) |
| Investment earnings on assets in excess of life insurance liabilities | 2,821 | 3,809 |
| | 9,076 | 12,389 |
| **Life investment contracts** | | |
| Difference between actual and assumed experience | 955 | 222 |
| Effects of changes in underlying assumptions | 123 | (467) |
| | 1,078 | (245) |
| Investment earnings on assets in excess of policy liabilities | 6,921 | 1,500 |
| **Profit after taxation** | 17,075 | 13,644 |

## 8. INSURANCE PREMIUM CEDED TO REINSURERS

Insurance premiums ceded to reinsurers on life insurance contracts were $35,191,000 (2012: $33,787,000) for the Group and Parent.

Reinsurance contracts were held with the following reinsurers during 2013: Swiss Re Life and Health Australia Limited, Munich Reinsurance Company of Australasia Limited, RGA Reinsurance Company of Australia Limited, Hannover Life Re of Australasia Limited and General Reinsurance Life Australia Limited.

(2012: Swiss Re Life and Health Australia Limited, Munich Reinsurance Company of Australasia Limited, RGA Reinsurance Company of Australia Limited, Hannover Life Re of Australasia Limited and General Reinsurance Life Australia Limited, Global Life Reinsurance Company of Australia Pty Limited).

## 9. FEE AND COMMISSION INCOME

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Administration fees | 891 | 475 |
| **Total fee and commission income** | 891 | 475 |

## 10. INVESTMENT INCOME

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Financial instruments designated at fair value through profit or loss | | |
| Equity securities | 438 | (1,122) |
| Debt securities | 6,802 | 5,464 |
| Unit Trusts/PIEs | 28,649 | (6,033) |
| Other | 8 | 3 |
| | 35,897 | (1,688) |
| Financial instruments at amortised cost | | |
| Loans | 1,768 | 2,007 |
| | 1,768 | 2,007 |
| Fair value movement from financial instruments held for trading | | |
| Derivative financial instruments | 2,123 | 3,545 |
| | 2,123 | 3,545 |
| Net exchange losses on financial instruments at amortised cost | (382) | (476) |
| | (382) | (476) |
| | 39,406 | 3,388 |
| **SUMMARY OF INVESTMENT INCOME** | | |
| Interest and similar income | 8,386 | 9,103 |
| Dividend income | 37 | 175 |
| Distributions from unitised investments | 6,639 | 8,442 |
| Net fair value gains/(losses) on financial assets at fair value through profit or loss | 22,221 | (17,877) |
| Net fair value gains on financial assets held for trading | 2,123 | 3,545 |
| **NET INVESTMENT INCOME** | 39,406 | 3,388 |

## 11. INVESTMENT PROPERTY INCOME

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Increase in fair value of investment property (note 23) | 476 | 477 |
| Rental income from investment property | 808 | 808 |
| **Total investment property income** | 1,284 | 1,285 |

## 12. OTHER INCOME

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Reinsurance treaty recapture | - | 6,500 |
| Other income | 65 | 103 |
| **Total other income** | 65 | 6,603 |

In June 2012 $6.5m was received for the recapture of the reinsurance contract relating to the Direct Mail book, which was purchased as part of the acquisition of Farmers Mutual Life Limited in February 2007.

## 13. CLAIMS EXPENSE

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Claims paid to policyholders under life insurance contracts | | |
| Claims paid on death or critical illness | 54,671 | 44,636 |
| **Total life insurance claims and benefits paid** | 54,671 | 44,636 |

## 14. REINSURANCE RECOVERIES

Reinsurance recoveries received for the year on life insurance contracts was $38,685,000 (2012: $33,550,000) for the Group and Parent.

## 15. COMMISSION AND MANAGEMENT EXPENSES

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **LIFE INSURANCE CONTRACTS** | | |
| Acquisition costs | | |
| Commissions | 19,669 | 17,304 |
| Other expenses | 13,924 | 12,649 |
| Maintenance costs | | |
| Commissions | 10,542 | 9,765 |
| Other expenses | 14,620 | 11,816 |
| Corporate financing activities | 1,837 | - |
| | 60,592 | 51,534 |
| **LIFE INVESTMENT CONTRACTS** | | |
| Acquisition costs | | |
| Commissions | 1,330 | 463 |
| Movement in deferred acquisition cost | (1) | 12 |
| Other expenses | 3 | 10 |
| Maintenance costs | | |
| Commissions | 1,988 | 1,828 |
| Other expenses | 118 | 155 |
| Investment management expenses | 610 | 617 |
| | 4,048 | 3,085 |
| **Total commissions and management expenses** | 64,640 | 54,619 |

During the year the Company has undertaken corporate financing activities with respect to the purchase of life insurance policies from TOWER Health and Life Limited and the group risk business of TOWER Life (N.Z.) Limited and the sale of the management rights in the Fidelity KiwiSaver Scheme. Although both transactions did not complete until after 30 June 2013, the Company is required to recognise associated costs as incurred. For further information refer to note 46.

## 15. COMMISSION AND MANAGEMENT EXPENSES (CONTINUED)

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Total commission and management expenses include the following: | | |
| Employee benefit expense | | |
| Wages and salaries and other short term benefits | 14,223 | 11,979 |
| Contribution to superannuation schemes | 985 | 816 |
| Employee share purchase scheme (note 33) | 59 | 71 |
| Remuneration of auditors (appointed auditor: PricewaterhouseCoopers) | | |
| Audit services | 155 | 137 |
| Advisory services | 28 | 19 |
| Acquisition advice services | 151 | - |
| Tax services | | |
| – Compliance | 36 | 39 |
| – Advisory | 9 | 83 |
| Depreciation (note 24) | 619 | 626 |
| Amortisation | | |
| Acquired in-force business (note 28) | 465 | 605 |
| Software (note 28) | 514 | 139 |
| Impairment | | |
| Acquired in-force business (note 28) | - | 664 |
| Internally developed software | 588 | - |
| Directors' fees | 448 | 392 |
| Operating lease costs (note 43) | 162 | 145 |
| Direct rental property expenses (note 23) | 322 | 284 |
| Bad and doubtful debts expense | 148 | 325 |

During the normal course of business, management have written off receivables from agents' commission accounts where the agencies have been terminated. In addition, as disclosed under note 22, the Company has increased its provision for impairment of the mortgages and loans portfolio and agents' commission accounts by $149,000 (2012: $294,000). These amounts are included in bad and doubtful debts expense.

## 16. INCOME TAX EXPENSE

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **(A) INCOME TAX EXPENSE** | | |
| Current tax | 2,069 | (68) |
| Deferred tax | 1,196 | 562 |
| Adjustment to prior period deferred tax | 15 | (451) |
| | 3,280 | 43 |
| Tax credit attributed to policyholders | 4,684 | 2,803 |
| Tax expense attributed to shareholders | (1,404) | (2,760) |
| Total tax expense | 3,280 | 43 |
| **(B) NUMERICAL RECONCILIATION OF INCOME TAX EXPENSE TO PRIMA FACIE TAX PAYABLE** | | |
| Profit before income tax expense | 19,727 | 13,518 |
| Tax at the New Zealand tax rate of 28% (2012: 28%) | 5,524 | 3,785 |
| Tax effect of non-taxable income | (9,021) | (8,004) |
| Tax effect of non-deductible expenses | 7,142 | 5,124 |
| Subsidiary tax losses transferred to parent company | (98) | (111) |
| Benefit of imputation credits received | (281) | (243) |
| Prior period adjustment | 14 | (508) |
| **Income tax expense** | 3,280 | 43 |

Income tax expense includes both tax on shareholder profits and on returns attributed to policyholders.

### (C) IMPUTATION CREDIT ACCOUNT

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Imputation credits available for use in subsequent reporting periods | 117 | 109 |

### (D) TAX CHARGE RELATING TO COMPONENTS OF OTHER COMPREHENSIVE INCOME

The tax charge relating to components of other comprehensive income is as follows:

| | Before tax | Deferred Tax charge | After tax | Before tax | Deferred Tax charge | After tax |
|---|---|---|---|---|---|---|
| | 2013 $'000 | 2013 $'000 | 2013 $'000 | 2012 $'000 | 2012 $'000 | 2012 $'000 |
| **GROUP AND PARENT** | | | | | | |
| Fair value gains/(losses) on revaluation – land and building | 555 | (155) | 400 | 552 | (155) | 397 |
| Employee share purchase plan expense | 59 | - | 59 | 71 | - | 71 |
| | 614 | (155) | 459 | 623 | (155) | 468 |

## 16. INCOME TAX EXPENSE (CONTINUED)

### (E) INCOME TAX ASSET

An income tax asset of $3,881,000 (2012: $2,560,000) is recognised on the statements of financial position of the Company and Group at 30 June 2013. The income tax will be utilised to meet the Company's future shareholder income tax liabilities once tax losses carried forward have been exhausted. The Company cannot request a refund of this income tax asset and it will not be utilised in the next financial year.

## 17. DISCONTINUED OPERATIONS

| | | Group | | Parent | |
|---|---|---|---|---|---|
| | Note | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| **Revenue** | | | | | |
| Fee and commission income | a | 3,753 | 3,688 | 3,753 | 3,688 |
| Investment income | b | 1 | 3 | - | - |
| **Total revenue** | | 3,754 | 3,691 | 3,753 | 3,688 |
| **Expenses** | | | | | |
| Claims expenses | a | - | 13 | - | 13 |
| Net change in life insurance contract liabilities | a | (399) | (83) | (399) | (83) |
| Commission and management expenses | a,b | 3,436 | 3,559 | 3,435 | 3,556 |
| **Total expenses** | | 3,037 | 3,489 | 3,036 | 3,486 |
| **Net income before tax** | | 717 | 202 | 717 | 202 |
| Income tax expense | a | 89 | 33 | 89 | 33 |
| **Net income after tax** | | 628 | 169 | 628 | 169 |

### (A) SALE OF MANAGEMENT RIGHTS IN THE FIDELITY KIWISAVER SCHEME TO GROSVENOR INVESTMENT MANAGEMENT LIMITED

On 8 July 2013, the Company entered into an Agreement for the sale of its management rights in the Fidelity KiwiSaver Scheme ('Agreement') to Grosvenor Investment Management Limited ('GIML') and Grosvenor Financial Services Group Limited ('GFSGL') for consideration of $16.5m comprising cash and shares in GFSGL. This amount represents the minimum receivable by Fidelity Life in relation to the transaction, with the potential for additional payments if the number of members in the Fidelity KiwiSaver Scheme increases by at least 2,000 in each of the two years post completion.

Fidelity Securities Limited, the Fund Manager of the five Fidelity wholesale funds (Fidelity Global Shares Fund, Fidelity Global Bond Fund, Fidelity Property Fund, Fidelity Asset Class Conservative Fund, and Fidelity Asset Class Growth Fund), along with the management rights to the five wholesale funds, were also included within this agreement.

The revenue and expenses relating to the management rights in the Fidelity KiwiSaver Scheme are deemed to be held for sale and have been disclosed separately in the statement of other comprehensive income. The sale completed on 23 August 2013. For further information refer to note 46.

## 17. DISCONTINUED OPERATIONS (CONTINUED)

### (A) SALE OF MANAGEMENT RIGHTS IN THE FIDELITY KIWISAVER SCHEME TO GROSVENOR INVESTMENT MANAGEMENT LIMITED (CONTINUED)

Analysis of the results in relation to the benefits received of the management rights relating to the Fidelity KiwiSaver Scheme:

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Revenue** | | |
| Fee and commission income | 3,753 | 3,688 |
| **Total revenue** | 3,753 | 3,688 |
| **Expenses** | | |
| Claims expenses | - | 13 |
| Net change in life insurance contract liabilities | (399) | (83) |
| Commission and management expenses | 3,435 | 3,556 |
| **Total expenses** | 3,036 | 3,486 |
| **Net income before tax** | 717 | 202 |
| Income tax expense | 89 | 33 |
| **Net income after tax** | 628 | 169 |

### INCOME TAXATION FROM DISCONTINUED OPERATIONS CONSISTS OF:

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **(a) Income tax expense** | | |
| Current tax | 89 | 33 |
| | 89 | 33 |
| **(b) Numerical reconciliation of income tax expense to prima facie tax payable** | | |
| Income before income tax expense | 717 | 202 |
| Tax at the New Zealand tax rate of 28% (2012: 28%) | 201 | 57 |
| Tax effect of non-taxable/non-deductible amounts | (112) | (24) |
| **Income tax expense from discontinued operations** | 89 | 33 |

## 17. DISCONTINUED OPERATIONS (CONTINUED)

### (A) SALE OF MANAGEMENT RIGHTS IN THE FIDELITY KIWISAVER SCHEME TO GROSVENOR INVESTMENT MANAGEMENT LIMITED (CONTINUED)

As at 30 June 2013 all assets and liabilities in relation to the Fidelity KiwiSaver Scheme Management Rights were held by Fidelity Life and comprised of:

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Assets of disposal group classified as held for sale** | | |
| Sundry receivables | 117 | 102 |
| Deferred tax assets | 16 | 8 |
| Deferred acquisition costs | - | 862 |
| | 133 | 972 |

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Liabilities of disposal group classified as held for sale** | | |
| Creditors and accruals | 172 | 135 |
| Employee entitlements | 65 | 36 |
| Deferred tax liability | - | 241 |
| Life insurance contract liabilities | 102 | 500 |
| | 339 | 912 |

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Cash flows of disposal group classified as held for sale** | | |
| Operating cash inflows | 1,231 | 1,399 |
| **Total cash inflows** | 1,231 | 1,399 |

## 17. DISCONTINUED OPERATIONS (CONTINUED)

### (B) FIDELITY CAPITAL GUARANTEED BOND

| | Group | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Investment income** | | |
| Financial instruments designated at fair value through profit or loss – Debt securities | 2,119 | 2,711 |
| (Increase)/reduction in funds attributable to Bondholders | (2,118) | (2,708) |
| **Investment income** | 1 | 3 |
| **Expenses** | | |
| Auditors' fees | 10 | 32 |
| Other expenses | 49 | 74 |
| Movement in provision for future on-going operating expenses | (58) | (103) |
| **Total operating expenses** | 1 | 3 |
| **Net discontinued operations loss before tax** | - | - |
| Income tax expense from discontinued operations | - | - |
| **NET DISCONTINUED OPERATIONS LOSS AFTER TAX** | - | - |

In August 2011 there was significant volatility in investment markets. Major losses were incurred by the Company's wholly owned subsidiary, Fidelity Capital Guaranteed Bond Limited ('FCGBL'). The net asset value of the investments (the 'Fund'), managed by Tyndall Investment Management Limited, fell below the Bond Floor on 10 August 2011, triggering an Event of Default. This led to the Capital Guarantor, Westpac Banking Corporation, New Zealand Branch, issuing a Close Out Notice and assuming control and direction of the Fund. Open position Active Portfolio Assets were closed out and, in accordance with the Supplemental Trust Deed (No. 1), the resulting proceeds were invested in Fixed Portfolio Assets during August 2011. The resulting proceeds were invested in a zero coupon bond and cash. No future interest coupons will be paid and interest is no longer expensed or accrued.

Following these events in the 2011 financial statements FCGBL was deemed to be a discontinuing operation and the financial statements for the subsidiary are based on a realisable value basis. FCGBL continues to be accounted for on a realisable value basis.

In the current year, interest income and net changes in financial assets at fair value through profit or loss on investments have been offset by a realisable value adjustment to the senior bond liability. In addition the provision for on-going expenses has been adjusted to reflect actual expenses incurred in the year and future expected cash flows. The net impact is that profit before tax is nil.

Assets and liabilities for 30 June 2013 and 30 June 2012 are carried at net realisable values. As at 30 June 2013, all assets were held with the Capital Guarantor and comprised a $65.6 million zero coupon bond (2012: $63.5 million) with a face value of $65.7 million (2012: $65.7 million) on the maturity date of 15 July 2013; and $0.2 million (2012: $0.2 million) of cash and accrued interest in a money market bank account. In addition at 30 June 2013 the Company had $0.03 million (2012: $0.1 million) in a separate operating bank account to cover on-going expenses accrued and expected to be incurred prior to the maturity date of 15 July 2013.

## 17. DISCONTINUED OPERATIONS (CONTINUED)

### (B) FIDELITY CAPITAL GUARANTEED BOND (CONTINUED)

The Capital Guarantor guarantees the payment of the principal amount at maturity of the $75 million Capital Guaranteed Bonds to the extent that the principal amount of the bonds is not paid in full by FCGBL from the liquidated proceeds of the Fund. As at 30 June 2013 this is estimated to be $9.1 million (2012: $9.1 million) (for further information refer to note 46).

**Investment income consists of:**

| | Group | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Interest and similar income | 1 | 3 |
| **Net investment income from discontinued operations** | 1 | 3 |

## 18. CASH AND CASH EQUIVALENTS

| | Group | | Parent | |
|---|---|---|---|---|
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Cash at bank and in hand | | | | |
| Bank balances | 12,984 | 15,441 | 12,790 | 15,194 |
| Deposits at call | - | 102 | - | 102 |
| **Total cash and cash equivalents** | 12,984 | 15,543 | 12,790 | 15,296 |

## 19. ASSETS ARISING FROM REINSURANCE CONTRACTS

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Assets arising from reinsurance contracts comprise: | | |
| Life insurance contracts | 12,091 | 10,347 |
| | 12,091 | 10,347 |
| **Life insurance contracts reinsurance assets** | | |
| Carrying amount at 1 July | 10,347 | 6,983 |
| Reinsurance claims made to reinsurers | 38,277 | 33,112 |
| Payments received from reinsurers | (36,533) | (29,748) |
| **CARRYING AMOUNT AT 30 JUNE** | 12,091 | 10,347 |
| Expected maturity | | |
| Within 12 months | 12,091 | 10,347 |
| | 12,091 | 10,347 |

## 20. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

| | Group | | Parent | |
|---|---|---|---|---|
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| **FINANCIAL ASSETS DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS** | | | | |
| **Debt securities** | | | | |
| Local Authority | 8,355 | 11,021 | 8,355 | 11,021 |
| New Zealand Government | 21,357 | 11,216 | 21,357 | 11,216 |
| Corporate – New Zealand | 147,829 | 144,406 | 82,216 | 80,912 |
| Unitised Funds | 196,503 | 176,755 | 196,503 | 176,755 |
| **Total debt securities** | 374,044 | 343,398 | 308,431 | 279,904 |
| **Equity securities** | | | | |
| Corporate – New Zealand | 797 | - | 797 | - |
| Corporate – non-New Zealand | - | 8,309 | - | 8,309 |
| Unitised Funds | 110,622 | 85,521 | 110,622 | 85,521 |
| **Total equity securities** | 111,419 | 93,830 | 111,419 | 93,830 |
| **TOTAL FINANCIAL ASSETS DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS** | 485,463 | 437,228 | 419,850 | 373,734 |
| **Expected maturity based on contractual terms** | | | | |
| Within 12 months | 381,679 | 278,910 | 316,066 | 278,910 |
| Later than 12 months | 103,784 | 158,318 | 103,784 | 94,824 |
| | 485,463 | 437,228 | 419,850 | 373,734 |

As per note 17(b) the instrument related to FCGBL has been measured on a realisable value basis (2012: realisable value basis).

## 21. DERIVATIVE FINANCIAL INSTRUMENTS

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Assets** | | |
| Forward currency | 392 | 2,721 |
| Interest rate swaps | 465 | - |
| **Derivative assets** | 857 | 2,721 |
| Less non-current portion | | |
| Interest rate swaps | 465 | - |
| **Current portion of derivative assets** | 392 | 2,721 |
| **Liabilities** | | |
| Forward currency | 2,477 | 166 |
| Put options | 80 | - |
| Call options | - | 7 |
| **Current portion of derivative liabilities** | 2,557 | 173 |

The notional principal amounts of outstanding derivatives at 30 June 2013 were:

- forward foreign exchange contracts $120,404,000 (2012: $92,935,000);
- interest rate swaps $55,000,000 (2012: $nil);
- put options $3,990,000 (2012: $nil); and
- call options $nil (2012: $31,072,000).

## 22. LOANS AND OTHER RECEIVABLES

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Mortgage and agents' loans | **25,995** | 29,473 |
| Policy loans | **143** | 143 |
| Other loans | **846** | 558 |
| **Total loans** | **26,984** | 30,174 |
| Less provision for impairment on loans (note 5(D)) | **(923)** | (774) |
| **Net loans receivable** | **26,061** | 29,400 |
| **Other receivables** | | |
| Proceeds due from sale of investments | **287** | 214 |
| Outstanding premiums | **848** | 928 |
| Prepayments | **1,332** | 1,011 |
| Interest due on loans | **380** | 697 |
| Prepaid deposit | **2,000** | - |
| Sundry receivables | **612** | 196 |
| **Total other receivables** | **5,459** | 3,046 |
| **TOTAL LOANS AND OTHER RECEIVABLES** | **31,520** | 32,446 |
| **Expected maturity** | | |
| Within 12 months | **8,805** | 6,469 |
| Later than 12 months | **22,715** | 25,977 |
| | **31,520** | 32,446 |

The provisions above are all made against specific loans and receivables where it is considered there has been events making full repayment unlikely.

There have been no collective provisions included (2012: nil).

The creation and release of the provision for impaired receivables has been included in other expenses in the profit and loss component of the statements of other comprehensive income. Amounts charged to the allowance account are generally written off when there is no expectation of recovering additional cash.

Refer to note 5(D) for reconciliation of impairment provision.

The Company paid a deposit of $2m on entering the agreement to purchase the life insurance policies from TOWER Health and Life Limited and the group risk business of TOWER Life (N.Z.) Limited. Refer to note 46 for further information on the acquisition.

## 23. INVESTMENT PROPERTY

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **At fair value** | | |
| Opening balance | 9,275 | 8,798 |
| Capitalised expenditure | 452 | - |
| Net gain from fair value adjustment | 476 | 477 |
| **Closing balance** | 10,203 | 9,275 |

### (A) DIRECT OPERATING EXPENSES FROM INVESTMENT PROPERTY

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| That generated rental income during the period | 322 | 284 |
| | 322 | 284 |

### (B) VALUATION BASIS

Investment property includes commercial office buildings based in Auckland.

Investment property (including the owner occupied component – refer note 24) was valued on 30 June 2013 at $19.3m (2012: $17.5m), by P R Amesbury (ANZIV, SPINZ) an independent registered valuer in the firm of Barratt-Boyes Jefferies Lawton Limited.

The fair values are based on active market prices calculated on capitalisation rates derived from sales of comparable properties, adjusted, if necessary, for any difference in the nature, location or condition of the specific assets.

### (C) CONTRACTUAL OBLIGATIONS

There are no contractual obligations to purchase, construct or develop investment property or for any other repairs, maintenance or enhancements (2012: nil).

## 24. PROPERTY, PLANT AND EQUIPMENT

| | Land | Buildings | Building fit out | Leasehold improve-ments | Motor vehicles | Computer equipment | Furniture and office equipment | Total |
|---|---|---|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 |
| **GROUP AND PARENT** | | | | | | | | |
| **At 1 July 2011** | | | | | | | | |
| Cost | 2,820 | 4,982 | 972 | 67 | 515 | 1,376 | 692 | 11,424 |
| Accumulated depreciation | - | - | (628) | (21) | (202) | (1,014) | (567) | (2,432) |
| **Net book amount** | 2,820 | 4,982 | 344 | 46 | 313 | 362 | 125 | 8,992 |
| **Year ended 30 June 2012** | | | | | | | | |
| Opening net book amount | 2,820 | 4,982 | 344 | 46 | 313 | 362 | 125 | 8,992 |
| Additions | - | - | 13 | 12 | - | 324 | 34 | 383 |
| Revaluation | 94 | 458 | - | - | - | - | - | 552 |
| Depreciation | - | (130) | (121) | (10) | (80) | (226) | (59) | (626) |
| Disposals | - | - | - | - | (19) | - | - | (19) |
| **Closing net book amount** | 2,914 | 5,310 | 236 | 48 | 214 | 460 | 100 | 9,282 |
| **At 1 July 2012** | | | | | | | | |
| Cost | 2,914 | 5,310 | 985 | 79 | 445 | 1,673 | 748 | 12,154 |
| Accumulated depreciation | - | - | (749) | (31) | (231) | (1,213) | (648) | (2,872) |
| **Net book amount** | 2,914 | 5,310 | 236 | 48 | 214 | 460 | 100 | 9,282 |
| **Year ended 30 June 2013** | | | | | | | | |
| Opening net book amount | 2,914 | 5,310 | 236 | 48 | 214 | 460 | 100 | 9,282 |
| Additions | - | 401 | - | 2 | 201 | 254 | 80 | 938 |
| Revaluation | 221 | 334 | - | - | - | - | - | 555 |
| Depreciation | - | (133) | (121) | (10) | (87) | (215) | (53) | (619) |
| Disposals | - | - | (9) | - | (26) | - | - | (35) |
| **Closing net book amount** | 3,135 | 5,912 | 106 | 40 | 302 | 499 | 127 | 10,121 |
| **At 30 June 2013** | | | | | | | | |
| Cost | 3,135 | 5,912 | 976 | 81 | 499 | 1,908 | 828 | 13,339 |
| Accumulated depreciation | - | - | (870) | (41) | (197) | (1,409) | (701) | (3,218) |
| **Net book amount** | 3,135 | 5,912 | 106 | 40 | 302 | 499 | 127 | 10,121 |

GROUP AND PARENT

**(A) OWNER-OCCUPIED PROPERTIES**

Owner-occupied properties are stated at their revalued amounts as assessed by qualified external valuers. Values are calculated on the basis of existing use, being the estimated arms-length value at which the properties could be exchanged with vacant possession and without allowing for alternatives to their current use. The most recent valuation was undertaken by P R Amesbury a registered valuer in the firm of Barratt-Boyes Jefferies Lawton Limited on 30 June 2013. For further information on the valuation refer to note 23(b).

## 24. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

### (B) IF LAND AND BUILDINGS WERE STATED ON THE HISTORICAL COST BASIS, THE AMOUNTS WOULD BE AS FOLLOWS:

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Cost | 7,318 | 6,917 |
| Accumulated depreciation | (1,241) | (1,108) |
| **Net book amount** | 6,077 | 5,809 |

## 25. INVESTMENT IN SUBSIDIARIES

The Parent holds the following interests in subsidiaries

| Company | Nature of activities | Class of Shares | Ownership | |
|---|---|---|---|---|
| | | | 2013 | 2012 |
| Fidelity Capital Guaranteed Bond Limited | Investment (Discontinued Operations) | Ordinary | 100% | 100% |
| Fidelity Fund Management Limited | Non-trading Trustee Company | Ordinary | 100% | 100% |
| Fidelity Securities Limited | Fund Manager (Discontinued Operations) | Ordinary | 100% | 100% |

All subsidiaries are incorporated in New Zealand and have a balance date of 30 June.

Fidelity Securities Limited was sold to Grosvenor Investment Management Limited ('GIML') on 23 August 2013.

## 26. DEFERRED TAX

The balance comprises temporary differences attributable to:

| Deferred tax assets | Fixed assets | Provisions | Unused tax losses | Total |
|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 |
| GROUP AND PARENT | | | | |
| Balance at 30 June 2011 | 613 | 877 | 12,687 | 14,177 |
| Movement through profit or loss | (157) | 249 | 833 | 925 |
| Balance at 30 June 2012 | 456 | 1,126 | 13,520 | 15,102 |
| Movement through profit or loss | (354) | 349 | 1,993 | 1,988 |
| **Balance at 30 June 2013** | 102 | 1,475 | 15,513 | 17,090 |

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Deferred tax assets to be recovered:** | | |
| Later than 12 months | 15,616 | 11,452 |
| Within 12 months | 1,474 | 3,650 |
| | 17,090 | 15,102 |

## 26. DEFERRED TAX (CONTINUED)

| Deferred tax liabilities | Investment property | Insurance reserves | Deferred acquisition costs | Total |
|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 |
| **GROUP AND PARENT** | | | | |
| Balance at 30 June 2011 | 168 | 884 | 21,270 | 22,322 |
| Movement through profit or loss | 97 | 478 | 460 | 1,035 |
| Movement through other comprehensive income | 155 | - | - | 155 |
| Balance at 30 June 2012 | 420 | 1,362 | 21,730 | 23,512 |
| Movement through profit or loss | 96 | (117) | 3,218 | 3,197 |
| Movement through other comprehensive income | 155 | - | - | 155 |
| **Balance at 30 June 2013** | 671 | 1,245 | 24,948 | 26,864 |

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Deferred tax liabilities to be settled:** | | |
| Later than 12 months | 26,864 | 23,512 |
| | 26,864 | 23,512 |

## 27. DEFERRED ACQUISITION COSTS – INVESTMENT

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Carrying amount at 1 July | 867 | 2,130 |
| Acquisition costs deferred during the year | 6 | 6 |
| Amortisation | (867) | (1,269) |
| **Carrying amount at 30 June** | 6 | 867 |

## 28. INTANGIBLE ASSETS

| | Software | Internally developed software | AVIF | Total |
|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 |
| **GROUP AND PARENT** | | | | |
| **At 1 July 2011** | | | | |
| Cost | 978 | 1,222 | 6,054 | 8,254 |
| Accumulated amortisation | (764) | - | (2,622) | (3,386) |
| **Net book amount** | 214 | 1,222 | 3,432 | 4,868 |
| **Year ended 30 June 2012** | | | | |
| Opening net book amount | 214 | 1,222 | 3,432 | 4,868 |
| Additions | 218 | 1,244 | - | 1,462 |
| Amortisation | (139) | - | (605) | (744) |
| Impairment charge | - | - | (664) | (664) |
| **Closing net book amount** | 293 | 2,466 | 2,163 | 4,922 |
| **At 1 July 2012** | | | | |
| Cost | 1,201 | 2,466 | 6,054 | 9,721 |
| Accumulated amortisation | (908) | - | (3,891) | (4,799) |
| **Net book amount** | 293 | 2,466 | 2,163 | 4,922 |
| **Year ended 30 June 2013** | | | | |
| Opening net book amount | 293 | 2,466 | 2,163 | 4,922 |
| Additions | 174 | 754 | - | 928 |
| Amortisation | (104) | (410) | (465) | (979) |
| Impairment charge | - | (588) | - | (588) |
| **Closing net book amount** | 363 | 2,222 | 1,698 | 4,283 |
| **As at 30 June 2013** | | | | |
| Cost | 1,375 | 3,220 | 6,054 | 10,649 |
| Accumulated amortisation | (1,012) | (998) | (4,356) | (6,366) |
| **Net book amount** | 363 | 2,222 | 1,698 | 4,283 |

### Internally developed software

Software includes internally developed software. This relates to the development of significant, identifiable and unique software utilised by the Company and Group. Employee and contractor costs associated with developing the software is capitalised and amortised over the estimated useful life being 3 - 5 years. Internally developed software includes the charges for both implemented projects and any work in progress at the end of the period. Amortisation commences once the software is put into production.

An impairment review is undertaken annually to determine if any impairment has occurred on the outstanding unamortised amount. An impairment charge has been applied where no future economic benefits were deemed to be realisable (2012: nil).

## 28. INTANGIBLE ASSETS (CONTINUED)

**Acquired value of in-force business**

The acquired value of in-force business ('AVIF') from the acquisition of Farmers' Mutual Life Limited ('FMLL') has been determined by an actuarial valuation and relates to the future anticipated profits emerging from the life insurance contracts. On 1 March 2007 the AVIF was valued at $6,054,000, which, it was determined, should be amortised over 10 years, being the life expectancy of the outstanding life insurance contracts. An impairment review is undertaken annually at the balance date to determine if any impairment has occurred on the unamortised amount.

At 30 June 2013 the unamortised amount was $1,698,000. Using a discount rate of 10% (2012:10%) the AVIF was valued at $1,914,000 (2012: $2,163,000). No impairment charge has been recognised for the year to 30 June 2013 (2012: impairment charge of $664,000).

The decrease in AVIF is due to the amortisation of the residual AVIF over the remaining time to the tenth anniversary of the FMLL acquisition (2012: The fall in AVIF due to a reduction in the value of planned profit margins on the FMLL book, resulting from the application of a uniform planned margin. The technical change in the AVIF accords with the underlying change in value of economic capital. In addition, due to the change in the solvency margin calculation methodology (see note 5(F)) the AVIF valuation in 2012 included a charge for solvency capital).

## 29. PAYABLES AND OTHER FINANCIAL LIABILITIES

| | | Group | | Parent | |
|---|---|---|---|---|---|
| | Note | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Creditors and accruals | | 5,482 | 5,029 | 5,454 | 4,949 |
| Claims notified | | 11,653 | 11,376 | 11,653 | 11,376 |
| Premiums in advance | | 412 | 392 | 412 | 392 |
| Reinsurance liabilities | | 9,843 | 9,396 | 9,843 | 9,396 |
| Employee entitlements | | 2,314 | 1,528 | 2,314 | 1,528 |
| Payable to subsidiary | | - | - | 7 | 7 |
| Payable to related entity | 40 | - | 1,913 | - | 1,913 |
| Employee share purchase plan provision | 47 | 837 | 1,018 | 837 | 1,018 |
| | | 30,541 | 30,652 | 30,520 | 30,579 |
| **Expected maturity** | | | | | |
| Within 12 months | | 29,936 | 29,798 | 29,915 | 29,725 |
| Later than 12 months | | 605 | 854 | 605 | 854 |
| **Total payables and other financial liabilities** | | 30,541 | 30,652 | 30,520 | 30,579 |

## 30. INTEREST BEARING LIABILITIES

| | Group | | Parent | |
|---|---|---|---|---|
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Capital guaranteed bonds | 65,778 | 63,660 | - | - |
| **Total interest bearing liabilities** | 65,778 | 63,660 | - | - |
| **Expected maturity** | | | | |
| Within 12 months | 65,778 | - | - | - |
| Later than 12 months | - | 63,660 | - | - |
| | 65,778 | 63,660 | - | - |

At 30 June 2013 FCGBL was listed on the New Zealand Debt Exchange ('NZDX').

In accordance with the FCGBL's supplemental Trust Deed the principal and interest amounts owing to the holders of the Capital Guaranteed Bonds rank ahead of all amounts owing to the Subordinated bondholder.

The carrying value of the Capital Guaranteed Bonds at 30 June 2013 reflects the market value of the underlying investment portfolio on a realisable value basis. The bond matured on 15 July 2013. The Trustee was permitted, in accordance with the Supplemental Trust Deed and Guarantee to make demand to Westpac as Guarantor for any difference between the principal amount of the outstanding Senior Bonds and the liquidated proceeds from the Fixed Portfolio.

Due to the Close Out of the Fund resulting in no surplus, as described in note 17(b), coupon payments are discharged and cancelled.

## 31. LIFE INSURANCE CONTRACT LIABILITIES

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **Opening balance at 1 July** | (17,054) | (17,813) |
| Premiums received | 101,676 | 93,534 |
| Liabilities released for payments on death, surrender and other terminations in the year | (54,671) | (44,649) |
| Net cost of reinsurance | 3,494 | (237) |
| Non-investment commission | (30,211) | (27,069) |
| Expenses other than commission | (33,099) | (26,167) |
| Other movements | (730) | 5,347 |
| **Closing balance at 30 June** | (30,595) | (17,054) |
| **Expected maturity** | | |
| Within 12 months | 936 | 6,344 |
| Later than 12 months | (31,531) | (23,398) |
| | (30,595) | (17,054) |
| Life insurance contracts with a discretionary participation feature that have a guaranteed element | 32,047 | 31,835 |
| **Life insurance contract liabilities contain the following components** | | |
| Future policy benefits | 647,430 | 620,586 |
| Future expenses | 239,067 | 219,573 |
| Planned margins of revenues over expenses | 117,901 | 112,237 |
| Future revenues | (1,034,993) | (969,450) |
| | (30,595) | (17,054) |

## 32. LIFE INVESTMENT CONTRACT LIABILITIES

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Participating contracts | | |
| Guaranteed element | 194,751 | 185,054 |
| | 194,751 | 185,054 |
| Non-participating contracts designated at fair value through profit or loss | 143,463 | 113,895 |
| | 338,214 | 298,949 |
| Movement in life investment contract liabilities | | |
| **Opening balance at 1 July** | 298,949 | 307,664 |
| Contributions received | 58,018 | 45,309 |
| Fees deducted from account balances | (2,458) | (1,514) |
| Liabilities released for payments on death, surrender and other terminations in the year | (39,675) | (45,457) |
| Investment return credited to policyholders | 25,328 | (4,243) |
| Other movements | (1,948) | (2,810) |
| **Closing balance at 30 June** | 338,214 | 298,949 |
| **Expected maturity** | | |
| Within 12 months | 145,634 | 119,011 |
| Later than 12 months | 192,580 | 179,938 |
| | 338,214 | 298,949 |

## 33. SHARE CAPITAL

| | Group and Parent | | | |
|---|---|---|---|---|
| | 2013 Shares | 2012 Shares | 2013 $'000 | 2012 $'000 |
| (A) AUTHORISED SHARE CAPITAL | | | | |
| Ordinary shares – fully paid. No par value | 1,439,082 | 1,439,082 | 13,186 | 12,946 |
| (B) MOVEMENTS | | | | |
| Opening balance of ordinary shares issued | 1,439,082 | 1,438,582 | 12,946 | 12,581 |
| Issues of ordinary shares during the year | - | 500 | - | 45 |
| Employee share purchase plan fully vested shares | - | - | 181 | 249 |
| Employee share purchase plan expense | - | - | 59 | 71 |
| **Closing balance of ordinary shares issued** | 1,439,082 | 1,439,082 | 13,186 | 12,946 |
| **Held:** | | | | |
| Directly | 1,418,182 | 1,409,699 | | |
| Employee share purchase plan trust | 20,900 | 29,383 | | |
| **Total balance of ordinary shares held** | 1,439,082 | 1,439,082 | | |

## 33. SHARE CAPITAL (CONTINUED)

### (C) ORDINARY SHARES

Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of and amounts paid on the shares held.

## 34. RETAINED EARNINGS AND RESERVES

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **(A) REVALUATION RESERVE** | | |
| Movements in the revaluation reserve were as follows: | | |
| **Balance at 1 July** | 769 | 372 |
| Owner occupied land and buildings revaluation, net of tax | 400 | 397 |
| **Balance 30 June** | 1,169 | 769 |

The asset revaluation reserve is used to record increments and decrements on the revaluation of the owner occupied land and buildings.

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| **(B) RETAINED EARNINGS** | | |
| Movements in Retained Earnings were as follows: | | |
| **Balance 1 July** | 126,686 | 116,136 |
| Profit for the year | 17,075 | 13,644 |
| Dividends (note 35) | (3,404) | (3,094) |
| **Balance at 30 June** | 140,357 | 126,686 |

## 35. DIVIDENDS

| | Group and Parent | | | |
|---|---|---|---|---|
| | 2013 Per share | 2012 Per share | 2013 $'000 | 2012 $'000 |
| **Ordinary shares** | | | | |
| Final dividend | 2.37 | 2.15 | 3,404 | 3,094 |
| **Total dividend paid** | 2.37 | 2.15 | 3,404 | 3,094 |

The dividends are fully imputed.

On 4 September 2013 the Company declared an ordinary dividend of $2.42 (gross of tax) per share issued amounting to $3,482,578 (gross of tax) and a special dividend of $0.58 (gross of tax) per share issued amounting to $834,668 (gross of tax). The dividends are not imputed. This dividend is not recognised in the financial statements, as it is a post balance date declaration with no liability attaching at 30 June 2013.

## 36. EARNINGS PER SHARE

### (i) BASIC

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Company and held as treasury shares.

| | 2013 '000 | 2012 '000 |
|---|---|---|
| Profit attributable to equity holders of the Company | $16,447 | $13,475 |
| Profit from discontinued operation attributable to equity holders of the Company | $628 | $169 |
| Weighted average number of ordinary shares in issue | 1,439 | 1,439 |

| | 2013 $ | 2013 $ |
|---|---|---|
| **Basic earnings per share** | | |
| From continuing operations | 11.43 | 9.36 |
| From discontinued operations | 0.43 | 0.12 |

### (ii) DILUTED

There is no dilution in the earnings per share as the employee share purchase plan is recognised within the basic earnings per share, as all shares are currently issued.

## 37. RECONCILIATION OF NET PROFIT AFTER TAXATION TO CASH FLOWS FROM OPERATING ACTIVITIES

| | Group | | Parent | |
|---|---|---|---|---|
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| **Net profit after taxation** | 17,075 | 13,644 | 17,075 | 13,644 |
| **Non cash items** | | | | |
| Losses/(gains) on sale of property and equipment | 16 | (7) | 16 | (7) |
| Fair value gains on investment property | (476) | (477) | (476) | (477) |
| Fair value (gains)/losses on investments | (19,220) | 15,990 | (17,102) | 17,874 |
| Depreciation of property and equipment | 619 | 626 | 619 | 626 |
| Equity compensation plans, equity settled expense | 59 | 71 | 59 | 71 |
| Taxation | 317 | (1,128) | 317 | (1,128) |
| Amortisation of acquired value of in-force business and intangibles | 979 | 744 | 979 | 744 |
| Impairment of acquired value of in-force business and intangibles | 588 | 664 | 588 | 664 |
| Realisation adjustment to Senior Bonds | 2,118 | 2,708 | - | - |
| Movement in provision for future on-going expenses | (58) | (103) | - | - |
| | 2,017 | 32,732 | 2,075 | 32,011 |
| **Changes in working capital** | | | | |
| Increase in reinsurance assets | (1,744) | (3,364) | (1,744) | (3,364) |
| Decrease in deferred acquisition costs | 861 | 1,263 | 861 | 1,263 |
| Increase/(decrease) in insurance liabilities and investment contracts | 25,724 | (7,956) | 25,724 | (7,956) |
| (Increase)/decrease in other assets | (657) | 1,690 | (658) | 895 |
| Increase in other liabilities | 2,706 | 5,986 | 2,702 | 6,594 |
| Decrease/(increase) in derivatives | 4,248 | (1,520) | 4,248 | 109 |
| Decrease in accrued interest payable | - | (3,469) | - | - |
| **Items classified as financing activities** | | | | |
| Interest paid | - | 3,469 | - | - |
| **Cash flows from operating activities** | 33,155 | 28,831 | 33,208 | 29,552 |

## 38. INVESTMENT AND NON-INVESTMENT LINKED

NZ IFRS 4 requires disclosure of disaggregated information in respect of amounts relating to investment linked business, non-investment linked business and shareholders' funds for certain categories as shown below. Non-investment linked business includes shareholders' funds.

| | Investment linked | Non investment linked | Total |
|---|---|---|---|
| | $'000 | $'000 | $'000 |
| **GROUP** | | | |
| **2013** | | | |
| Investment assets | 330,813 | 165,710 | 496,523 |
| Other assets | 7,400 | 84,576 | 91,976 |
| Policy liabilities | 338,214 | (30,595) | 307,619 |
| Liabilities other than policy liabilities | - | 126,168 | 126,168 |
| Shareholders' retained earnings | - | 140,357 | 140,357 |
| Premium revenue | 55,560 | 104,134 | 159,694 |
| Investment revenue | 35,228 | 5,463 | 40,691 |
| Claims expense | 39,675 | 54,671 | 94,346 |
| Other operating expenses | 4,048 | 64,028 | 68,076 |
| Investment revenues paid or allocated to policyholders | (25,328) | - | (25,328) |
| Operating profit before tax | 5,504 | 14,940 | 20,444 |
| Operating profit after tax | 1,078 | 15,997 | 17,075 |

| | Investment linked | Non investment linked | Total |
|---|---|---|---|
| | $'000 | $'000 | $'000 |
| **GROUP** | | | |
| **2012** | | | |
| Investment assets | 292,221 | 157,003 | 449,224 |
| Other assets | 6,728 | 84,341 | 91,069 |
| Policy liabilities | 298,949 | (17,054) | 281,895 |
| Liabilities other than policy liabilities | - | 117,997 | 117,997 |
| Shareholders' retained earnings | - | 126,686 | 126,686 |
| Premium revenue | 43,795 | 95,048 | 138,843 |
| Investment revenue | 1,056 | 3,620 | 4,676 |
| Claims expense | 45,457 | 44,649 | 90,106 |
| Other operating expenses | 4,939 | 53,239 | 58,178 |
| Investment revenues paid or allocated to policyholders | 4,243 | - | 4,243 |
| Operating profit before tax | 1,913 | 11,807 | 13,720 |
| Operating (loss)/ profit after tax | (245) | 13,889 | 13,644 |

## 39. FINANCIAL INSTRUMENTS BY CATEGORY

ASSETS AS PER STATEMENT OF FINANCIAL POSITION

| | Assets at fair value through profit or loss | Loans and other receivables | Total |
|---|---|---|---|
| | $'000 | $'000 | $'000 |
| GROUP | | | |
| Year ended 30 June 2013 | | | |
| Financial assets at fair value through profit or loss | 485,463 | - | 485,463 |
| Derivative financial instruments | 857 | - | 857 |
| Loans and other receivables | - | 28,188 | 28,188 |
| Cash and cash equivalents | - | 12,984 | 12,984 |
| Assets arising from reinsurance contracts | - | 12,091 | 12,091 |
| | 486,320 | 53,263 | 539,583 |
| Year ended 30 June 2012 | | | |
| Financial assets at fair value through profit or loss | 437,228 | - | 437,228 |
| Derivative financial instruments | 2,721 | - | 2,721 |
| Loans and other receivables | - | 31,435 | 31,435 |
| Cash and cash equivalents | - | 15,543 | 15,543 |
| Assets arising from reinsurance contracts | - | 10,347 | 10,347 |
| | 439,949 | 57,325 | 497,274 |

As per note 17(b) the instrument related to FCGBL has been measured on a realisable value basis (2012: realisable value basis).

| | | | |
|---|---|---|---|
| PARENT | | | |
| Year ended 30 June 2013 | | | |
| Financial assets at fair value through profit or loss | 419,850 | - | 419,850 |
| Derivative financial instruments | 857 | - | 857 |
| Loans and other receivables | - | 28,188 | 28,188 |
| Cash and cash equivalents | - | 12,790 | 12,790 |
| Assets arising from reinsurance contracts | - | 12,091 | 12,091 |
| | 420,707 | 53,069 | 473,776 |
| Year ended 30 June 2012 | | | |
| Financial assets at fair value through profit or loss | 373,734 | - | 373,734 |
| Derivative financial instruments | 2,721 | - | 2,721 |
| Loans and other receivables | - | 31,435 | 31,435 |
| Cash and cash equivalents | - | 15,296 | 15,296 |
| Assets arising from reinsurance contracts | - | 10,347 | 10,347 |
| | 376,455 | 57,078 | 433,533 |

## 39. FINANCIAL INSTRUMENTS BY CATEGORY (CONTINUED)

LIABILITIES AS PER STATEMENT OF FINANCIAL POSITION

| | Liabilities at fair value through profit or loss | Measured at amortised cost | Total |
|---|---|---|---|
| | $'000 | $'000 | $'000 |
| **GROUP** | | | |
| **Year ended 30 June 2013** | | | |
| Life investment contract liabilities | 338,214 | - | 338,214 |
| Derivative financial instruments | 2,557 | - | 2,557 |
| Payables and other financial liabilities | - | 26,978 | 26,978 |
| Interest bearing liabilities | - | 65,778 | 65,778 |
| | 340,771 | 92,756 | 433,527 |
| **Year ended 30 June 2012** | | | |
| Life investment contract liabilities | 298,949 | - | 298,949 |
| Derivative financial instruments | 173 | - | 173 |
| Payables and other financial liabilities | - | 27,714 | 27,714 |
| Interest bearing liabilities | - | 63,660 | 63,660 |
| | 299,122 | 91,374 | 390,496 |

As per note 17(b) the instrument related to FCGBL has been measured on a realisable value basis (2012: realisable value basis).

| | Liabilities at fair value through profit or loss | Measured at amortised cost | Total |
|---|---|---|---|
| **PARENT** | | | |
| **Year ended 30 June 2013** | | | |
| Life investment contract liabilities | 338,214 | - | 338,214 |
| Derivative financial instruments | 2,557 | - | 2,557 |
| Payables and other financial liabilities | - | 26,957 | 26,957 |
| | 340,771 | 26,957 | 367,728 |
| **Year ended 30 June 2012** | | | |
| Life investment contract liabilities | 298,949 | - | 298,949 |
| Derivative financial instruments | 173 | - | 173 |
| Payables and other financial liabilities | - | 27,641 | 27,641 |
| | 299,122 | 27,641 | 326,763 |

## 40. RELATED PARTY TRANSACTIONS

### (A) PARENT ENTITIES

The ultimate parent entity within the Group is Fidelity Life Assurance Company Limited.

### (B) DIRECTORS

The names of persons who were Directors of the Company at any time during the financial year are as follows: Ian Braddock; Jeff Meltzer; Carole Durbin; Colin Wise; Anne Blackburn.

### (C) KEY MANAGEMENT PERSONNEL COMPENSATION

Key management personnel compensation for the year ended 30 June 2013 and the year ended 30 June 2012 is set out below. The key management personnel are all the Directors of the Company and the executives with the greatest authority for the strategic direction and management of the Company.

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Short term benefits | 2,730 | 2,518 |
| **Total** | 2,730 | 2,518 |

### (D) OTHER TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL OR ENTITIES RELATED TO THEM

Information on transactions with key management personnel or entities related to them, other than compensation, are set out below.

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Loans to key management personnel, or entities related to them, comprise: | | |
| Secured loans: | | |
| Secured loans at 1 July | 1,946 | 1,844 |
| Secured loans advanced during the year | 34 | 119 |
| Loan repayments received – secured loans | (707) | (17) |
| **Secured loans at 30 June** | 1,273 | 1,946 |
| **Interest revenue from secured loans** | 90 | 105 |

All transactions are at arms length.

### (E) TRANSACTIONS WITH RELATED PARTIES

The following transactions occurred with related parties:

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Commissions paid in the year to shareholders as at 30 June who held agency agreements with the Company | 2,950 | 2,129 |

All transactions are at arms length.

## 40. RELATED PARTY TRANSACTIONS (CONTINUED)

### (F) OUTSTANDING BALANCES

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

| | Group | | Parent | |
|---|---|---|---|---|
| | 2013 $'000 | 2012 $'000 | 2013 $'000 | 2012 $'000 |
| Fidelity Funds Management Limited | - | - | (7) | (7) |
| Fidelity Global Shares Fund | 13 | (1,913) | 13 | (1,913) |
| Fidelity Global Bond Fund | 13 | - | 13 | - |
| Fidelity KiwiSaver Scheme | (50) | - | (50) | - |
| Loans made to shareholders | 2,433 | 3,409 | 2,433 | 3,409 |
| Agency accounts with shareholders | | | | |
| Due to Shareholder | (66) | (92) | (66) | (92) |

At 30 June 2012 the Group and Company held money on deposit in an Australian denominated bank account on behalf of Fidelity Global Shares Fund. The payable balance was settled in cash to Fidelity Global Shares Fund in July 2012.

During the year Fidelity Life paid audit fees on behalf of Fidelity Global Shares Fund and Fidelity Global Bond Fund and recharged these costs to the entities as applicable. There were no other transactions with these entities for the year.

Fidelity Life, as manager of the Fidelity KiwiSaver Scheme, has identified errors in the members' PIE tax calculation. Overall, this has resulted in a net overpayment of PIE tax to the Inland Revenue. The Manager will claim the excess tax from the Inland Revenue on behalf of members for reimbursement at the earliest practicable date. Above a threshold of three dollars, Fidelity Life will compensate members, in accordance with the requirements of the trustee, for the loss of income arising from these overpayments to the Inland Revenue up to the date that the members are reimbursed. A best estimate of this compensation is $50,000; but the level of final compensation up to the date of final payment is still to be determined.

### (G) TERMS AND CONDITIONS

**Secured loans**

The secured loans are for periods of up to 25 years repayable in cash, at interest rates of 5.7% per annum (2012: 5.7% per annum), and are secured by first mortgages over individuals' residences or investment properties.

**Unsecured loans**

No unsecured loans were made to key management personnel or entities related to them during the year (2012: nil). Where an unsecured loan is extended interest is payable at the prescribed Inland Revenue Department Fringe Benefit Tax rate or higher.

**Commissions paid to shareholders**

Commissions paid to shareholders who hold agency agreements with the Company are paid at standard rates applicable to other commission agents.

**Outstanding balances with related parties**

Subsidiary advances are payable on demand. Outstanding balances are unsecured, do not bear interest and are repayable in cash.

**Loans made to shareholders**

Loans secured by mortgages over properties or other assets are made to shareholders during the normal course of business and at arms length. In the year the average annual interest rate was 5.7% (2012: 5.7%) on a mixture of fixed and floating rates. The loans are for periods of up to 25 years.

## 41. GUARANTEES

### FIDELITY KIWISAVER SCHEME – CAPITAL GUARANTEED KIWI FUND

The Company provides a guarantee to the Trustee on behalf of members who hold Units in the Capital Guaranteed Kiwi Fund ('CGK Fund'). The guarantee is given by the Company in its capacity as the manager of the Fidelity KiwiSaver Scheme ('Scheme'). Under the guarantee the Company guarantees that on 31 March 2014 the Unit Value of the CGK Fund will be not less than $2.502343. The Company further guarantees that the Unit Value of the CGK Fund on 31 March in each subsequent year will be no less than the Unit Value of the CGK Fund on the preceding 31 March. The Company is required to give effect to its obligations under the guarantee by transferring into the Scheme for the CGK Fund investment assets of a value sufficient to ensure the Unit Value of the CGK Fund meets the guaranteed value as at the relevant 31 March. The investment assets transferred must be authorised investments for the CGK Fund and are valued in accordance with the valuation methodology set out in the Scheme's Trust Deed.

The guarantee is conditional upon the Company's continued appointment as manager of the Scheme.

The Company's obligation to pay under the guarantee is at all times subordinated to its obligation to pay all life insurance policyholder liabilities of the Company and is not referable to the Fidelity Life Statutory Fund Number 1. This means that in a liquidation of the Company or otherwise, the Company will only be required to meet its obligations under the guarantee after all life insurance policyholder liabilities have been paid in full. The Company's obligations under the guarantee are also unsecured and will rank behind all secured and preferential creditors of the Company and equally with all other unsecured creditors. There are no restrictions on the amount of insurance policyholder liabilities or secured or unsecured creditors that the Company may incur during the term of the guarantee.

This guarantee terminated on 23 August 2013 due to the completion of the sale of management rights in the Fidelity KiwiSaver Scheme to Grosvenor Investment Management Limited ('GIML') and was replaced by a new guarantee. For details refer note 46.

The Company has a provision within policyholder liabilities for this guarantee of $40,000 (2012: $448,000).

### FIDELITY KIWISAVER SCHEME

The Company provides a death benefit to members of the Scheme. If a member dies while they are a member of the Scheme, on application by the member's personal representatives, the member's estate will be paid the death benefit "top up" if the member is eligible.

If the member's death is the result of an accident, and the value of the Member's Accumulation is less than $10,000, the Company will "top up" the death benefit payment to $10,000. This "top up" is only available if, at the date of the member's death, the member is making regular contributions and at the date of death was under the age of eligibility for NZ Superannuation but aged at least 10 years. If the member is under the age of 10 years the Company will top up any payment to $2,000. The value of any top up will be reduced by the total of any payments already made on hardship or disability grounds, or first home withdrawal.

The death benefit is not a life policy under the Insurance (Prudential Supervision) Act 2010 and is not referrable to the Fidelity Life Statutory Fund Number 1.

The Company's obligations to provide the death benefit will cease at the earlier of:

(a) 22 August 2014; or

(b) the date that the Scheme is merged into another KiwiSaver Scheme managed by GIML, GFSGL or a related company.

The Company has a provision within policyholder liabilities for this death benefit of $61,000 (2012: $52,000).

## 42. CONTINGENCIES

In relation to the Company's wholly owned subsidiary, FCGBL, The New Zealand Guardian Trust Company Limited (the 'Trustee') entered into a guarantee with Westpac Banking Corporation, New Zealand Branch (the 'Capital Guarantor') on 7 February 2007 to cover payment of the principal amount at maturity of the Capital Guaranteed Bonds to the extent that the principal amount of $75m is not paid in full by FCGBL from the liquidated proceeds of the investments. This guarantee is deemed a contingent asset available to the capital guaranteed bondholders to reimburse them for the original capital invested ($75m) if insufficient funds arise at the guarantee payment date, being the later of the maturity date of 15 July 2013 or the date at which the investments are liquidated in accordance with the transaction documents. Payment of interest is not guaranteed by the Capital Guarantor or any other person. The fair value of the guarantee has not been recognised in these financial statements.

In addition FCGBL has included in the provision for on-going expenses of $0.03m an allowance for on-going operating expenses to cover expenses expected to be incurred up to the maturity date. Fidelity Life has a contingent liability to the extent that additional expenses or liabilities above this provision are incurred up to and past the maturity date, however any amounts are not expected to be significant.

The Capital Guaranteed Bond matured after the reporting period on 15 July 2013. Refer to note 46 for information on the effect of the maturity.

The Group had no further contingent liabilities or assets as at 30 June 2013 (2012: nil).

## 43. COMMITMENTS

### (A) CAPITAL COMMITMENTS

There were no material capital commitments at balance date other than those disclosed elsewhere in the financial statements (2012: nil).

### (B) OPERATING LEASE COMMITMENTS : GROUP AND PARENT AS LESSEE

Leases are for:

- commercial office space in Tauranga, Wellington, Christchurch, Hamilton and Dunedin;
- photocopier rental;
- car parking.

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows: | | |
| Within one year | 204 | 204 |
| Later than one year but not later than five years | 234 | 397 |
| Later than five years | - | 5 |
| | 438 | 606 |

## 43. COMMITMENTS (CONTINUED)

### (B) OPERATING LEASE COMMITMENTS : GROUP AND PARENT AS LESSEE (CONTINUED)

The Group has entered into lease agreements with the right of renewal/extension of lease terms (being the conditional portion of the lease) as follows:

**Lease A (Christchurch):**

- 1 June 2014 right of renewal for a further non-cancellable lease to 31 May 2017

**Lease B (Dunedin):**

- 1 July 2015 right of renewal for a further non-cancellable lease to 30 June 2018

### (C) OPERATING LEASES: GROUP AND PARENT AS LESSOR

Leases are for commercial office space in Auckland.

| | Group and Parent | |
|---|---|---|
| | 2013 $'000 | 2012 $'000 |
| Commitments for minimum lease payments in relation to non-cancellable operating leases are receivable as follows: | | |
| Within one year | 384 | 809 |
| Later than one year but not later than five years | - | 242 |
| | 384 | 1,051 |

The Group has entered into lease agreements with tenants for the right of renewal/extension of lease terms (being the conditional portion of the lease) as follows:

**Tenant B:**

- 30 November 2013 right of renewal for a further non-cancellable lease to 29 November 2016; and
- 30 November 2016 right of renewal for a further non-cancellable lease to 29 February 2019.

## 44. RESTRICTIONS ON ASSETS

As at 30 June 2013 there are no restrictions on the use of assets invested for policyholder benefits, nor any restrictions on legal titles to assets.

From 1 July 2013 under the Insurance (Prudential Supervision) Act 2010 ('IPSA') Fidelity Life is required to have a statutory fund. Fidelity Life's statutory fund was implemented on 1 July 2013 and is called the Fidelity Life Statutory Fund Number 1. The Fidelity Life Statutory Fund Number 1 is established in the records of the Company and relates only to life insurance business, as defined under IPSA.

The purpose of a statutory fund is to ensure that the funds received and paid out in respect of life insurance policies are separately identifiable as being part of the statutory fund. The assets of the Fidelity Life Statutory Fund Number 1 are only available for the life insurance business. In addition the assets of the Fidelity Life Statutory Fund Number 1 enjoy certain protections under IPSA which are designed to ensure that the interests of holders of life insurance policies are given certain priority over the interests of other parties, such as unsecured creditors.

There are no other restrictions on the use of assets invested for policyholder benefits, nor any restrictions on legal titles to assets.

## 45. FIDUCIARY ACTIVITIES

Fidelity Fund Management Limited, a wholly owned subsidiary, acts as a trustee for a number of superannuation funds. The Company manages $191,034,000 (2012: $156,235,000) on behalf of this subsidiary.

As at 30 June 2013 the Company was the manager of the Fidelity KiwiSaver Scheme and the Golden Harvest Retirement Plan and as such managed $304,134,000 (2012: $250,962,000) on a fiduciary basis. The Company sold the management rights to the Fidelity KiwiSaver Scheme on 23 August 2013, refer to note 46 for further information. The Golden Harvest Retirement Plan was wound up effective 31 December 2011.

## 46. EVENTS OCCURRING AFTER BALANCE DATE

### (A) LICENSE TO CARRY ON INSURANCE BUSINESS IN NEW ZEALAND

Under Reserve Bank of New Zealand ('RBNZ') requirements all insurers who wish to continue to operate in New Zealand are required to have a full licence prior to 7 September 2013. Fidelity Life was granted a full licence on 2 August 2013.

### (B) PURCHASE OF LIFE INSURANCE POLICIES FROM TOWER HEALTH AND LIFE LIMITED AND THE GROUP RISK BUSINESS OF TOWER LIFE (N.Z.) LIMITED

On 1 August 2013, the Company completed an asset purchase of the in-force life insurance policies of TOWER Health and Life Limited and the group risk business of TOWER Life (N.Z.) Limited. Through the purchase, the Company took management of life insurance policies with an aggregate annual in-force premium in excess of $66m for individual risk and $16m for group risk.

As part of the transaction the Company acquired two companies, Life Operations Limited and Life and Advisory Services Limited. Life Operations Limited comprises the 69 staff positions transferring from the legacy TOWER operations; the tangible assets included in the purchase price; assigned intermediary contracts in relation to the in-force policies; and a number of commercial contracts related to the acquired business.

The Company entered into a Transition Services Agreement ('TSA') with TOWER Insurance Limited and TOWER Limited. The TSA outlines the responsibilities of both parties in relation to the separation and migration of business systems; and the provision of operational support for the transferring business.

The purchase price of $145.0m for the transaction was derived with reference to the value of in force business ('VIF') at September 2012. At completion, Fidelity Life paid $71.8m cash consideration with the balance in transferred liabilities and other assets. A mechanism in the Sale and Purchase Agreement ('SPA') provides for the final value ascribed to the transaction to be recalculated with reference to the VIF at the date of settlement, with an adjustment to the purchase price to be made. The transaction was funded through a combination of full risk transfer and a payment from capital reserves.

At the date of signing the financial statements these final calculations are still to be finalised, and are unable to be estimated with a high degree of certainty. In addition, due to the significant time period between September 2012 and the settlement date it is deemed that any disclosures derived with reference to the VIF at September 2012 would be materially different to the final position. Accordingly the amounts disclosed here are provisional.

## 46. EVENTS OCCURRING AFTER BALANCE DATE (CONTINUED)

### (C) SALE OF MANAGEMENT RIGHTS IN THE FIDELITY KIWISAVER SCHEME TO GROSVENOR INVESTMENT MANAGEMENT LIMITED

On 23 August 2013, the Company completed the sale of its management rights in the Fidelity KiwiSaver Scheme to Grosvenor Investment Management Limited ('GIML') and Grosvenor Financial Services Group Limited ('GFSGL') for consideration of $16.5m comprising cash and shares in GFSGL. The Company has an option to convert the shares to cash two years post completion, at the value struck on completion day. This amount represents the minimum receivable by Fidelity Life in relation to the transaction, with the potential for additional payments if the number of members in the Fidelity KiwiSaver Scheme increases by at least 2,000 in each of the two years post completion.

Through the sale, the Company has transferred the management rights to funds under management of more than $300.0m on behalf of around 64,800 KiwiSaver members. Fidelity Securities Limited, the Fund Manager of the five Fidelity wholesale funds (Fidelity Global Shares Fund, Fidelity Global Bond Fund, Fidelity Property Fund, Fidelity Asset Class Conservative Fund, and Fidelity Asset Class Growth Fund) was also sold to GIML, along with the management rights to the five wholesale funds.

In the financial statements at 30 June 2013 the Company does not ascribe a value to the management rights, but has recognised transaction costs incurred prior to balance date, see note 17(a). Accordingly the 2014 financial statements will include an estimated one-off profit for the $16.5m less the transaction costs incurred post balance date, estimated at $0.4m.

### (D) FIDELITY KIWISAVER SCHEME – CAPITAL GUARANTEED KIWI FUND

As of the 23 August 2013, the Company provides a guarantee to the Trustee on behalf of members of the Fidelity KiwiSaver Scheme ('Scheme') who hold Units in the Capital Guaranteed Kiwi Fund ('CGK Fund'). This guarantee replaces the prior guarantee in relation to the CGK Fund, as outlined in note 41, which terminated at completion of the sale of management rights in the Fidelity KiwiSaver Scheme to Grosvenor Investment Management Limited ('GIML'). Under the guarantee the Company guarantees that on 31 March 2014 the Unit Value of the CGK Fund will be not less than $2.502343. The Company is required to give effect to its obligations under the guarantee by transferring into the Scheme for the CGK Fund investment assets of a value sufficient to ensure the Unit Value of the CGK Fund meets the guaranteed value as at 31 March 2014. The investment assets transferred must be authorised investments for the CGK Fund and are valued in accordance with the valuation methodology set out in the Scheme's Trust Deed. The guarantee will terminate on satisfaction of this obligation.

The Company's obligation to pay under the guarantee is at all times subordinated to its obligation to pay all life insurance policyholder liabilities of the Company and is not referable to the Fidelity Life Statutory Fund Number 1 (refer note 44). This means that in a liquidation of the Company or otherwise, the Company will only be required to meet its obligations under the guarantee after all life insurance policyholder liabilities have been paid in full. The Company's obligations under the guarantee are also unsecured and will rank behind all secured and preferential creditors of the Company and equally with all other unsecured creditors. There are no restrictions on the amount of insurance policyholder liabilities or secured or unsecured creditors that the Company may incur during the term of the guarantee.

### (E) FIDELITY CAPITAL GUARANTEED BOND LIMITED ('FCGBL')

The Capital Guaranteed Bond matured after the reporting period on 15 July 2013. There was a shortfall of $9.1m in the liquidated proceeds of the investments requiring the capital guarantee to be called upon. Senior bondholders were repaid their capital investment of $75m in full on the maturity date, with no additional cost to the Company. The repayment sources were:

- a zero-coupon bond with a face value of $65,700,000 maturing 15 July 2013;
- a money market account of $165,000; and
- payment by the capital guarantor of $9,135,000.

Post this settlement there are no further obligations due to Senior or Junior bondholders.

There were no other events requiring adjustment to or disclosure in the financial statements other than those disclosed elsewhere.

## 47. SHARE BASED COMPENSATION

The Fidelity Life Employee Share Purchase Scheme (the 'Scheme') was established by the Company in 1988 to assist employees to become shareholders. No shares have been allocated since 2007. From time to time employees who had been with the Company for a period of at least one year were entitled to participate in the Scheme. Shares were issued to the Scheme at an issue price based on the fair value of the shares at the date of issue. Fair value was determined by the Board of Directors by reference to a combination of recent trading activity and an independent valuer's report. Allocated shares participate in dividends, but voting rights are held by the trustees of the Scheme. Neither the Company nor its related parties have rights with respect to the shares issued by the Scheme.

Ian Braddock, the chairman of the Company, and Milton Jennings, CEO, are trustees of the Scheme, as such, they have non-beneficial control of any shares in the Scheme not yet allocated to employees. The Trustees are appointed by the Company's board of directors. Other key management personnel are also included within the Scheme.

Shares are held in trust for employees and vest eight years from the end of the income tax year in which the shares were purchased.

The Scheme entitled employees to purchase shares in Fidelity Life Assurance Company Limited at a discount. This discount is recorded by the Company and Group as an employee benefit expense. Refer to note 15 for the expense incurred by the Company and Group for the year.

The fair value of the shares has been determined in reference to the latest arms length trading undertaken.

Movements in the number and carrying value of shares held by the employee trust comprise:

| | 2013 | 2012 | 2013 | 2012 |
|---|---|---|---|---|
| | Number | Number | $'000 | $'000 |
| Held by Trust at 1 July | 29,383 | 43,383 | 1,018 | 1,267 |
| Shares vested from Trust | (8,483) | (14,000) | (181) | (249) |
| **Balance at 30 June** | **20,900** | 29,383 | **837** | 1,018 |

At 30 June 2013, shares held in employee trust unvested were as follows:

| | Year of Grant | Number of Shares | Market Price | Grant Price |
|---|---|---|---|---|
| **Fidelity Life Employee Share Purchase Scheme** | | | | |
| | 2005 | 7,960 | 43.70 | 29.13 |
| | 2006 | 9,285 | 64.76 | 43.18 |
| | 2007 | 3,655 | 83.75 | 55.84 |

At any time during the vesting period the employee has an option to require the Group to re-purchase the shares at the lower of cost or fair value.

# *Independent Auditors' Report*
to the shareholders of Fidelity Life Assurance Company Limited

## *Report on the Financial Statements*
We have audited the financial statements of Fidelity Life Assurance Company Limited (the "Company") on pages 20 to 91, which comprise the statements of financial position as at 30 June 2013, the statements of comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and the notes to the financial statements that include a summary of significant accounting policies and other explanatory information for both the Company and the Group. The Group comprises the Company and the entities it controlled at 30 June 2013 or from time to time during the financial year.

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

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

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

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

We have no relationship with, or interests in, Fidelity Life Assurance Company Limited or any of its subsidiaries other than in our capacities as auditors, tax advisors and providers of other assurance related and advisory services. These services have not impaired our independence as auditors of the Company and the Group.

*PricewaterhouseCoopers, 188 Quay Street, Private Bag 92162, Auckland 1142, New Zealand*
*T: +64 9 355 8000, F: +64 9 355 8001, pwc.co.nz*

# *Independent Auditors' Report*
Fidelity Life Assurance Company Limited

***Opinion***

In our opinion, the financial statements on pages 20 to 91:

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

(ii) comply with International Financial Reporting Standards; and

(iii) give a true and fair view of the financial position of the Company and the Group as at 30 June 2013 and their financial performance and cash flows for the year then ended.

***Emphasis of Matter***

Without modifying our opinion, we draw attention to note 2(a) of the financial statements which describes the basis of accounting applied for the Company's subsidiary Fidelity Capital Guaranteed Bond Limited. The financial results and position of Fidelity Capital Guaranteed Bond Limited as consolidated into the Group's financial statements for the periods presented have been prepared on a realisation basis and presented as a discontinued operation. As disclosed in note 17 of the Company's financial statements, significant volatility in the investment market during August 2011 resulted in trading losses. An Event of Default occurred and the Guarantor provided a Close Out Notice in accordance with the Supplemental Trust Deed. After the reporting period, the Fidelity Capital Guaranteed Bond matured on 15 July 2013.

## *Report on Other Legal and Regulatory Requirements*

We also report in accordance with Sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993. In relation to our audit of the financial statements for the year ended 30 June 2013:

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

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

## *Restriction on Distribution or Use*

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

PricewaterhouseCoopers

Chartered Accountants
5 September 2013

Auckland

# APPOINTED ACTUARY'S REVIEW OF FIDELITY LIFE ASSURANCE COMPANY LIMITED

at 30 June 2013

This return is prepared under sections 77 and 78 of the Insurance (Prudential Supervision) Act 2010 which requires that a licensed insurer must ensure that the actuarial information contained in, or used in the preparation of, financial statements of the insurer and any group financial statements is reviewed by the Appointed Actuary.

In relation to Financial Statements for Fidelity Life Assurance Company Limited for both the insurer and group for the year ended 30 June 2013 and as that date, I confirm the following:

**Appointed Actuary:** John Laurence Smith

**Work undertaken:** The review of the actuarial information contained in, or used in the preparation of, financial statements of the insurer and group was conducted in accordance with the Solvency Standard for Life Insurance Business (RBNZ, August 2011).

**Scope and limitations:** The actuarial information reviewed was: (a) information relating to an insurer's calculations of premiums, claims, reserves, dividends, insurance and annuity rates, and technical provisions; and (b) information relating to assessments of the probability of uncertain future events occurring and the financial implications for the insurer if those events do occur; and (c) information specified in the Solvency Standard for Life Insurance Business as actuarial information for the purposes of this review.

There were no restrictions on the scope of my investigation.

The return is provided as a statutory disclosure by Fidelity Life Assurance Company Limited for both the insurer and group. No warranty is provided to third parties for any other purpose.

**Relationship with insurer:** I am a permanent employee of Fidelity Life Assurance Company Limited. I also own 2,650 shares of which 2,400 are owned directly and 250 are beneficially held on my behalf.

**Information:** I obtained all information and explanations that I required.

**Actuarial opinion:** In my actuarial opinion and from an actuarial perspective:

(i) the actuarial information contained in the insurer and group financial statements at and in the year to 30 June 2013 has been appropriately included in those statements;

(ii) the actuarial information used in the preparation of the insurer and group financial statements at and in the year to 30 June 2013 has been used appropriately.

**Solvency margin:** In my actuarial opinion and from an actuarial perspective:

Fidelity Life Assurance Company Limited (licensed insurer) is maintaining the solvency margin calculated under the solvency standard for life insurance business (IPSA 21(2)(b)).

**Statutory funds:** In my actuarial opinion and from an actuarial perspective:

Fidelity Life Assurance Company Limited (licensed insurer) after establishing a statutory fund will maintain the solvency margin in respect of the statutory fund calculated under the solvency standard for life insurance business (IPSA 21(2)(c)).

John L Smith

John Smith
**Appointed Actuary**

5 September 2013

# DIRECTORY/EXTERNAL SERVICES

## Board of Directors

**Ian L Braddock**
BCom CA MInstD
Chairman
Auckland
Chartered Accountant
Chairman: Leukaemia & Blood Cancer Endowment Fund Trust

**Colin G O Wise**
Auckland

**Jeff Meltzer**
JP BCom FCA MInstD AAMINZ
Auckland
Chartered Accountant
Partner: Meltzer Mason
Director: Housing New Zealand Corporation
Trustee: Fidelity Family Trust

**Carole Durbin**
BCom LLB(Hons) FInstD
Auckland
Director/Trustee: Southern Cross Healthcare Group
Consultant: Simpson Grierson

**Anne Blackburn**
MA
Auckland
Director: TSB Bank Limited, Fisher Funds Management Limited

## Company Officers

**Chief Executive Officer**
Milton Jennings BCom CA

**Chief Financial Officer**
Ed Eadie BSc(Hons)

**Appointed Actuary**
John Smith MSc FNZSA FIAA

## Consulting Actuary

Peter Davies
BBus Sc FNZSA FIAA

## Solicitors

DLA Phillips Fox
Simpson Grierson
Wilson Harle
McVeagh Fleming

## Bankers

ANZ Bank New Zealand Limited

## Auditors

PricewaterhouseCoopers

## Investment Adviser

MCA NZ Limited

## Investment Managers

AMP Capital Investors (New Zealand) Limited

Devon Funds Management Limited New Zealand

Grosvenor Financial Services Group Limited

State Street Global Advisors, Australia, Limited

Stewart Financial Group Limited

Tyndall Investment Management New Zealand Limited

Vanguard Investments Australia Limited

## Currency Adviser

Bancorp Treasury Services Limited

## Reinsurers

General Reinsurance Life Australia Limited

Hannover Life Re of Australasia Limited

Munich Reinsurance Company of Australasia Limited

RGA Reinsurance Company of Australia Limited

Swiss Re Life and Health Australia Limited

## Registered Office

Fidelity House
81 Carlton Gore Road
Newmarket
Auckland 1023
**Telephone** 09 373 4914
**Facsimile** 09 308 9953

## Hamilton Office

1st Floor
John Sullivan House
62 Tristram Street
Hamilton 3240
**Telephone** 07 929 4840
**Facsimile** 07 929 4841

## Tauranga Office

Level 1/Unit 3
9 Devonport Road
Tauranga 3110
**Telephone** 0800 434 335
**Facsimile** 07 579 5370

## Wellington Office

Fidelity House
Level 1, 191 High Street
Lower Hutt
Wellington 5045
**Telephone** 04 920 7477
**Facsimile** 04 586 8733

## Christchurch Office

Level 1
324 Cashel Street
Christchurch 8011
**Telephone** 03 377 2323
**Facsimile** 03 379 2818

## Dunedin Office

Ground Floor
Otago House
89 Princes Street
Dunedin 9016
**Telephone** 0508 566 726

**www.fidelitylife.co.nz**

40 YEARS

Fidelity Life

THE NEW ZEALAND LIFE COMPANY