FM Insurance Company Limited (New Zealand Branch)

Financial statements
for the year ended 31 December 2011

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for the year ended 31 December 2011

Contents

FM Insurance Company Limited (New Zealand Branch)

Directors' report for the year ended 31 December 2011

The directors present their report, together with financial statements of FM Insurance Company Limited (New Zealand Branch) for the financial year ended 31 December 2011.

No disclosure has been made in respect of Section 211(1)(a) and (e) to (j) of the Companies Act 1993 in accordance with Section 211(3) of the Act.

Corporate Information

The Registered Office of the Branch is:
C/-KPMG Centre
18 Viaduct Harbour Avenue
Auckland 1010

The Branch is a part of FM Insurance Company Limited (the "Company"). The Company is incorporated in the United Kingdom.

The Company is a wholly owned subsidiary of Factory Mutual Insurance Company (FMIC), the registered office of which is 270 Central Avenue, Johnston, RI 02919-4949, USA.

FM Insurance Company Ltd has a financial strength rating of A+ (Superior) issued by A M Best and AA (Very Strong) issued by Fitch Ratings.

Principal activities

The Branch's principal activities during the year continued to be the underwriting of property insurance risks and the provision of related engineering and loss prevention services to large and medium sized clients.

Results

The results of the Branch's operations for the financial year are set out on page 6 and the financial position of the Branch at the end of the financial year is set out on page 7.

Dividends

The directors do not recommend the payment of a dividend (2010: $Nil).

Review of the business

Gross premium income increased to $22,368,484 from $16,108,051 during the year. The Branch made a post tax loss of $(1,536,559) during the year. The loss is attributable to natural catastrophe claims arising from the Christchurch earthquake.

The loss for the year, and other movements described in the Statement of changes in equity, resulted in an overall decrease in Total Deemed Equity to a deficit of $(4,116,275) as at 31 December 2011.

Significant changes in state of affairs

Significant changes in the state of affairs of the Branch during the financial year were as follows:

- Appointments to the executive management team were: Andrew Stafford.
- Resignations to the executive management team were: Lynette Schultheis.

There were no other changes to the executive management team.

Events subsequent to reporting date

No transactions or events occurred after the reporting date which significantly affected, or may significantly affect, the results of the Branch, the operations of the Branch, or the state of affairs of the Branch.

FM Insurance Company Limited (New Zealand Branch)

Directors' report
for the year ended 31 December 2011

Future developments

Insurance and investment operations are, by their nature, volatile due to the exposure to natural perils and industry cycles and thus, profit predictions are difficult.

The Company anticipates:

- Market conditions will be such during 2012 that premiums will increase from 2011 levels, reflecting industry trends consequential to the Christchurch earthquake;
- Operating results will improve in 2012 from 2011 levels, subject to natural catastrophe claims levels.

The Company lodged an application to the Reserve Bank of New Zealand during 2011 for a provisional license as required under the Insurance (Prudential Supervision) Act 2010. The new licensing regime commences from 7 March 2012, requiring all insurers to operate under a provisional or full license. All insurers must be operating under a full license by 7 September 2013.

Going concern

The directors believe the Company is able to manage its business risks successfully in any economic environment. Furthermore, the directors have a high expectation that the Company has adequate resources to continue in existence for the foreseeable future. As such, they continue to adopt the going concern basis in preparing the Branch annual financial statements.

Directors

The names of the Company's directors in office at any time during or since the end of the financial year are as follows:

Director	Title	Date Changed
Kenneth Davey	Executive director	
Omar Hameed	Executive director	
Kevin Ingram	Executive director	
Ian Berg	Executive director	
Shivan Subramaniam	Non executive director	
Jeffery Burchill	Non executive director	
Ruud Bosman	Following retirement from FM Global, Ruud Bosman remained on the Board, becoming an Independent Non executive director	Change effective 1 December 2011
Thomas Lawson	Non executive director	Appointed 11 October 2011
Kenneth Lever	Independent Non executive Director	Appointed 11 October 2011
Thomas Keevil	Independent Non executive Director	Appointed 11 October 2011
Peter Charles Wilson	Independent Non executive Director	Appointed 11 October 2011
Dennis J. Bessant		Resigned 26 July 2011
Carol Barton		Resigned 26 July 2011
Michael Lebovitz		Resigned 26 July 2011

FM Insurance Company Limited (New Zealand Branch)

Directors' report
for the year ended 31 December 2011

Directors were in office for the entire period unless otherwise stated.

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

Insurance of directors

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

Disclosure of information to the auditors

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

Non audit services

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

Re-appointment of auditors

Pursuant to a shareholders' resolution, the Company is not obliged to reappoint its auditor annually and Ernst & Young will therefore continue in office.

On behalf of the board

K. S. [signature] **Director** **Dated:** 30 May 2012

[signature] **Director** **Dated:** 30 May 2012

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Independent Auditor's Report

To the Shareholders of FM Insurance Company Limited

Report on the Financial Statements

We have audited the financial statements of the New Zealand branch of FM Insurance Company Limited on pages 6 to 33, which comprise the statement of financial position of the New Zealand branch of FM Insurance Company Limited as at 31 December 2011, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the 31 December 2011 then ended, and a summary of significant accounting policies and other explanatory information.

This report is made solely to the company's shareholders, as a body, in accordance with Section 19(3) of the Financial Reporting Act 1993. Our audit has been undertaken so that we might state to the company's shareholders those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the New Zealand branch of the company and the company's shareholders as a body, for our audit work, for this report, or for the opinions we have formed.

Directors' Responsibility for the Financial Statements
The directors are responsible for the preparation of the 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 control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). These auditing 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 our 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, we have considered the internal control relevant to the New Zealand branch of the company's preparation of the financial statements that give a true and fair view of the matters to which they relate in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the New Zealand branch of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the overall presentation of the financial statements.

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

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

Partners and employees of our firm may deal with the New Zealand branch of the company on normal terms within the ordinary course of trading activities of the business of the New Zealand branch of the company.

Opinion
In our opinion, the financial statements on pages 6 to 33:

- comply with generally accepted accounting practice in New Zealand; and
- give a true and fair view of the financial position of the New Zealand branch of the company as at 31 December 2011 and its financial performance and cash flows for the year then ended.

Ernst & Young

Report on Other Legal and Regulatory Requirements

In accordance with the Financial Reporting Act 1993, we report that:

- We have obtained all the information and explanations that we have required.
- In our opinion proper accounting records have been kept by the New Zealand branch of FM Insurance Company Limited as far as appears from our examination of those records.

Ernst + Young

Ernst & Young
Melbourne
30 May 2012

FM Insurance Company Limited (New Zealand Branch)

Statement of comprehensive income for the year ended 31 December 2011

	Note	2011 $	2010 $
Gross Premium Revenue	8	**22,368,484**	16,108,051
Outwards Reinsurance Expense	9	**(16,066,458)**	(11,207,231)
Net Premium Revenue		**6,302,026**	**4,900,820**
Gross Claims Expense	9	**(358,042,221)**	(67,587,966)
Reinsurance and Other Recoveries Revenue	8	**351,763,666**	62,145,008
Net Claims Expense		**(6,278,555)**	**(5,442,958)**
Net Acquisition and Underwriting Revenue	9	**2,758,294**	1,566,878
UNDERWRITING PROFIT		**2,781,765**	**1,024,740**
General and Administration Expenses	9	**(4,357,271)**	(2,252,366)
Investment Income	8	**38,947**	47,196
OPERATING LOSS BEFORE INCOME TAX		**(1,536,559)**	**(1,180,430)**
Income Tax Expense		**0**	(161,598)
OPERATING LOSS AFTER INCOME TAX		**(1,536,559)**	**(1,342,028)**
Other Comprehensive Income / (Expense), net of tax		**0**	0
TOTAL COMPREHENSIVE LOSS FOR THE YEAR		**(1,536,559)**	**(1,342,028)**
Operating loss for the year attributable to:			
Non-controlling Interest		**0**	0
Owners of the Parent		**(1,536,559)**	(1,342,028)
Operating loss after income tax		**(1,536,559)**	**(1,342,028)**
Total comprehensive loss for the year attributable to:			
Non-controlling Interest		**0**	0
Owners of the Parent		**(1,536,559)**	(1,342,028)
Total comprehensive loss after tax		**(1,536,559)**	**(1,342,028)**

The above Statement of comprehensive income should be read in conjunction with the notes to the financial statements.

FM Insurance Company Limited (New Zealand Branch)

Statement of financial position
at 31 December 2011

	Note	**2011** $	2010 $
Assets			
Trade and other receivables	*13*	**102,529,352**	12,819,946
Deferred reinsurance expense	*15*	**9,705,413**	4,785,700
Reinsurance and other recoveries on outstanding claims	*14*	**161,654,830**	50,861,076
Investments	*12*	**525,315**	525,473
TOTAL ASSETS		**274,414,910**	**68,992,195**
Liabilities			
Intercompany account	*7*	**40,312,801**	1,057,175
Trade and other payables	*16*	**8,156,924**	2,173,777
Unearned premium reserve	*15*	**13,387,842**	6,807,580
Deferred reinsurance commission		**915,217**	860,625
Unexpired risk liability	*15*	**349,571**	0
Outstanding claims provision	*14*	**215,408,830**	60,672,754
TOTAL LIABILITIES		**278,531,185**	**71,571,911**
NET ASSETS		**(4,116,275)**	**(2,579,716)**
DEEMED EQUITY: HEAD OFFICE ACCOUNT		**(4,116,275)**	**(2,579,716)**

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

FM Insurance Company Limited (New Zealand Branch)

Statement of changes in equity for the year ended 31 December 2011

2010	**Retained**	**Other**	**Total Deemed**
	$	$	**$**
Balance at the beginning of the financial year	**(377,063)**	**0**	**(377,063)**
Loss for the year	(1,342,028)	0	**(1,342,028)**
Other comprehensive income / (expense), net of tax	0	0	**0**
Restatement of prior year comparative recognising deferred reinsurance commission	(860,625)	0	**(860,625)**
Total comprehensive income / (expense) for the year	**(2,579,716)**	**0**	**(2,579,716)**
Transactions with owners	0	0	**0**
Balance at the end of the financial year	**(2,579,716)**	**0**	**(2,579,716)**

2011	**Retained**	**Other**	**Total Deemed**
	$	$	**$**
Balance at the beginning of the financial year	**(2,579,716)**	**0**	**(2,579,716)**
Loss for the year	(1,536,559)	0	**(1,536,559)**
Other comprehensive income / (expense), net of tax	0	0	**0**
Total comprehensive income / (expense) for the year	**(4,116,275)**	**0**	**(4,116,275)**
Transactions with owners	0	0	**0**
Balance at the end of the financial year	**(4,116,275)**	**0**	**(4,116,275)**

The above Statement of changes in equity should be read in conjunction with the notes to the financial statements.

Notes to the financial statements for the year ended 31 December 2011

1 Reporting entity

The Registered Office of the Branch is:
C/-KPMG Centre
18 Viaduct Harbour Avenue
Auckland 1010

The Branch is a part of FM Insurance Company Limited (the “Company”). The Company is incorporated in the United Kingdom.

The Company is a wholly owned subsidiary of Factory Mutual Insurance Company (FMIC), the registered office of which is 270 Central Avenue, Johnston, RI 02919-4949, USA. FMIC (the “Parent”) is the largest Group in which the financial results of FMI are included. Copies of the Group accounts are available to the public either at the above address or from www.fmglobal.com.

FM Insurance Company Ltd has a financial strength rating of A+ (Superior) issued by A M Best and AA (Very Strong) issued by Fitch Ratings.

The Branch’s principal activities during the year continued to be the underwriting of property insurance risks and the provision of related engineering and loss prevention services to large and medium sized clients.

The financial statements were authorised for issue by the board of directors on 30 May 2012.

2 Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 1993 (as amended by the Financial Reporting Amendment Act 2011) and the Companies Act 1993.

These financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand. They comply with the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards, as appropriate for profit-oriented entities that qualify and apply differential reporting concessions.

The Branch qualifies for differential reporting exemptions as described in the Framework for Differential Reporting issued by the Institute of Chartered Accountants New Zealand because the Branch is not publicly accountable and there is no separation between the shareholders and the governing body. The Branch has elected to take advantage of differential reporting concessions available to it except those available under NZ IAS 18 which allows revenue and expenses to be recognised inclusive of goods and services tax.

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following material items in the Statement of financial position:

- Measurement of investments at fair value;
- Measurement of the outstanding claims liability and related reinsurance and other recoveries at present value.

(c) Fair value

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

(d) Present value

Present value is the amount of an asset or liability using appropriate risk free discount rates.

(e) Functional and presentation currency

The financial statements are presented in New Zealand dollars ($), which is the Branch's functional currency.

(f) Use of estimates and judgements

The preparation of the financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The areas where estimates and assumptions involve a high degree of judgement or complexity and are considered significant to the financial statements are:

- Claims; and
- Reinsurance and other recoveries on outstanding claims.

(g) Reclassification of comparatives

Certain items have been reclassified from the Branch's prior year financial statements to conform to the current period's classification. There is no impact to the result for the period.

Reclassified items are described below:

- Internal loss adjustment expenses have been reclassified from "General and administration expenses" to "Gross claims expense"
- Reinsurance commission has been reclassified from "General and administration expenses" to "Acquisition and underwriting expenses"
- Unrealised net gains (losses) relating to revaluation of government bond have been reclassified from "General and administration expenses" to "Investment income".

(h) Changes in accounting policies

There were no changes in accounting policies during the current reporting period.

(i) Retrospective restatement of comparatives

A retrospective adjustment has been made to prior period comparative information of the Branch in respect of deferred reinsurance commission, reflecting correct treatment under NZIFRS. Deferred reinsurance commission was not recognised in the prior year financial statements. The table below highlights the principal adjustment made by the Branch in restating its position as at 31 December 2010.

	2010 Previously reported $	Adjustment $	2010 Restated $
Liabilities			
Deferred Reinsurance Commission	0	860,625	860,625

(j) Rounding

Except as otherwise indicated, financial information presented in New Zealand dollars has not been rounded.

(k) Recently issued standards (effective for years beginning from 1 January 2013)

In 2011 the International Accounting Standards Board (IASB) issued the following accounting standards that will be incorporated into NZ IFRS:

- NZ IAS 27 Separate Financial Statements
- NZ IAS 28 Investments in Associates and Joint Ventures
- NZ IFRS 10 Consolidated Financial Statements
- NZ IFRS 11 Joint Arrangements
- NZ IFRS 12 Disclosure of Interest in Other Entities
- NZ IFRS 13 Fair Value Measurement

Upon preliminary review management do not expect these standards to have a have a material impact on the Branch's financial statements in future periods.

3 Significant accounting policies

(a) Premiums

Premium revenue comprises amounts charged for insurance contracts. Premium is recognised as earned from the date of attachment of risk (generally the date a contract is agreed to but may be earlier if persuasive evidence of an arrangement exists) over the period of the related insurance contracts in accordance with the pattern of the incidence of risk accepted under the contracts. The pattern of the risks underwritten is generally matched by the passing of time. Premium for unclosed business (business written close to reporting date where attachment of risk is prior to reporting date) is recognised as revenue.

The unearned portion of premium is recognised as an unearned premium reserve on the Statement of financial position.

Premium receivable is recognised as the amount due and is normally settled between 60 days and 120 days. The recoverability of premium receivable is assessed and provision is made for impairment based on objective evidence and having regards to past default experience. Premium receivable is presented on the Statement of financial position net of any provision for impairment.

(b) Outwards reinsurance

Gross reinsurance premiums are recognised as an expense on the earlier of the date when premiums are payable or when the policy becomes effective.

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

Unearned reinsurance premiums are those proportions of premiums written in a year that relate to periods of risk after the reporting date. Unearned reinsurance premiums are deferred over the term of the underlying direct insurance policies.

(c) Claims

The outstanding claims liability is measured as the central estimate of the present value of expected future payments relating to claims incurred at the reporting date with an additional risk margin to allow for the inherent uncertainty in the central estimate. The liability is measured based on valuations performed by, or under the direction of, the Appointed Actuary. The expected future payments include those in relation to claims reported but not yet paid or not yet paid in full, claims incurred but not enough reported (IBNER), claims incurred but not reported (IBNR) and the anticipated direct and indirect claims handling costs. The liability is discounted to present value using a risk free rate.

The estimation of the outstanding claims liability involves a number of key assumptions and is the most critical accounting estimate. All reasonable steps are taken to ensure that the information on paid claims exposures is appropriate. However, given the uncertainty in establishing the liability, it is likely that the final outcome will be different from the original liability established. Changes in claims estimates are recognised in profit or loss in the reporting period in which the estimates are changed.

Claims expense represents claim payments adjusted for the movement in the outstanding claims liability.

(d) Reinsurance and other recoveries

Reinsurance and other recoveries received or receivable on paid claims and on outstanding claims (notified and not yet notified) are recognised as income. Reinsurance recoveries on paid claims are presented as part of receivables net of any provision for impairment based on objective evidence for individual receivables. Reinsurance and other recoveries on outstanding claims are measured as the present value of the expected future receipts calculated on the same basis as the outstanding claims liability. Reinsurance does not relieve the originating insurer of its liabilities to policyholders and is presented separately on the Statement of financial position.

(e) Liability adequacy test

The liability adequacy test is an assessment of the carrying value of the unearned premium liability and is conducted at each reporting date. If current estimates of the present value of the expected future cash flows relating to future claims arising from the rights and obligations under current general insurance contracts, plus an additional risk margin to reflect the inherent uncertainty in the central estimate, exceed the unearned premium liability (net of reinsurance) less relevant deferred acquisition costs (if any), then the unearned premium liability is deemed to be deficient. The test is performed at the level of a portfolio of contracts that are subject to broadly similar risks and that are managed together as a portfolio. In these accounts, this represents the overall New Zealand portfolio of contracts. Any deficiency arising in the test is recognised in the profit or loss with the corresponding impact on the Statement of financial position recognised first through the write down of deferred acquisition costs (if any) for the relevant portfolio of contracts, with any remaining balance being recognised on the Statement of financial position as an unexpired risk liability.

(f) Cash at bank

Cash at bank includes highly liquid financial assets with maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Branch in the management of its short-term commitments.

(g) Investments

Investments comprise assets held to back insurance liabilities (also referred to as technical reserves) and assets that represent deemed equity funds. Investments presently comprise of New Zealand government bonds.

All investments are designated as fair value through profit or loss upon initial recognition. They are initially recorded at fair value (being the cost of acquisition excluding transaction costs) and are subsequently re-measured to fair value at each reporting date.

(h) Creditors and accruals

Creditors and accruals are carried at cost, which is the fair value of the consideration to be paid in the future for the goods and services received. The amounts are discounted where the effect of the time value of money is material.

(i) Investment Income

Interest income is accounted for on an accrual basis and recognised in the Statement of comprehensive income.

Changes in the fair value of investments from the previous reporting date (or cost of acquisition excluding transaction costs if acquired during the financial period) are recognised as realised or unrealised gains or losses in profit or loss.

(j) Foreign currency

Transactions in foreign currencies are translated into the functional currency of the Branch at average exchange rates for the months in which the transactions occur.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on translation are recognised in profit or loss.

4 Risk management

The Branch has exposure to various risks including:

- Insurance risk;
- Market risk;
- Credit risk;
- Liquidity risk;
- Operational risk;
- Compliance risk; and
- Group risk.

This note presents information about the Branch's exposure to each of the above risks and the framework for identifying, analysing, evaluating, managing and monitoring risk.

(a) Risk management framework

<u>Group framework</u>

The Group has in place a risk management framework which provides reasonable assurance that the material risks are being prudently and soundly managed. At the same time it is acknowledged that all business activity entails risk so the focus is on management of this risk rather than complete risk avoidance.

The overall Group objectives and strategies are consistent globally with each operation conducting business the same way anywhere in the world, within the constraints of local regulations. This applies particularly to underwriting, capacity utilization, risk engineering and claims handling, for which comprehensive standards apply Company-wide.

At the Group level FMIC has an Enterprise Risk Management Committee (ERMC) and this is linked in by direct participation or reporting to the strategic planning and risk management processes undertaken by the following Groups:

- FMIC Global Planning Committee;
- FMIC Global Integration Committee;
- FMI Board of Directors;
- FMI Risk Management Committee; and
- Individual Operations including the Branch Risk Management sub-committee.

This framework provides a coherent strategic organization within the Group. The responsibility of risk management is thus shared appropriately with ultimate responsibility apportioned to the parent Company Board, with the Chairman and CEO oversight.

Company framework

In order to provide independent oversight of the Company's risks and risk management a FMI Risk Management Committee has been established. It is an executive committee in that it has the power to make decisions regarding the Company's risk management policies and practice.

The Committee takes input from, and provides feedback to, all FMI operating business units and Branches, periodically requires attendance from them, and circulates all minutes of meetings. It may also make recommendations to the senior management, or the Board and is accountable to the FMI Board and Risk & Compliance Committee.

Through a combination of systems, structures and processes within the global Company, risks are assessed, mitigated and monitored. An on-line Risk Register has been established and includes all risks identified by the Company. Separate Risk Registers have also been established as required for significant operating business units of the Company.

Branch framework

The Branch has established a risk management framework. The framework takes into account the interests of the Branch, the broader Group and external stakeholders such as clients and regulators. The Operations Manager is responsible for the role of risk management in Australia, and the development of both the Risk Management Strategy (RMS) and the framework. Assistance is provided by the FMI Risk Management Committee. The framework is designed to address risks arising out of the Branch operations and Business Plan. Any risks which have been identified as of particular importance to the Branch would be identified in the Branch Risk Register.

Closely aligned to the FMI Risk Management Committee, an Australian Branch Risk Management Sub-committee has been established.

The RMS is reviewed and approved by the Board and forwarded to the regulator being the *Australian Prudential Regulation Authority* (APRA) annually. The RMS:

- Is a high level, strategic document intended to describe key elements of the risk management framework;
- Describes board and management approved parameters (e.g. risk appetite) within which key decisions must be made;
- Describes management strategies and responsibilities, as well as the key processes to identify, assess, monitor, report on and control or mitigate all material risks, financial and non financial, likely to be faced; and
- Is a key input into how regulators understand and assess the approach to risk management.

Control mechanisms include:

- Policies
  - Procedural standards have been established Company wide, and are followed by the Branch. In addition, specific Branch policies have been established as required to respond to local requirements and practices.

- Reporting
  - Each operation throughout the Company issues monthly and quarterly reports on Key Result Areas (KRA's) and objectives, including to the board of FMI via the Managing Director of FM Insurance Company Ltd.
  - The Company has a global platform for data and processing which provides management information for all disciplines; and
  - Reviews of any new risk exposures identified are conducted and recorded in the Risk Register.

- Monitoring
  - The Australian Operations Manager is responsible for the ongoing monitoring of compliance within the Branch;
  - The Company's Compliance Officer (based in the UK) is responsible for ensuring Branch compliance and providing oversight for the Branch;
  - Management meetings and the meetings of the Australian Risk Management Committee provide a regular forum to review business issues and compliance concerns that may arise in that regard; and
  - Visits to the Branch by the Legal and Compliance function of FMI take place on a regular basis.

(b) Insurance risk

Background

A key risk from operating in the general insurance industry is the exposure to insurance risk arising from underwriting general insurance contracts. The insurance contracts transfer risk to the insurer by indemnifying the policyholders against adverse effects arising from the occurrence of specified uncertain future events. There is a risk that the actual amount of claims to be paid in relation to contracts will be different to the amount estimated at the time a product was designed and priced. The Branch is exposed to this risk because the price for a contract must be set before the losses relating to the product are known. Hence the insurance business involves inherent uncertainty.

A fundamental part of the Company's overall risk management strategy is the effective governance and management of the risks that impact the amount, timing and uncertainly of cash flows arising from insurance contracts.

Mitigating insurance risk

The insurance activities primarily involve the underwriting of risks and the management of claims.

The policies and procedures for the management of insurance risk are applied consistently across the Company with certain allowances made for local circumstances.

Key policies and processes include the following:

- Reinsurance
    - Reinsurance is used to limit exposure to large single claims and accumulation of claims that arise from the same event or the accumulation of similar events;
    - While a large portion of the business ceded by the Branch is reinsured with the Company's parent, the Branch can, and does, purchase additional external reinsurance protection. This generally relates to facultative reinsurance covers; and
    - The use of reinsurance introduces credit risk. The management of reinsurance includes the monitoring of reinsurers' credit risk and controls the exposure to reinsurance counterparty default. Refer to the financial risk management note for further details.

- Claims management and provisioning
    - Initial claims determination is managed by claims officers with the requisite degree of experience and competence with the assistance, where appropriate, of a loss adjustor or other party with specialist knowledge. It is the Company's policy to respond to and settle all genuine claims quickly whenever possible and to pay claims fairly, based on policyholders' full entitlements; and
    - Claims provisions are established using actuarial valuation models and include a risk margin for uncertainty (refer to the claims note).

(c) Market risk

Market risk is the risk that changes in market prices, such as interest rates and foreign exchange rates will affect the Branch's interest income, claims expense or the value of its holdings of financial instruments.

Policies and procedures designed to address this risk include various measures contained within the Branch's Capital Management Strategy (CMS).

(d) Credit risk

Credit risk is the risk of financial loss to the Branch if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Branch's premium receivables from brokers or policy holders, reinsurance receivables from reinsurers and investments.

Policies and procedures designed to address this risk include premium debtor follow-up and monitoring processes, reinsurer counterparty rating requirements and concentration limits, and investment counterparty rating requirements and concentration limits.

(e) Liquidity risk

Liquidity risk is the risk that the Branch will encounter difficulty in meeting obligations associated with its financial liabilities as they fall due, or can only secure such resources at a prohibitive cost.

Policies and procedures designed to address this risk include maintaining high solvency levels in excess of regulator requirements, holding of highly liquid investments, access to capital of the Company, access to pre-funding of reinsurance recoveries from the Parent.

(f) Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes, including business processes, personnel, technology and infrastructure, and from external factors.

The Branch's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Branch's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address this risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Company standards for the management of operational risk, including the following areas:

- Requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- Requirements for the reconciliation and monitoring of transactions;
- Documentation of controls and procedures;
- Requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- Development of contingency plans;
- Training and professional development; and
- Ethical and business standards.

Compliance with these standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the Audit Committee and senior management of the Group.

(g) Compliance risk

Compliance risk is the risk of either ineffective relationships with our insurance regulators or non-compliance with various laws, regulations and codes to which the Branch is required to adhere.

Policies and procedures designed to address this risk include regular meetings with regulators, engagement of consultants and advisors as required, filings & returns calendars, and periodic reviews undertaken by Legal & Compliance.

(h) Group risk

Group risk is the risks the Branch is exposed to as a member of the Factory Mutual Insurance Company (FMIC) Group. These may deplete or divert financial resources held by the Branch to meet liabilities arising from Group.

5 Regulatory capital

The lead regulator is the *Australian Prudential Regulation Authority* (APRA) which sets and monitors capital requirements for the combined Australian and New Zealand Branches as a whole.

The combined Australian and New Zealand Branches are compliant with all externally imposed capital requirements.

The overall Company is supervised by the *Financial Services Authority* (FSA) in the United Kingdom.

The Company's policy is to maintain a strong capital base so as to ensure creditor and market confidence and to sustain future development of the business.

The lead regulator for the New Zealand Branch is expected to change in 2013 to the *Reserve Bank of New Zealand* (RBNZ) following approval of a full license under new licensing rules in that country.

6 Operating segments

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

7 Financial assets & liabilities

The table below sets out the carrying amounts and fair values of the Branch's financial assets and liabilities:

	Note	Fair value through profit and loss	Amortised cost	**2010**
		$	$	**$**
Assets				
Investments	*12*	525,473	0	**525,473**
Trade and other receivables	*13*	0	12,819,946	**12,819,946**
Total Assets		525,473	12,819,946	**13,345,419**
Liabilities				
Intercompany account		0	1,057,175	**1,057,175**
Trade and other payables	*16*	0	2,173,777	**2,173,777**
Total Liabilities		0	3,230,952	**3,230,952**

		Fair value through profit and loss	Amortised cost	**2011**
		$	$	**$**
Assets				
Investments	*12*	525,315	0	**525,315**
Trade and other receivables	*13*	0	102,529,352	**102,529,352**
Total Assets		525,315	102,529,352	**103,054,667**
Liabilities				
Intercompany account		0	40,312,801	**40,312,801**
Trade and other payables	*16*	0	8,156,924	**8,156,924**
Total Liabilities		0	48,469,725	**48,469,725**

8 Analysis of Income

	Note	2011	2010
		$	$
Premium Revenue			
Gross written premium		**28,948,746**	16,325,497
Movement in unearned premium liability		**(6,580,262)**	(217,446)
Premium revenue		**22,368,484**	16,108,051
Reinsurance Revenue			
Reinsurance and other recoveries on paid claims		**240,969,912**	11,386,989
Movement in reinsurance and other recoveries on outstanding claims		**110,793,754**	50,758,019
Reinsurance and other recoveries revenue	*11*	**351,763,666**	62,145,008
Investment Income			
Interest on government stock		**32,500**	32,500
Other interest		**6,290**	12,275
Interest income		**38,790**	44,775
Realised net gains (losses)		**0**	0
Unrealised net gains (losses)		**157**	2,421
Net changes in fair value of investments		**157**	2,421
Total investment income		**38,947**	47,196
Total Income		374,171,097	78,300,255

9 Analysis of expenses

	Note	**2011** **$**	2010 $
Outwards Reinsurance Expense			
Outwards reinsurance paid		**20,986,171**	11,380,593
Movement in deferred reinsurance expense		**(4,919,713)**	(173,362)
Outwards reinsurance expense		**16,066,458**	11,207,231
Gross Claims Expense			
Claims paid, including external loss adjustment expense		**202,602,668**	7,456,075
Movement in outstanding claims		**154,736,076**	59,769,620
Internal loss adjustment expense		**703,477**	362,271
Gross claims expense	*11*	**358,042,221**	67,587,966
Net Acquisition and Underwriting Revenue			
Reinsurance commission received		**(3,162,457)**	(1,566,878)
Movement in deferred reinsurance commission		**54,592**	0
Movement in unexpired risk liability		**349,571**	0
Net Acquisition and underwriting revenue		**(2,758,294)**	(1,566,878)
General and Administration Expense			
Auditor remuneration		22,347	20,000
Other general and administration expense		**5,038,401**	2,594,637
Internal loss adjustment expense		**(703,477)**	(362,271)
General and administration expense		**4,357,271**	2,252,366
Total expenses		375,707,656	79,480,685

Notes to the financial statements
for the year ended 31 December 2011

10 Auditor remuneration

	2011	2010
	$	$
Assurance Services - Ernst & Young		
Audit of the financial statements	**22,347**	20,000
Audit of statutory returns in accordance with regulatory requirements	**0**	0
Total assurance services	**22,347**	**20,000**

11 Net Claims expense

	Note	2011	2010
		$	$
Gross claims expense - undiscounted		345,509,391	65,110,873
Discount to present value		(3,298,000)	(2,931,486)
Gross claims expense - discounted		342,211,391	62,179,387
Risk margin		15,830,830	5,408,579
Gross claims expense	*9*	358,042,221	67,587,966
Reinsurance and other recoveries revenue - undiscounted		342,709,836	60,020,752
Discount to present value		(2,342,000)	(2,487,486)
Reinsurance and other recoveries revenue - discounted		340,367,836	57,533,266
Risk margin		11,395,830	4,611,742
Reinsurance and other recoveries revenue	*8*	351,763,666	62,145,008
Net claims expense - undiscounted		2,799,555	5,090,121
Net discount to present value		(956,000)	(444,000)
Net claims expense - discounted		1,843,555	4,646,121
Net risk margin		4,435,000	796,837
Net claims expense - discounted including risk margin		**6,278,555**	**5,442,958**

12 Investments

	2011	2010
	$	$
Interest bearing investments		
Government bond	**525,315**	**525,473**

13 Trade and other receivables

The receivables are non-interest bearing and are normally settled between 30 days and 12 months. The balance has not been discounted because the effect of the time value of money is not material. The net carrying amount of the receivables is a reasonable approximation of the fair value of the assets because of the short term nature of the assets.

The following table provides the total amount of trade and other receivables at the reporting date for the relevant financial year:

	2011	2010
	$	$
Premium receivables		
Premium receivable	**1,209,819**	1,441,399
Provision for doubtful debts	**0**	0
Net premium receivable	**1,209,819**	1,441,399
Reinsurance receivables		
Reinsurance and other recoveries on paid claims	**101,319,533**	11,378,547
Provision for doubtful debts	**0**	0
Net reinsurance recoveries on paid claims	**101,319,533**	11,378,547
Other receivables		
Other receivables	**0**	0
Total trade and other receivables	**102,529,352**	**12,819,946**

14 Net outstanding claims provision

(a) Composition of net outstanding claims provision

	2011	2010
	$	$
Gross outstanding claims		
Gross outstanding claims	**186,873,000**	54,081,754
Loss adjustment expenses	**6,245,000**	2,003,000
Claims administration expenses	**7,224,000**	2,054,000
Gross outstanding claims - undiscounted	**200,342,000**	58,138,754
Discount to present value	**(6,280,000)**	(2,982,000)
Gross outstanding claims - discounted	**194,062,000**	55,156,754
Risk margin	**21,346,830**	5,516,000
Gross outstanding claims - discounted including risk margin	**215,408,830**	60,672,754
Reinsurance and other recoveries receivable on outstanding claims		
Reinsurance and other recoveries receivable on outstanding claims	**145,631,000**	45,989,076
Loss adjustment expenses	**4,884,000**	1,731,000
Claims administration expenses	**0**	1,055,000
Reinsurance and other recoveries receivable on outstanding claims - undiscounted	**150,515,000**	48,775,076
Discount to present value	**(4,880,000)**	(2,538,000)
Reinsurance and other recoveries receivable on outstanding claims - discounted	**145,635,000**	46,237,076
Risk margin	**16,019,830**	4,624,000
Reinsurance and other recoveries receivable on outstanding claims - discounted including risk	**161,654,830**	50,861,076
Net outstanding claims		
Net outstanding claims	**41,242,000**	8,092,678
Loss adjustment expenses	**1,361,000**	272,000
Claims administration expenses	**7,224,000**	999,000
Net outstanding claims - undiscounted	**49,827,000**	9,363,678
Net discount to present value	**(1,400,000)**	(444,000)
Net outstanding claims - discounted	**48,427,000**	8,919,678
Net risk margin	**5,327,000**	892,000
Net outstanding claims - discounted including risk	**53,754,000**	9,811,678

(b) Process to determine

Overview

The effective date of the actuarial report on the insurance liabilities is 31 December 2011. The actuarial report was prepared by Martin Fry (Fellow of the New Zealand Society of Actuaries, Institute of Actuaries of Australia, and Institute of Actuaries (London)) of Taylor Fry Consulting Actuaries. Taylor Fry Consulting Actuaries are satisfied with the nature, sufficiency and accuracy of data provided for the purpose of estimating insurance liabilities.

The outstanding claims provision is determined based on three building blocks being:

- An estimate of future cash flows;
- Discounting for the effect of the time value of money; and
- Adding a risk margin for uncertainty.

The process for determining each of the above is described below.

Future cash flows

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

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

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

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

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

Discounting

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

Risk margin

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

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

(c) Assumptions made

Adopted assumptions

Item	**2011**	2010
Loss adjustment expenses rate (to net incurred claims)		
- FM Lines	**4.50%**	4.50%
- AFM	**3.00%**	3.00%
Indirect claim management expenses rate (to gross outstanding claims provision)	**4.00%**	4.00%
Inflation rate	**3.75%**	4.00%
Discount rate	**3.25%**	5.25%
Risk margin rate	**11.00%**	10.00%

Description of the assumptions

Loss adjustment expenses rate

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

Indirect claim management expenses rate

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

Inflation rate

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

Discount rate

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

Risk margin rate

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

(d) Sensitivities

Modelled sensitivities

The impact of changes in key outstanding claims variables is summarised below. Each change has been calculated in isolation of the other changes.

It is not possible to quantify the sensitivity of certain assumptions such as legislative changes or uncertainty in the estimation process.

The impact on the net outstanding claims provision is disclosed for each of the key assumption. The movements are stated in absolute terms where the base assumption is a percentage, for example, if the base inflation rate assumption was 3.5%, a 1% increase would mean assuming a 4.5% inflation rate. All movements would be recognised directly through the Statement of comprehensive income.

Item	**Effect**
Increase discount rate by 0.5%	Reduce outstanding claim liabilities by NZ$0.275 million (0.5% of outstanding claim central estimates)
Increase inflation rate by 0.5%	Increase outstanding claim liabilities by NZ$0.280 million (0.5% of outstanding claim central estimates)
Increase risk margin by 0.5%	Increase outstanding claim liabilities by NZ$0.242 million (0.5% of outstanding claim central estimates)
Change incremental incurred cost movement for FMG for most recent accident quarter to the average incurred cost of small incurred cost quarters (<$10m)	Reduce outstanding claim liabilities by NZ$2.564 million (4.7% of outstanding claim central estimates)
Change incremental incurred cost movement for most recent accident quarter to the average incurred cost of large incurred cost quarters (>$10m)(includes Christchurch)	Increase outstanding claim liabilities by NZ$14.122 million (26.3% of outstanding claim central estimates)
Reduce expected XoL recovery for OSC claims to 30% for March 2011 quarter	Increase outstanding claim liabilities by NZ$8.837 million (16.4% of outstanding claim central estimates)
Increase XoL recovery for OSC claims to 70% for March 2011 quarter	Reduce outstanding claim liabilities by NZ$2.537 million (4.7% of outstanding claim central estimates)

Description of the sensitivities

General impact of changes

- Sensitivity analysis is conducted to quantify the exposure to changes in the key underlying variables. The valuation included in the reported results is calculated using certain assumptions about these variables as disclosed above. The movement in any key variable will impact the financial position and performance for a period. The information below describes how a change in each assumption will affect claims provisions and provides and analysis of the sensitivity of the net outstanding claims provision to changes in these assumptions.
- Impact to the outstanding claims liabilities as a consequence of any adverse scenarios will be limited by application of the stop loss provisions of the intercompany reinsurance policy.

Incremental incurred cost movement

- These sensitivities show the significance of incurred cost development assumptions. These are assumptions that have a very significant influence on the results of the valuation.

XoL

- These sensitivities show the significance of reinsurance assumptions. Due to the stop loss clause in the Branch's key Quota Share reinsurance treaty with FMIC, a significant change in the mix of estimated liabilities would be required in order to reduce the level of recoveries to 30%. Such a change in mix would likely also result in a reduction in the estimated cost net of facultative recoveries only. An increase to 70% is a more likely scenario.

Inflation rate

- Expected future payments are inflated to take account of inflationary increases. An increase or decrease in the assumed levels of inflation would have a corresponding impact on claims expense. Given the short tail nature of the Branch's provisions, the impact of a change in the inflation rate would not be material.

Discount rate

- The outstanding claims provision is calculated by reference to expected future payments. These payments are discounted to adjust for the tine value of money. An increase or decrease in the assumed discount rate will have an opposing impact on total claims expense. Given the short tail nature of the Branch's provisions, the impact of a change in the inflation rate would not be material.

Risk margin

- An increase of decrease in the risk margin would have a corresponding impact on claims expense.

15 Net unearned premium reserve

(a) Reconciliation of movements

	2011	2010
	$	$
Gross unearned premium reserve		
Gross unearned premium reserve at the beginning of the financial year	**6,807,580**	6,590,134
Gross deferral of premiums on contracts written	**28,948,746**	16,325,497
Gross earning of premiums on contracts written	**(22,368,484)**	(16,108,051)
Gross unearned premium reserve at the end of the financial year	**13,387,842**	6,807,580
Deferred reinsurance expense		
Deferred reinsurance expense at the beginning of the financial year	**4,785,700**	4,612,338
Deferral of reinsurance	**20,986,171**	11,380,593
Expensing of reinsurance	**(16,066,458)**	(11,207,231)
Deferred reinsurance expense at the end of the financial year	**9,705,413**	4,785,700
Net unearned premium reserve		
Net unearned premium reserve at the beginning of the financial year	2,021,880	1,977,796
Net deferral of premiums on contracts written	7,962,575	4,944,904
Net earning of premiums on contracts written	(6,302,026)	(4,900,820)
Net unearned premium reserve at the end of the financial year	**3,682,429**	**2,021,880**

(b) Liability adequacy test

The liability adequacy test has been conducted using the central estimate of the premium liabilities, together with an appropriate margin for uncertainty. The test is based on prospective information and so is heavily dependent on assumptions and judgements. The liability adequacy test at the reporting date resulted in a deficit (2010: surplus) for the Branch.

The following table provides the net surplus / (deficiency) calculated under the liability adequacy test at the reporting date for the relevant financial year:

Notes to the financial statements for the year ended 31 December 2011

	2,011	2010
	$	$
Premium reserve		
Gross unearned premium reserve	13,387,842	6,807,580
Deferred reinsurance expense	9,705,413	4,785,700
Net unearned premium reserve	3,682,429	2,021,880
Deferred acquisition costs	**0**	0
Net unearned premium reserve less DAC	**3,682,429**	2,021,880
Premium liability		
Gross central estimate of expected future cash flows for future claims	**10,847,000**	4,923,000
Reinsurance recoveries	**7,487,000**	3,894,000
Net central estimate of expected future cash flows for future claims	3,360,000	1,029,000
Risk margin	**672,000**	187,000
Net premium liability, includng risk margin	4,032,000	1,216,000
Net surplus (deficiency)	**(349,571)**	**805,880**
Assumptions		
Risk margin %	**20.0%**	18.2%
Probability of adequacy %	**75.0%**	75.0%
Policy administration % (to gross unearned premium reserve)	**5.0%**	8.5%

16 Trade and other payables

The payables are unsecured, non-interest bearing and are normally settled between 7 days and 90 days. The balance has not been discounted because the effect of the time value of money is not material. The net carrying amount of the payables is a reasonable approximation of the fair value of the liabilities because of the short term nature of the liabilities.

The following table provides the total amount of trade and other payables at the reporting date for the relevant financial year:

	2011	2010
	$	$
Trade and other payables		
Reinsurance creditors	**8,134,577**	2,153,777
Auditor fee payable	**22,347**	20,000
Total trade and other payables	**8,156,924**	**2,173,777**

17 Related parties

The Branch is a part of FM Insurance Company Limited (the "Company").

The Company is a wholly owned subsidiary of Factory Mutual Insurance Company (FMIC), (the "Parent").

The following table provides the total amount of transactions that were entered into with related parties for the relevant financial year:

	2011	2010
	$	$
FM Insurance Company (Australia) Ltd		
General and administration expenses	**4,357,271**	2,614,637
Factory Mutual Insurance Company		
Reinsurance expense	**8,341,159**	5,707,447
Reinsurance recoveries	**269,465,497**	6,247,988

Unless otherwise stated, related parties are members of the FMIC Group.

Terms and conditions of transactions with related parties:

- Reinsurance transactions to/from related parties are made in arm's length transactions both at normal market prices and on normal commercial terms.
- Outstanding balances at year-end are unsecured, interest free and settlement occurs in cash.

18 Equity retained for purposes of financial soundness

The Australian branch retains a level of equity and retained reserves which enable it to maintain an adequate solvency margin for ongoing ability to pay clients. These statements relate to a branch of an overseas company. Its assets are available to support the liabilities of the company outside of New Zealand. The New Zealand operations of FM Insurance Company Ltd are included within the Australian Branch.

19 Contingent liabilities

There were no known contingent liabilities as at the reporting date requiring disclosure in these financial statements.

Contingent liabilities are not recognised on the Statement of financial position but are required to be disclosed in the notes to the financial statements where the possibility of settlement is less than probable but more than remote. Provisions are not required with respect to such matters as it is not probable that a future sacrifice of economic benefits will be required or the amount cannot be reliably measured.

20 Commitments

(a) Capital commitments

The Branch has no capital expenditure contracted for at the reporting date but not recognised in the financial statements.

(b) Software license and/or rental commitments

The Branch has no current software license and/or rental commitments.

(c) Operating lease commitments

The Branch has no current non-cancellable operating lease commitments.

(d) Finance lease commitments

The Branch has no current finance lease commitments.

21 Subsequent events

No transactions or events occurred after the reporting date which significantly affected, or may significantly affect, the results of the Branch, the operations of the Branch, or the state of affairs of the Branch.