

**Genworth Financial  
Mortgage Insurance Pty  
Limited**

**ABN 60 106 974 305**

Annual Financial Report  
31 December 2013

# Directors' report

The directors present their report together with the financial report of Genworth Financial Mortgage Insurance Pty Limited ("the Company") for the year ended 31 December 2013 and the auditor's report thereon.

## Directors

The directors of the Company at any time during or since the end of the financial year are as follows:

Ellie Comerford  
Anthony Gill  
Richard Grellman  
Ian MacDonald  
Samuel Marsico  
Leon Roday  
Stuart Take  
Gayle Tollifson  
Jerome Upton

## Principal activities

The principal activity of the Company during the financial year was the provision of lenders mortgage insurance ("LMI").

## Review and result of operations

The Company's profit after income tax amounted to \$177,672,000 (2012: \$171,970,000).

Gross written premiums for 2013 of \$596,492,000 (2012: \$544,899,000) were 9.47% higher than 2012, mainly attributable to increased mortgage lending by customers owing to improved housing affordability as interest rates remained low in 2013.

Net earned premium increased to \$397,897,000 from \$363,333,000 in 2012 and the increase was as a result of higher written premiums, the seasoning of the in-force block of business and lower reinsurance premiums.

The loss ratio (net claims incurred/net earned premium) decreased from 71.45% to 32.07%, primarily driven by a reserving strengthening in 2012 that did not recur in 2013. The reserve strengthening in 2012 was as a result of higher than anticipated frequency and severity of claims paid arising from later stage delinquencies from prior years, particularly in sub-segments of the Queensland region as a result of regional economic pressures as well as our 2007 and 2008 vintages which have a higher concentration of self-employed borrowers. The decrease of 50.71% in net incurred claims was driven by lower new delinquencies and improved aging on our existing delinquencies in 2013. Paid claims also decreased in the year as a result of a decrease in both the number of claims and the average claim payment.

Underwriting and other operating expenses of \$110,035,000 (2012: \$100,530,000) increased by 9.45%, primarily from higher employee compensation and benefit expenses and higher operating expenses in 2013.

Financial income of \$103,269,000 (2012: \$257,295,000) decreased substantially from a combination of lower investment yields and unrealised losses on the portfolio of interest bearing securities of \$59,172,000 compared to unrealised gains of \$64,078,000 in 2012.

## Corporate structure

Genworth Financial Mortgage Insurance Pty Limited is incorporated and domiciled in Australia. The ultimate parent entity is Genworth Financial Inc, a company incorporated in the United States of America.

Genworth Financial Mortgage Insurance Pty Limited's registered office and principal place of business is Level 26, 101 Miller Street, North Sydney, NSW 2060

## **Dividends**

The Group paid an ordinary dividend of \$0.0928 per ordinary share, amounting to \$130,000,000, to its shareholder, Genworth Financial Services Pty Limited on 14 June 2013. In 2012, the Company paid an ordinary dividend of \$0.0228 per ordinary share, amounting to \$32,000,000 to its shareholder on 21 December 2012.

## **State of affairs**

There were no significant changes in the state of affairs of the Company that occurred during the year.

## **Environmental regulations**

The Company's operations are not subject to any significant environmental regulations under either Commonwealth or State legislation.

## **Events subsequent to reporting date**

There has not been any matter or circumstance that has arisen since the end of the financial year to the date of this report that, in the opinion of the directors of the Company, would significantly affect the operations of the Company, the results of those operations or the state of affairs of the Company in future financial years.

## **Likely developments**

The Company's ultimate parent entity previously announced a plan to pursue a sale of up to 40% of its Australian business subject to market conditions, valuation considerations including business performance, and regulatory approvals. Executing the planned sale, including through an initial public offering ("IPO"), remains a key priority in reducing the parent entity's exposure to mortgage insurance risk, rebalancing the capital among its three main mortgage insurance platforms and generating capital. In Australia, there is concentration among a small group of banks that write most of the mortgages. These banks continue to evaluate the utilisation of mortgage insurance in connection with the implementation of the bank capital standards in Australia introduced by the Basel Committee, and this could impact both the size of the mortgage insurance market in Australia and our market share. The response of banks to the new capital standards will develop over time and this response could impact the Company's business. As execution of an IPO is subject to market conditions, valuation considerations, including business performance, and regulatory considerations, the Company believes it is likely that there will be better execution opportunities in 2014.

Further information about likely developments in the operations of the Company and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the Company.

## **Indemnification and insurance of officers and auditors**

During the financial year, the Company paid premiums to insure directors and certain officers of the Company for the year ended 31 December 2013 and, since the end of the financial year, the Company has paid or agreed to pay premiums in respect of such insurance contracts for the year ending 31 December 2014. Such insurance contracts insure against liability (subject to certain exclusions) persons who are or have been directors or officers of the Company.

The directors have not included details of the nature of the liabilities covered or the amount of the premium paid as such disclosure is prohibited under the terms of the contracts.

The Company has not indemnified or made a relevant agreement for indemnifying against a liability any person who is or has been an auditor of the Company.

## **Directors' interests and benefits**

Other than the aggregate remuneration paid or receivable by directors included in the financial report, and remuneration as an executive paid or payable by the related body corporate, no director has received or become entitled to receive any benefit because of a contract made by the Company or a related body corporate with a director or with a firm of which a director is a member, or with an entity in which the director has a substantial interest.

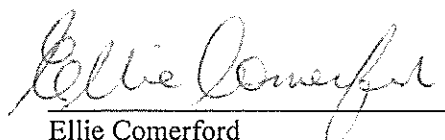
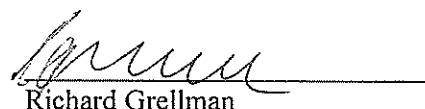
## **Rounding off**

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the financial report and directors' report have been rounded off to the nearest thousand dollars, unless otherwise stated.

## **Lead auditor's independence declaration**

The lead auditor's independence declaration is set out on page 4 and forms part of the directors' report.

Signed in accordance with a resolution of the directors:

  
Ellie Comerford  
Director  
Richard Grellman  
Director

Dated at Sydney, 12 February 2014.



*Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001*

To: the directors of Genworth Financial Mortgage Insurance Pty Limited

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 31 December 2013 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit.

*KMG*

KPMG

A handwritten signature in black ink, appearing to read 'Ian Moyser'.

Ian Moyser  
*Partner*

Sydney

12 February 2014

# Statement of comprehensive income

For the year ended 31 December 2013

	Note	2013 \$'000	2012 \$'000
Gross written premium	5	596,492	544,899
Movement in unearned premium		(125,030)	(101,047)
Outward reinsurance premium expense		<u>(73,565)</u>	<u>(80,519)</u>
Net earned premium		397,897	363,333
Net claims incurred	9	(127,617)	(259,556)
Acquisition costs		(47,172)	(44,503)
Other underwriting expenses	7	<u>(62,863)</u>	<u>(56,027)</u>
Profit from underwriting		160,245	3,247
Financial income	6	103,269	257,295
Financing costs		<u>(11,456)</u>	<u>(12,871)</u>
<b>Profit before income tax</b>		252,058	247,671
Income tax expense	10(a)	<u>(74,386)</u>	<u>(75,701)</u>
<b>Profit for the year</b>		<u>177,672</u>	<u>171,970</u>
<b>Total comprehensive income for the year</b>		<u>177,672</u>	<u>171,970</u>
<b>Profit attributable to the members</b>		<u>177,672</u>	<u>171,970</u>
<b>Total comprehensive income attributable to members</b>		<u>177,672</u>	<u>171,970</u>

The statement of comprehensive income is to be read in conjunction with the notes to the financial statements.

# Statement of financial position

As at 31 December 2013

	Note	2013 \$'000	2012 \$'000
<b>Assets</b>			
Cash	11	84,794	23,071
Accrued investment income		40,023	41,524
Investments	14	3,554,061	3,523,751
Trade and other receivables	12	6,321	4,621
Prepayments		1,322	2,647
Deferred reinsurance expense	13	93,373	79,120
Non-reinsurance recoveries		19,631	24,749
Deferred acquisition costs	15	128,386	137,505
Plant and equipment	16	1,585	2,109
Deferred tax asset	18	7,609	2,430
Investment in controlled entity		27,598	27,598
Intangibles	17	7,311	11,559
Goodwill		7,490	7,490
<b>Total assets</b>		<u>3,979,504</u>	<u>3,888,174</u>
<b>Liabilities</b>			
Trade and other payables	21	60,689	94,854
Reinsurance payable		109,111	95,639
Outstanding claims	19	240,146	301,413
Unearned premiums	20	1,249,083	1,124,052
Employee benefits provision	22	6,076	5,735
Interest bearing liabilities	23	137,741	136,989
<b>Total liabilities</b>		<u>1,802,846</u>	<u>1,758,682</u>
<b>Net assets</b>		<u>2,176,658</u>	<u>2,129,492</u>
<b>Equity</b>			
Share capital	24	1,401,559	1,401,559
Share based payment reserve	24(a)	1,954	2,460
Other reserves	25	(603,268)	(603,268)
Retained earnings		1,376,413	1,328,741
<b>Total equity</b>		<u>2,176,658</u>	<u>2,129,492</u>

The statement of financial position is to be read in conjunction with the notes to the financial statements.

# Statement of changes in equity

For the year ended 31 December 2013

	Share capital	Other reserves	Share based payment reserve	Retained earnings	Total
	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Balance at 31 December 2011</b>	1,401,559	(603,268)	1,975	1,188,771	1,989,037
Dividends declared and paid	-	-	-	(32,000)	(32,000)
Expense for year	-	-	802	-	802
Share based payment recharged by parent company	-	-	(317)	-	(317)
Profit after taxation	-	-	-	171,970	171,970
<b>Balance at 31 December 2012</b>	1,401,559	(603,268)	2,460	1,328,741	2,129,492
Dividends declared and paid	-	-	-	(130,000)	(130,000)
Expense for year	-	-	172	-	172
Share based payment recharged by parent company	-	-	(678)	-	(678)
Profit after taxation	-	-	-	177,672	177,672
<b>Balance at 31 December 2013</b>	1,401,559	(603,268)	1,954	1,376,413	2,176,658

The statement of changes in equity is to be read in conjunction with the notes to the financial statements.



# Statement of cash flows

For the year ended 31 December 2013

	Note	2013 \$'000	2012 \$'000
<b>Cash flows from operating activities</b>			
Premiums received		596,492	545,383
Interest and other income		182,218	189,156
Financial expense on long term borrowings		(11,456)	(12,871)
Claims paid		(188,884)	(293,063)
Cash payments in the course of operations		(181,148)	(165,018)
Income tax paid		(96,851)	(95,741)
<b>Net cash provided by operating activities</b>	30(b)	<u>300,371</u>	<u>167,846</u>
<b>Cash flows from investing activities</b>			
Payments for plant and equipment and intangibles		(890)	(210)
Payments for investments		(355,831)	(1,122,417)
Proceeds from sale of investments		399,888	634,369
<b>Net cash provided by/ (used in) investing activities</b>		<u>43,167</u>	<u>(488,258)</u>
<b>Cash flows from financing activities</b>			
Payment of dividends		(130,000)	(32,000)
<b>Net cash used in financing activities</b>		<u>(130,000)</u>	<u>(32,000)</u>
<b>Net increase/ (decrease) in cash held</b>		213,538	(352,412)
<b>Cash and cash equivalents at the beginning of the financial year</b>		<u>353,670</u>	<u>706,082</u>
<b>Cash and cash equivalents at the end of the financial year</b>	30(a)	<u>567,208</u>	<u>353,670</u>

The statement of cash flows is to be read in conjunction with the notes to the financial statements.

# Notes to the financial statements

## 1 Statement of significant accounting policies

Genworth Financial Mortgage Insurance Pty Limited (the “Company”) is a company domiciled in Australia. The Company is a for-profit entity.

The financial statements were authorised for issue by the Board of Directors on 12 February 2014.

### (a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards adopted by the Australian Accounting Standards Board (“AASB”) and the Corporations Act 2001. International Financial Reporting Standards (“IFRSs”) form the basis of Australian Accounting Standards adopted by the AASB, being Australian equivalents to IFRS (“AIFRS”). The financial reports of the Company also comply with IFRSs and interpretations adopted by the International Accounting Standards Board.

### (b) Basis of preparation

The financial report is presented in Australian dollars.

The statement of financial position has been prepared using the liquidity format of presentation, in which the assets and liabilities are presented broadly in order of liquidity. The assets and liabilities comprise both current amounts (expected to be recovered or settled within 12 months after the reporting date) and non-current amounts (expected to be recovered or settled more than 12 months after the reporting date). For those assets and liabilities that comprise both current and non-current amounts, information regarding the respective current and non-current amounts is disclosed in the relevant note to the financial statements.

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2014, and have not been applied in preparing these financial statements. An initial assessment of these standards and amendments has taken place and the application of these standards is not expected to have material impact on the Company’s accounting policies. AASB 9 Financial Instruments, which becomes mandatory for the Company’s 2015 financial statements could change the classification and measurement of financial assets. The Company does not plan to adopt this standard early and the extent of the impact has not been determined.

The financial report is prepared on the historical cost basis except for investments being stated at fair value and outstanding claims and the related reinsurance recoveries on unpaid claims being stated at present value.

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the financial report and directors’ report have been rounded off to the nearest thousand dollars, unless otherwise stated.

The Company does not prepare consolidated accounts for the consolidated entity comprising it and its controlled entity as the directors do not consider the consolidated entity to be a disclosing entity.

Consolidated accounts are prepared by the Company’s highest parent entity of the Australian Group, Genworth Financial Mortgage Insurance Finance Pty Limited.

The preparation of a financial report requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical

experience and various other factors that are believed to be reasonable in the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

These estimates and underlying assumptions are reviewed on an ongoing basis and actual results may vary from estimates. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of Australian Accounting Standards that have a significant effect on the financial report and estimates with a significant risk of material adjustment in the next year are discussed in Note 2.

The accounting policies have been applied consistently by the Company.

**(c) Classification of insurance contracts**

Contracts under which an entity accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary are classified as insurance contracts. Insurance risk is risk other than financial risk.

**(d) Revenue recognition**

*Earned and unearned premium revenue*

Premiums comprise amounts charged to the policyholder, excluding stamp duties and goods and services tax ("GST") collected on behalf of third parties. Premiums have been brought to account as income from the date of attachment of risk over periods up to eleven years based on an actuarial assessment of the pattern and period of risk. The earned portion of premium received is recognised as revenue. The balance of premium received is carried as an unearned premium reserve.

*Interest revenue*

Interest revenue is recognised as it accrues, taking into account the coupon rate on investments and interest rates on cash and cash equivalents, net of withholding tax paid or payable.

**(e) Goods and services tax**

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Taxation Office ("ATO"). In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the statement of financial position. Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

**(f) Reinsurance**

*Reinsurance expense*

Premium ceded to reinsurers is recognised as an expense in accordance with the pattern of reinsurance coverage received. Accordingly, a portion of outwards reinsurance premium is treated at the balance date as a deferred reinsurance expense.

### ***Reinsurance and other recoveries receivable***

Reinsurance and other recoveries receivable on paid claims, reported claims not yet paid and incurred but not reported claims ("IBNR") are recognised as revenue. Recoveries receivable on paid claims are presented as part of trade and other receivables net of any provision for impairment based on objective evidence for individual receivables. Recoveries receivable are assessed in a manner similar to the assessment of outstanding claims. Reinsurance does not relieve the Company of its liabilities to policyholders and reinsurance recoveries are, if applicable, presented as a separate asset on the statement of financial position.

#### **(g) Claims**

Claims expense and a liability for outstanding claims are recognised in respect of direct and inward reinsurance business. The liability covers claims reported and outstanding, IBNR and the expected direct and indirect costs of settling those claims. Outstanding claims are assessed by estimating the ultimate cost of settling delinquencies, which includes IBNR and settlement costs, using statistics based on past experience and trends. Changes in outstanding claims are recognised in profit or loss in the reporting period in which the estimates are changed.

The provision for outstanding claims contains a risk margin to reflect the inherent uncertainty in the central estimate (refer to Note 3 for further detail).

#### **(h) Taxation**

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the statement 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 expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the statement of financial position date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the statement of financial position method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit; nor differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the statement of financial position date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

The Company is a member of Genworth Financial New Holdings Pty Limited tax consolidation group. Under the tax consolidation system the head entity is liable for the current income tax liabilities of that group. Entities are jointly and severally liable for the current income tax liabilities of the tax consolidated group where the head entity defaults, subject to the terms of the valid tax sharing agreement between the entities in the group. Assets and liabilities arising in the Company under the tax funding arrangement are recognised as amounts receivable from or payable to other entities in the tax consolidated group.

**(i) Cash and cash equivalents**

Cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term and highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

**(j) Acquisition costs**

Costs associated with obtaining and recording mortgage insurance contracts are referred to as acquisition costs and are capitalised when they relate to the acquisition of new business or the renewal of existing business. These are presented as deferred acquisition costs ("DAC") and amortised under the same basis as the earning pattern of premium over the period of the related insurance contracts. The balance at the reporting date represents the capitalised acquisition costs relating to unearned premium and is stated at cost subject to the liability adequacy test (refer Note 1(k)).

The Company reviews all assumptions underlying DAC and tests DAC for recoverability annually. If the balance of unearned premiums is less than the current estimate of future losses and related expenses a charge to income is recorded for additional DAC amortisation.

**(k) Liability adequacy test**

The liability adequacy test is an assessment of the carrying amount of the unearned premium liability and is conducted at each reporting date. If current estimates of the present value of the expected cash flows relating to future claims plus an additional risk margin, to reflect the inherent uncertainty in the central estimate, exceed the unearned premium liability less related deferred reinsurance and deferred acquisition costs, then the unearned premium liability is deemed to be deficient. The test is performed at the level of portfolio of contracts that are subject to broadly similar risks and that are managed together as a single portfolio. Any deficiency is recognised in the statement of comprehensive income, with a corresponding impact in the statement of financial position, recognised first through the write down of related deferred acquisition costs, and any remaining balance being recognised as an unexpired risk liability (refer to Note 34).

**(l) Investment assets**

***Financial assets backing general insurance liabilities***

The assets backing general insurance liabilities are those assets required to cover the technical insurance liabilities (outstanding claims and unearned premiums) plus an allowance for capital adequacy.

The Company has designated the assets backing general insurance activities based on their function. Initially insurance technical balances are offset against the required assets with any additional assets required being allocated based on liquidity.

In accordance with the Company's investment strategy, the Company actively monitors the average duration of the notional assets allocated to insurance activities to ensure sufficient funds are available for claim payment obligations.

The Company values financial assets and any assets backing insurance activities at fair value through profit and loss, with any resultant unrealised profits and losses recognised in the statement of comprehensive income.

The valuation methodologies of assets valued at fair value are summarised below:

- Cash assets and bank overdrafts are carried at face value of the amounts deposited or drawn;

- Fixed interest securities are initially recognised at fair value, determined as the quote cost at date of acquisition. They are subsequently remeasured to fair value at each reporting date. For securities traded in an active market, fair value is determined by reference to published bid price quotations. For securities not traded, and securities traded in a market that is not active, fair value is determined using valuation techniques with the most common technique being reference to observable market data by reference to the fair values of recent arm's length transactions involving the same or similar instruments. In absence of observable market information, unobservable inputs which reflect management's view of market assumption are used. Valuation techniques are utilised that maximise the use of observable inputs and minimise the use of unobservable inputs.

#### ***Financial assets not backing general insurance liabilities***

Investments that do not back general insurance liabilities include the investment in the controlled entity which is stated at cost less impairment losses. The balance of investments not backing insurance liabilities are designated as financial assets on the same basis as those backing insurance liabilities.

#### **(m) Payables**

Liabilities are recognised for amounts to be paid in the future for goods or services received. Trade accounts payable are normally settled within 30-60 days. The carrying amount of accounts payable approximates fair value.

#### **(n) Depreciation and amortisation**

Depreciation is recognised in profit or loss on a straight line basis over the estimated useful lives of each item of plant and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives, unless it is reasonably certain the Company will obtain ownership by the end of the lease term. Assets are depreciated or amortised from the date of acquisition.

Depreciation and amortisation methods, useful lives and residual values are reviewed at each reporting date. Where changes are made, adjustments are reflected in current and future periods only.

The estimated useful lives for the current and comparative periods are as follows:

	2013	2012
Leasehold improvements	5-10 years	5-10 years
Furniture & equipment	5-8 years	5-8 years
Computing hardware	3-5 years	3-5 years
Intangibles	5 years	5 years

#### **(o) Intangible assets**

##### ***Acquired intangible assets***

Acquired intangible assets are initially recorded at their cost at the date of acquisition, being the fair value of the consideration provided and, for assets acquired separately, incidental costs directly attributable to the acquisition. All intangible assets acquired have a finite useful life and are amortised on a straight line basis over the estimated useful life of the assets being the period in which the related benefits are expected to be realised (shorter of legal benefit and expected economic life).

##### ***Software development expenditure***

Software development expenditure that meets the criteria for recognition as an intangible asset is capitalised in the statement of financial position and amortised over its expected useful life, subject to impairment testing.

Costs incurred in researching and evaluating a project up to the point of formal commitment to a project are expensed as incurred. Only software development projects with total budgeted expenditure of more than \$250,000 are considered for capitalisation. Smaller projects and other costs are treated as maintenance costs, being an ongoing part of maintaining effective technology, and are expensed as incurred.

All capitalised costs are deemed to have an expected useful life of 5 years unless it can be clearly demonstrated for a specific project that the majority of the net benefits are to be generated over a longer or shorter period. The capitalised costs are amortised on a straight line basis over the period following completion of a project or implementation of part of a project.

The recoverability of the carrying amount of the asset is reviewed each reporting date by determining whether there is any indication that the carrying value may be impaired. If such indication exists, the item is tested for impairment by comparing the recoverable amount, or value in use, of the asset to the carrying value. An impairment charge is recognised in the income statement when the carrying value exceeds the calculated recoverable amount. The impairment charges can be reversed if there has been a change in the estimate used to determine the recoverable amount.

**(p) Goodwill**

All business combinations are accounted for by applying the purchase method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill is stated at deemed cost less any accumulated impairment losses.

**(q) Employee entitlements**

The carrying amount of provisions for employee entitlements approximates present value.

*Wages, salaries and annual leave*

The accruals for employee entitlements to wages, salaries and annual leave represent present obligations resulting from employees' services provided up to the statement of financial position date, calculated at undiscounted amounts based on wage and salary rates that the entity expects to pay as at reporting date, including related on-costs.

*Long service leave*

The Company's net obligation in respect of long-term benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods. A liability for long service leave is recognised as the present value of estimated future cash outflows to be made in respect of services provided by employees up to the reporting date. The estimated future cash outflows are discounted using interest rates on national government guaranteed securities which have terms to maturity that match, as closely as possible, the estimated future cash outflows. Factors which affect the estimated future cash outflows such as expected future salary increases including related on-costs and expected settlement dates are incorporated in the measurement.

*Superannuation commitments*

The superannuation plan is a defined contribution plan. All employees are entitled to varying levels of benefits on retirement based on accumulated employer contributions and investment earnings thereon as well as benefits in the event of disability or death. Contributions by the Company are, as a minimum, in accordance with the Superannuation Guarantee Levy.

**(r) Impairment of assets**

The carrying amounts of the Company's assets, other than deferred tax assets (see Note 1(h)) and DAC (see Note 1(j)), are reviewed at each statement of financial position date to determine

whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

For goodwill and assets that have an indefinite useful life, the recoverable amount is estimated at each statement of financial position date.

An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount. Impairment losses are recognised in the statement of comprehensive income, unless an asset has previously been revalued, in which case the impairment loss is recognised as a reversal to the extent of that previous revaluation with any excess recognised as a loss in the statement of comprehensive income.

**(s) Leases**

All leases entered into are operating leases, where the lessor retains substantially all the risks and benefits of ownership of the leased items. Lease payments are recognised as an expense on a straight line basis over the term for these leases.

**(t) Receivables**

The collectability of receivables is assessed at balance date and an impairment loss is made for any doubtful accounts.

The carrying amount of receivables approximates net fair value.

**(u) Share-based payment transactions**

Genworth Financial Inc, the ultimate parent entity, provides benefits to directors and employees of the Group in the form of share-based payments including share options and restricted share units ("RSUs"), whereby directors and employees render services to the Group in exchange for shares or rights over shares in Genworth Financial Inc ("equity-settled transactions").

The cost of equity-settled transactions under the Genworth Financial Inc Omnibus Incentive Plan is measured by reference to the fair value at the date which they are granted. The fair value is calculated using the Black-Scholes option pricing model. No account is taken of any performance conditions, other than conditions linked to the price of the shares of Genworth Financial Inc ("market conditions").

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("vesting date").

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) an estimated number of awards that will ultimately vest. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition.

In the case where an equity-settled award vests and subsequently is cancelled, it is treated as if it had not vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately.



(v) **Interest bearing liabilities and finance costs**

Interest bearing liabilities are initially recognised at fair value less transaction costs that are directly attributable to the transaction. After initial recognition the liabilities are carried at amortised cost using the effective interest rate method.

Finance costs include interest, which is accrued at the contracted rate and included in payables; amortisation of transaction costs which are capitalised, presented together with borrowings, and amortised over the life of the borrowings; and amortisation of discounts or premiums (the difference between the original proceeds, net of transaction costs, and the settlement or redemption value of borrowings) over the term of the liabilities.

## **2 Accounting estimates and judgements**

### **Critical accounting estimates and judgements**

The Company makes judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. 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 areas where critical accounting estimates and judgements are applied are noted below.

#### ***Estimation of premium revenue and unearned premiums (Note 5 and 20)***

Premium is earned over periods of up to eleven years. The principle underlying the earning recognition is to derive a premium earning scale which recognises the premium in accordance with the incidence of claims risk.

The review of the premium earning scale is based on an analysis of the historical pattern of claims incurred and the pattern of policy cancellations. The estimate for unearned premiums is established on the basis of this earning scale.

Assumptions recommended by the Appointed Actuary recognise that the unearned premium relating to cancelled policies is brought to account immediately.

#### ***Estimation of outstanding claims liabilities (Note 19)***

Provision is made for the estimated claim cost of reported delinquencies at the statement of financial position date, including the cost of delinquencies incurred but not yet reported to the Company.

The estimated cost of claims includes direct expenses to be incurred in settling claims gross of expected third party recoveries. The Company takes all reasonable steps to ensure that it has appropriate information regarding its claims exposure. However, given the uncertainty in establishing claims provisions, the final outcome may prove to be different from the original liability established.

The estimation of IBNR is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Company, where more information about the claim event is generally available. IBNR claims may often not be apparent to the insured or notified to the Company until some time after the events giving rise to the claims have happened.

In calculating the estimated cost of unpaid claims, the Company uses a variety of estimation techniques, generally based upon statistical analysis of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortion in the underlying statistics or which

might cause the cost of unsettled claims to increase or decrease when compared with the cost of previously settled claims.

Provisions are calculated gross of any recoveries. A separate estimate is made of the amounts that will be recoverable from lenders under specified arrangements. Estimates are also made for amounts recoverable from borrowers and property valuers, based upon the gross provisions.

Details of specific assumptions used in deriving the outstanding claims liabilities at the statement of financial position date are detailed in Note 3.

### **3 Actuarial assumptions and methods**

The Company internally valued the outstanding claims liabilities at the statement of financial position date. The valuation approach is consistent with that recommended by the Appointed Actuary.

The valuation methods used are based on the underlying attributes of the claims portfolio. The Company establishes provisions for outstanding claims in two parts:

- delinquent loans advised to the Company; and
- IBNR.

The provision in respect of delinquent loans not in possession by the mortgagee is determined according to the following formula:

- outstanding loan amount multiplied by frequency factor multiplied by severity factor.

In applying this formula:

- the outstanding loan amount insured is the total outstanding amount on those loans advised to the Company by the lenders as being delinquent;
- the frequency and severity factors are based on a review of historical claims and delinquency experience performed by the Appointed Actuary and adopted by the Company.

For loans where the mortgagee is in possession ("MIPs") but a claim has not yet been submitted the approach taken is a case estimate based approach using the current outstanding loan balance (including accumulated arrears) adjusted for selling costs, the most recent property valuation, or an estimate there of, and any amounts not eligible to be claimed.

For MIPs where the claim has been submitted the approach adopted is to provision for the claimed amount, adjusted for amounts not eligible to be claimed.

#### **Actuarial assumptions and process**

Historical information relating to arrears and claims history for the Company was provided to the Appointed Actuary in order to determine the underlying assumptions.

The Appointed Actuary examined the experience of the 1992-2013 underwriting years, including the mix of business by loan value ratio ("LVR") and loan size band, the region in which the mortgaged property is located, product types, loan purpose and arrears duration.

Statistical modelling was used to identify significant explanatory factors affecting outcomes for frequency and severity based on historical claims experience.

The Appointed Actuary identifies significant explanatory factors affecting outcomes and incorporates this information into models for frequency and severity. The models incorporate past and anticipated movements in key variables to determine appropriate assumptions for reserving. The actuarial assumptions used in determining the outstanding claims liabilities, other than MIPs, are:

### ***Frequency***

While the propensity for a delinquent loan to become a claim varies for many explanatory factors (as determined by the Appointed Actuary's analyses), the frequency basis is summarised on any given balance date and expressed so that it varies only by LVR band and number of payments in arrears (taking into account the average mix of effects of the other explanatory factors on the balance date). Additional loadings are placed on these factors according to geographic location, number of payments in arrears, loan balance, external dispute resolution (those borrowers accessing ombudsman services or seeking legal representation), and the lender, to adjust for shorter term expectations of frequency.

### ***Severity***

Claim severity, where severity is expressed as a percentage of the outstanding loan amount at the latest arrears date, varies according to the number of payments in arrears and the geographic region of the properties secured by the mortgages and the lender.

The following average frequency and severity factors have been used in the measurement of outstanding claims:

Average frequency factor is 37% (2012: 42%)

Average severity factor is 25% (2012: 25%)

### ***IBNR***

The IBNR provision is estimated by analysing the historical pattern of reported delinquencies.

### ***Risk Margin***

The risk margin is an additional allowance for uncertainty in the ultimate cost of claims over and above the central estimate determined on the bases set out above. The overall margin adopted by the Company is determined after considering the uncertainty in the portfolio, industry trends, the Company's risk appetite and the margin corresponding with that appetite.

To determine the risk margin, the Appointed Actuary reviews the factors impacting the portfolio to establish a recommended margin at the level required by the Company and the Australian Prudential Regulation Authority ("APRA"). Factors considered include:

- Variability of claims experience of the portfolio;
- Quality of historical data;
- Uncertainty due to future economic conditions;
- Diversification within the portfolio, and;
- Increased uncertainty due to future legislative changes.

The risk margin is applied to the net central estimate.

A risk margin for outstanding claims of 15% (2012: 15%) of net central estimate has been assumed and is intended to achieve a 75% probability of sufficiency ("PoS"). The risk margins for outstanding claims and premium liabilities are separately determined. A risk margin of 37% (2012: 30%) of net central estimate has been assumed for the premium liabilities (unearned premium) at the 75% PoS level.

No discounting has been applied to non-current claims on the basis that the effect is immaterial.

The weighted average term to settlement is approximately 21 months (2012: 21 months).

### Sensitivity Analysis

The valuation of outstanding claims incorporates a range of factors that involves interactions with economic indicators, statistical modelling and observed historical claims development and experience. Certain variables can be expected to impact outstanding claims liabilities more than others, and consequently a greater degree of sensitivity to these variables can be expected.

Future economic conditions and in particular house prices and interest rates (and unemployment for new delinquencies) impacts frequency and, to a lower extent, severity.

The actuarial result is based on the central estimate of the net outstanding claim liabilities. The impact on the profit and loss before income tax to changes in key actuarial assumptions is detailed in the table below.

The upper and lower bounds of a 95% confidence interval of frequency and severity outcomes are applied as sensitivity factors. The impact of applying the sensitivities is asymmetric around the central estimate due to the assumed asymmetry of the distribution of outcomes of the net outstanding claim liabilities.

### Impact on outstanding claims liabilities to changes in key variables

	Change in variable 2013	Impact on outstanding claims liabilities 2013 \$'000	Change in variable 2012	Impact on outstanding claims liabilities 2012 \$'000
Frequency factor – upper 97.5 <sup>th</sup>	19%	72,093	17%	70,994
Frequency factor – lower 2.5 <sup>th</sup>	(14%)	(53,291)	(13%)	(60,905)
Severity factor – upper 97.5 <sup>th</sup>	7%	45,744	3%	32,112
Severity factor – lower 2.5 <sup>th</sup>	(6%)	(37,702)	(3%)	(28,842)

### Claims handling expenses

Claims handling expenses are estimated after considering historical actual expenses and the projected costs of handling claims over the weighted average term to settlement.

## 4 Insurance contracts – Insurance risk management

### Risk management objectives and policies for mitigating insurance risk

The Company has established policies, processes and procedures for managing insurance risk. The risk under any one insurance contract arises out of the uncertainty surrounding the probability of timing and severity of claims under the contract.

The Company manages its insurance risk through underwriting limits, approval procedures for transactions that involve new products or that exceed set limits, pricing guidelines, centralised management of reinsurance and monitoring of emerging issues and trends.

The Company uses several methods to assess and monitor insurance risk exposures both for individual types of risks insured and overall risks. These methods include provision of quantitative and qualitative analysis on economic and portfolio trends and key economic indicators through use of appropriate management reports, technologies and risk tools.

#### **Objectives in managing risk arising from insurance and policies for mitigating those risks**

The Company manages insurance risk to reduce the volatility of operating profits. In addition to the inherent uncertainty of insurance risk, which can lead to significant variability in loss experience, profits from insurance business are affected by market factors, particularly competition and movements in asset values. Short-term variability is, to some extent, a feature of insurance business.

In accordance with Prudential Standards issued by the prudential regulator, APRA, the Company has developed, implemented and maintains a Risk Management Framework ("RMF") and a Risk Management Strategy ("RMS"), including a Reinsurance Management Strategy ("ReMS"). The RMS incorporates the Company's Risk Appetite Statement.

The RMF and RMS formalise and communicate the Company's approach to the management of risk, with an emphasis on encouraging openness and the early reporting of material risks. It establishes:

- the strategy for operating within the Company's risk appetite;
- clear roles and responsibilities for the management of risk for the Board, management and staff;
- the mechanisms by which the business determines its risk profile, considers and accepts new risks, and audits and monitors those risks; and
- reporting requirements for risk assessments and actions and their escalation to appropriate levels within the Company and within the Genworth Group.

The RMF, RMS and ReMS outline the Company's policies, procedures, processes and controls that comprise its risk management and control systems. These systems address financial and non-financial risk; enterprise, balance sheet, market, credit, insurance, reinsurance, and operational risk that have the potential to impact the Company. Annually, the Board certifies to APRA that strategies have been put in place to monitor those risks, that the Company has systems in place to ensure compliance with legislative and prudential requirements and that the Board has satisfied itself as to the compliance with these.

Effective 1 January 2013 the Company has implemented an Internal Capital Adequacy Assessment Process ("ICAAP"). This is a Board approved process whereby the Company assesses its capital needs and manages its capital levels accordingly.

#### **Underwriting strategy**

The Company's underwriting strategy is to manage and mitigate insurance risk to an acceptable level. Acceptable insurance risks to the Company constitute loans secured against residential real estate security located in Australia and, until new business was stopped in September 2011, New Zealand. This can comprise loans for vacant land, existing homes, new home construction, and investment (rental) housing, as well as home improvements, renovations, personal investment purposes and personal consumer purposes. The acceptability of insurance proposals submitted to the Company is determined by their compliance with the Company's underwriting guidelines.

The Company's Underwriting function is responsible for ensuring ongoing adherence with the Company's underwriting guidelines, with oversight from the Risk function. The Company also undertakes monthly operating and risk reviews, which include detailed commentary on the Australian housing market and economy, a review of the portfolio profile, an analysis of portfolio trends and an outline of key risk issues affecting the Company.

## **Reinsurance strategy**

Through reinsurance, the Company aims to mitigate insurance risk and to manage loss exposures. Reinsurance is also used to improve capital efficiency as well as available capital and surplus. The use of reinsurance enables the Company to write a larger volume of new business than would otherwise be the case and to write policies in amounts larger than the risk the Company is willing to retain.

In January 2013, the Company terminated one of the two layers of the excess loss reinsurance arrangement with a related entity Brookfield Life Assurance Company Limited. As at 31 December 2013, the Company had reinsurance arrangements in place with Brookfield Life Assurance Company Limited, and with a number of unrelated reinsurers. In January 2014, the Company terminated the final layer of the excess loss reinsurance arrangement with Brookfield Life Assurance Company Limited to eliminate all reliance on affiliated reinsurance, effective from 1 January 2014. During the year, the Company expanded and renewed excess of loss reinsurance treaties with external Reinsurers. In aggregate, they provide a capped catastrophe reinsurance protection for losses. The Company sets the criteria for acceptable reinsurance in terms of risk appetite and counter party risk and monitors the reinsurance program to mitigate overall insurance risk.

All of the non-related reinsurers have ratings from Standard & Poor's ("S&P") or AM Best equivalent of A- or better. Brookfield Life Assurance Company Limited is an unrated company, and has supplied alternative capital support by means of commitments from its parent entity.

## **Terms and conditions of insurance contracts**

The terms and conditions of insurance contracts that have a material effect on the amount, timing and uncertainty of future cash flows arising from insurance contracts are discussed below.

### ***Product features***

The Company offers Lenders Mortgage Insurance ("LMI") and portfolio credit enhancement policies. The Company's principal product is LMI with single premiums and 100% coverage. Most business is sourced when the insured lending institutions collect an amount equal to the single premium from prospective borrowers at the time the loan proceeds are advanced and remit the amount to the Company as the mortgage insurer. A smaller proportion of business is sourced when lenders insure a portfolio of existing loans that were previously uninsured. This usually occurs when the lender plans to securitise those loans.

The Company records the proceeds to unearned premium, invests those proceeds and recognises the premiums over time in accordance with the expected expiration of risk.

LMI protects the lending institution against loss should a borrower default on their loan. If the security property is required to be sold as a result of the default, the funds received from the sale, net of selling costs, may not cover the full balance outstanding on the loan. Should this occur, the lender is entitled to make an insurance claim on the Company for reimbursement of any remaining amount outstanding, subject to the terms and conditions of the relevant LMI Master Policy of the Company.

Upon payment of a claim for a loss in respect of an insured loan, the lender assigns the insured loan contract to the Company.

## **Concentrations of insurance risks**

Insurance risk is managed primarily through pricing, product design, risk selection, investment strategy, rating and reinsurance. It is vital that the Company closely monitors and responds to any changes in the general economic and commercial environment in which it operates.

Due to the nature of the Australian economy, the majority of mortgages are originated through the country's four largest banks. The Company has a high concentration of business written on mortgages originating through three of these lenders.

Within the insurance process, concentrations of risk may arise where a particular event or series of events could impact upon the Company's liabilities.

The Company uses the global risk reporting methodology developed by its ultimate parent company, which summarises key business risk (performance) indicators, tracks key economic and business performance measures and highlights any adverse trends through use of performance triggers against plan. Concentration limits are monitored on a monthly basis. Trigger levels have been established in consultation with the ultimate parent company, for geographical dispersion, lender concentration and LVR bands. Portfolio exposure against these triggers is monitored quarterly.

The greatest likelihood of significant losses to the Company arises from a severe and prolonged economic downturn. The assumptions the Company uses to calculate these risks follow APRA's requirements to assess the probable maximum loss ("PML"). The Company's reinsurance arrangements provide protection against this exposure.

#### **Interest rate risk**

As the outstanding loan balances on loans insured by the Company include accrued interest (but not penalty interest) and most insured mortgages are variable rate mortgages, the Company has an exposure to interest rate risk as part of any potential claims in the event the proceeds of sale of a property are less than the outstanding loan balance and related expenses covered by the policy.

#### **Credit risk**

The Company's exposure to credit risk on policies it issues is minimal as non-payment of the premium will lead to policies either not being incepted or being cancelled.

The Company is exposed to credit risk on reinsurance contracts as a result of exposure to individual cedants.

As at the statement of financial position date, there are no amounts due from reinsurance cedants. However the Company does monitor its potential exposure to reinsurers in the context of the extent of the anticipated claims on the cedant and the cedants' claims paying abilities.

	2013 \$'000	2012 \$'000
<b>5 Gross written premium</b>		
Direct premium	586,478	529,212
Inward reinsurance premium	10,014	15,687
	<u>596,492</u>	<u>544,899</u>
<b>6 Financial income</b>		
Dividend income	-	10,000
Interest	161,775	174,686
Gains/ (losses) in fair value of investments		
• Unrealised	(59,172)	64,078
• Realised	666	8,531
	<u>103,269</u>	<u>257,295</u>

	2013 \$'000	2012 \$'000
<b>7 Other underwriting expenses</b>		
Depreciation and amortisation expense	5,641	6,011
Employee expenses		
• Salaries and wages	30,655	27,512
• Superannuation contributions	2,103	1,834
• Employee benefits	194	239
Occupancy expenses	3,172	3,108
Marketing expenses	820	946
Administrative expenses	20,278	16,377
	<u>62,863</u>	<u>56,027</u>

## 8 Auditor's remuneration

<b>Audit services</b>	2013 \$	2012 \$
• Audit of financial reports	269,780	300,035
• Other regulatory audit services	54,045	35,000
	<u>323,825</u>	<u>335,035</u>
<b>Other services</b>		
• Non-assurance services	1,238,695	1,493,521
	<u>1,238,695</u>	<u>1,493,521</u>

In 2013 and 2012 non-assurance services provided primarily related to the proposed IPO and were settled by the ultimate parent company.

## 9 Net claims incurred

	Current Year \$'000	2013 Prior Years \$'000	Total \$'000	Current Year \$'000	2012 Prior Years \$'000	Total \$'000
<b>Gross claims expense</b>						
Direct	180,441	(55,659)	124,782	175,312	74,748	250,060
Inwards reinsurance	10,142	(2,442)	7,700	10,098	1,052	11,150
Gross claims incurred – undiscounted and discounted	<u>190,583</u>	<u>(58,101)</u>	<u>132,482</u>	<u>185,410</u>	<u>75,800</u>	<u>261,210</u>
<b>Reinsurance and other recoveries revenue</b>						
Reinsurance and other recoveries – undiscounted and discounted	<u>2,376</u>	<u>(7,241)</u>	<u>(4,865)</u>	<u>1,914</u>	<u>(3,568)</u>	<u>(1,654)</u>
<b>Net claims incurred</b>	<u>192,959</u>	<u>(65,342)</u>	<u>127,617</u>	<u>187,324</u>	<u>72,232</u>	<u>259,556</u>

Current year amounts relate to risks borne in the current financial year. Prior year amounts relate to a reassessment of the risks borne in all previous financial years.



The favourable loss experience in 2013 is attributable to lower delinquencies as well as a reduction in paid claims resulting from a decrease in both the number of claims and average claim amount.

	2013 \$'000	2012 \$'000
<b>10 Income tax expense</b>		
(a) Income tax expense		
Current tax	80,688	74,114
Deferred tax (Note 18(c))	(4,180)	(1,473)
(Over)/under provision in prior year:		
• Current tax	(1,123)	2,022
• Deferred tax	(999)	1,038
	<u>74,386</u>	<u>75,701</u>
 (b) Numerical reconciliation of income tax expense to prima facie tax payable		
Prima facie income tax expense calculated at 30% (2012: 30%) on profit	75,617	74,301
Increase/ (decrease) in income tax expense due to:		
• Non-taxable items	(1,920)	(3,291)
• Tax benefit of New Zealand branch losses not recognised	2,811	1,631
• (Over)/ under provision in prior year	(2,122)	3,060
Income tax expense on the profit	<u>74,386</u>	<u>75,701</u>

## 11 Cash

Cash at bank	<u>84,794</u>	<u>23,071</u>
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For an analysis of the sensitivity of cash assets to currency and interest rate risk refer to Note 29(a).

## 12 Trade and other receivables

<b>Current</b>		
Other debtors	<u>6,321</u>	<u>4,621</u>

For an analysis of the sensitivity of other receivables to currency and credit risk refer to Note 29(a). Carrying amounts of receivables reasonably approximate fair value at statement of financial position date.

None of the receivables are impaired or past due.

	2013 \$'000	2012 \$'000
<b>13 Deferred reinsurance expense</b>		
Balance at 1 January	79,120	1,997
Deferral of reinsurance premium on current year contracts	78,764	131,500
Expensing of reinsurance premium previously deferred	(64,511)	(54,377)
Balance as at 31 December	<u>93,373</u>	<u>79,120</u>
Current	51,608	64,152
Non-current	<u>41,765</u>	<u>14,968</u>
	<u>93,373</u>	<u>79,120</u>

#### 14 Investments

Short term deposits	482,414	330,599
Government and semi-government bonds	1,341,850	1,290,376
Corporate bonds	<u>1,729,797</u>	<u>1,902,776</u>
	<u>3,554,061</u>	<u>3,523,751</u>
Current	1,130,082	705,649
Non-current	<u>2,423,979</u>	<u>2,818,102</u>
	<u>3,554,061</u>	<u>3,523,751</u>

All investments are classified as financial assets or assets backing insurance activities designated at fair value through profit and loss. For an analysis of the sensitivity of investments at fair value through profit or loss to currency and interest rate risks refer to Note 29(a).

#### 15 Deferred acquisition costs

Balance at 1 January	137,505	141,451
Acquisition costs incurred in year	50,172	44,161
Amortisation charge	(59,291)	(48,107)
Balance as at 31 December	<u>128,386</u>	<u>137,505</u>
Current	37,078	50,904
Non-current	<u>91,308</u>	<u>86,601</u>
	<u>128,386</u>	<u>137,505</u>

#### 16 Plant and equipment

Plant and equipment - at cost	10,288	10,136
Less: Accumulated depreciation	<u>(8,703)</u>	<u>(8,027)</u>
Total plant and equipment - net book value	<u>1,585</u>	<u>2,109</u>

##### Reconciliations

Reconciliations of the carrying amounts for plant and equipment are set out below:

	2013 \$'000	2012 \$'000
<b>Cost</b>		
Opening balance at 1 January	10,136	9,930
Additions	152	210
Disposals	-	(4)
Closing balance at 31 December	<u>10,288</u>	<u>10,136</u>
<b>Accumulated depreciation</b>		
Opening balance at 1 January	(8,027)	(6,916)
Depreciation charge	(676)	(1,114)
Disposals	-	3
Closing balance at 31 December	<u>(8,703)</u>	<u>(8,027)</u>

## 17 Intangibles

Intangibles - at cost	25,538	24,847
Less: Accumulated amortisation	<u>(18,227)</u>	<u>(13,288)</u>
Total intangibles	<u>7,311</u>	<u>11,559</u>

### Reconciliations

Reconciliations of the carrying amounts for intangibles are set out below:

<b>Cost</b>		
Opening balance at 1 January	24,847	24,868
Additions	738	-
Disposals	(47)	(21)
Closing balance at 31 December	<u>25,538</u>	<u>24,847</u>
<b>Accumulated amortisation</b>		
Opening balance at 1 January	(13,288)	(8,391)
Amortisation charge	(4,965)	(4,897)
Disposals	26	-
Closing balance at 31 December	<u>(18,227)</u>	<u>(13,288)</u>

The intangibles balance represents software development expenditure.

## 18 Deferred tax

The balance comprises temporary differences attributable to:

Deferred tax assets (a)	8,129	8,418
Deferred tax liabilities (b)	<u>(520)</u>	<u>(5,988)</u>
Net deferred tax (c)	<u>7,609</u>	<u>2,430</u>

### (a) Deferred tax assets

The balance comprises temporary differences attributable to:

Employee benefits	3,636	2,627
Purchased interest on investments	-	1,688
Provision for indirect claims handling costs	<u>4,493</u>	<u>4,103</u>
	<u>8,129</u>	<u>8,418</u>

	2013 \$'000	2012 \$'000
<b>(b) Deferred tax liabilities</b>		
The balance comprises temporary differences attributable to:		
Unrealised gains on investments	-	(415)
Research and development claims on fixed assets and intangibles	(520)	(2,743)
Accrued interest income	-	(2,830)
	<u>(520)</u>	<u>(5,988)</u>

**(c) Net deferred tax**

**Movements in net deferred tax**

Opening balance at 1 January	2,430	1,995
Credited to the statement of comprehensive income (Note 10)	4,180	1,473
Over/ (under) provision of prior year tax	999	(1,038)
Closing balance at 31 December	<u>7,609</u>	<u>2,430</u>

**19 Outstanding claims**

Central estimate	211,383	265,326
Risk margin	28,763	36,087
Gross outstanding claims	<u>240,146</u>	<u>301,413</u>

**Reconciliation of changes in outstanding claims:**

Balance at 1 January	301,413	334,920
Current year net claims incurred	127,617	259,556
Claims paid	(188,884)	(293,063)
Balance at 31 December	<u>240,146</u>	<u>301,413</u>

Current	188,091	256,096
Non-current	52,055	45,317
	<u>240,146</u>	<u>301,413</u>

**20 Unearned premiums**

Balance at 1 January	1,124,052	1,022,522
Premiums incepted during the year	596,492	544,899
Premiums earned during the year	(471,461)	(443,852)
Exchange rate revaluation adjustment	-	483
Balance as at 31 December	<u>1,249,083</u>	<u>1,124,052</u>
Current	357,103	330,476
Non-current	891,980	793,576
	<u>1,249,083</u>	<u>1,124,052</u>

**21 Trade and other payables**

Accrued expenses	15,678	27,409
Interest payable	56	31
Trade creditors	17,734	17,994
Payable to related entities	27,221	49,420
	<u>60,689</u>	<u>94,854</u>

	2013 \$'000	2012 \$'000
Current	60,089	88,004
Non current	<u>600</u>	<u>6,850</u>
	<u>60,689</u>	<u>94,854</u>

For an analysis of the sensitivity of payables to currency and liquidity risk, refer to Note 29(a).

Included in the related entity payables are the balances related to taxes payable to the head entity of \$34,625,000 (2012: \$51,912,000), net of other related party receivables. Under the tax consolidation system, current tax liabilities recognised for the year by the Company are assumed by the head entity in the tax consolidated group. The current tax liabilities arising for the Company under the tax funding agreement are recognised as an intercompany payable to the head entity in the tax consolidated group.

## 22 Employee benefits provision

Annual leave	2,651	2,744
Long service leave	<u>3,425</u>	<u>2,991</u>
	<u>6,076</u>	<u>5,735</u>
Current	4,199	3,803
Non-current	<u>1,877</u>	<u>1,932</u>
	<u>6,076</u>	<u>5,735</u>

As at the balance date there were 308 employees (2012: 294 employees).

## 23 Interest bearing liabilities

Subordinated notes	140,000	140,000
Less: capitalised transaction costs	<u>(2,259)</u>	<u>(3,011)</u>
	<u>137,741</u>	<u>136,989</u>

The subordinated notes were issued on 30 June 2011 with a face value of \$140 million and are eligible for recognition as lower Tier 2 capital in transitional arrangements under prudential standards issued by APRA. See Note 26(a)(i) for further information.

Key terms and conditions:

- Interest is payable quarterly in arrears, with the rate each calendar quarter being the average of the 90 day Bank Bill Swap rate ("BBSW") at the end of the prior quarter plus a margin equivalent to 4.75% per annum; and
- The notes mature on 30 June 2021 (non callable for the first 5 years) with the issuer having the option to redeem at par from 30 June 2016. Redemption at maturity, or any earlier date provided for in the terms and conditions of issue, is subject to prior approval by APRA.

2013	2012
\$'000	\$'000

## 24 Share capital

### Issued fully paid capital

1,401,559,000 ordinary shares (2012: 1,401,559,000)	<u>1,401,559</u>	<u>1,401,559</u>
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All Ordinary shares are fully paid. Ordinary shares have the right to receive dividends as declared and, in the event of winding up the Company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of and amounts paid up on shares held.

Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the Company.

### (a) Share based payment reserve

Balance at 1 January	2,460	1,975
Share based compensation	172	802
Share based payment recharged from parent company	<u>(678)</u>	<u>(317)</u>
Balance at 31 December	<u>1,954</u>	<u>2,460</u>

Refer to Note 35 for detailed information.

## 25 Other reserves

Other reserves	<u>(603,268)</u>	<u>(603,268)</u>
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The balance in the other reserves comprises goodwill which has not been recognised as an asset due to the acquisition of the lenders mortgage insurance business from GE Mortgage Insurance Pty Ltd and GE Capital Mortgage Insurance Corporation (Australia) Pty Ltd, being between entities under common control with the Company at that time. Consequently, goodwill has not been recognised as an asset in the financial statements of the acquirer.

## 26 Capital management

### (a) Capital management strategy

The capital management strategy plays a central role in managing risk to create shareholder value whilst meeting the crucial and equally important objective of providing an appropriate level of capital to protect policyholders' and lenders' interests and satisfy regulators. Capital finances growth, capital expenditure and business plans and also provides support in the face of adverse outcomes from insurance and other activities and investment performance.

The determination of the capital amount and mix is built around three core considerations. The Company aims to hold capital to meet the highest requirements derived from these three considerations:

#### (i) Regulatory capital

APRA introduced the new Life and General Insurance Capital Standards ("LAGIC") with effect from 1 January 2013. The introduction of these standards mandates a new methodology of calculating prescribed capital, with the minimum required capital (formerly Minimum Capital Requirement ("MCR")) now known as the Prescribed Capital Requirement ("PCR").

The Company is subject to APRA's prudential standards, which set out the basis for calculating the PCR, which is the minimum level of capital that the regulator deems must be held to meet policyholder obligations. The capital base is expected to be adequate for the size, business mix, complexity and risk profile of the business and so the PCR utilises a risk based approach to capital adequacy. The PCR is the sum of the capital charges for insurance, investments and other assets, investment concentration, operational and catastrophe concentration risk plus any supervisory adjustment imposed by APRA.

Under the LAGIC regime the subordinated notes of \$140,000,000 no longer qualify for recognition as regulatory capital. Transitional arrangements are available to phase out these capital instruments over a 9 year period which has been approved by APRA. Consequently only 90% of the value of the subordinated notes is included in the capital base.

It is the Company's policy to hold regulatory capital levels in excess of the PCR required by APRA. The Company maintains sufficient capital to support the PCR, which is APRA's derivation of the required capital to meet a 1 in 200 year risk of absolute ruin, and has at all times during the current and prior financial year complied with the externally imposed capital requirements to which it is subject.

Capital calculations for regulatory purposes are based on a premium liabilities model, which is different from the deferral and matching model which underpins the measurement of assets and liabilities in the financial statements. The premium liabilities model estimates future expected claim payments arising from future events insured under existing policies. This differs from the measurement of the outstanding claims liabilities on the statement of financial position, which considers claims relating to events that occur only up to and including the reporting date.

*(ii) Ratings capital*

The Company sets its target capital strength by reference to a target financial strength rating from an independent ratings agency. The ratings help to reflect the financial strength of the Company and demonstrate to the stakeholders the ability to pay claims for the long term. The Company has AA- and A3 ratings based on latest ratings published for the Company by Standard & Poor's Rating Services and Moody's, respectively.

*(iii) Economic capital*

In conjunction with the considerations set out above, which are important to the functioning of the business, consideration is given to the capital needs of the business through ongoing operations.

**(b) Internal capital adequacy assessment process (ICAAP)**

Effective 1 January 2013, the Company has implemented an ICAAP as part of its compliance with the new LAGIC standards. The purpose of ICAAP is to assist the Company in making a proactive internal assessment of its capital requirements considering the current strategy, business plan and associated risks inherent in that business plan. In addition to the internal capital requirement, the ICAAP recognises the capital required for regulatory and ratings agency purposes, and identifies planned and potential sources of capital required to meet these objectives. The ICAAP is also designed to further augment the current corporate governance practices undertaken by the Board of Directors in respect of the ongoing assessment of the Company's risk profile, risk appetite, strategic plan and capital adequacy.

The ICAAP summary statement is designed to summarise the major components of the ICAAP, which are:

- (i) Risk Management Framework
- (ii) Risk Management Strategy

(iii) Capital Management and Planning

- The identification of the amount of capital required to be held against the risks of the business;
- The strategy for ensuring adequate capital is maintained over time, including the identification of specific capital targets; and
- The plans for how target levels of capital are to be met and the means available for sourcing additional capital if and when required;

(iv) Capital Monitoring

- The actions and procedures for monitoring the Company's compliance with its regulatory capital requirements and capital targets including the triggers to alert management to, and specified actions to avert and rectify, potential breaches of these requirements;
- The processes for reporting on the ICAAP and its outcomes to the Board and senior management.

(v) Stress Testing and scenario analysis relating to potential risk exposures and available capital resources.

(vi) ICAAP integration - ensuring that the ICAAP is taken into account in making business decisions.

(c) **Capital composition**

Total capital is defined as equity as shown in the statement of financial position. Consideration is also given to capital support from reinsurance and any debt, although the extent of recognition varies depending on the capital basis being assessed.

(d) **Regulatory capital compliance**

APRA's prudential standards require additional disclosure of regulatory capital in the annual financial statements.

	2013 \$'000
<b>Tier 1 capital</b>	
Paid-up ordinary shares	1,401,559
Other reserves	(601,314)
Retained earnings	1,376,413
Less: Deductions	(36,136)
Net surplus relating to insurance liabilities	253,430
<b>Net Tier 1 capital</b>	<u>2,393,952</u>
<b>Tier 2 capital</b>	126,000
<b>Total capital base</b>	<u>2,519,952</u>
Insurance risk charge	179,365
Insurance concentration risk charge	1,435,217
Asset risk charge	123,761
Asset concentration risk charge	-
Operating risk charge	21,824
Aggregation benefit	(58,457)
<b>Total prescribed capital amount</b>	<u>1,701,710</u>
<b>Prescribed Capital Amount coverage</b>	<u>1.48</u>



Prior to 1 January 2013, under the previous regulatory reporting requirements, the Company was subject to a different capital base calculation and MCR.

	2012 \$'000
<b>Tier 1 capital (section 1)</b>	
Paid-up ordinary shares	1,401,559
Other reserves	(600,807)
Retained earnings	1,328,741
Less: Deductions	(48,643)
Net surplus relating to insurance liabilities	251,686
Net Tier 1 capital	2,332,536
Net Lower Tier 2 capital	140,000
Total capital base	2,472,536
Minimum capital requirement	1,657,605
<b>Capital adequacy multiple</b>	<u>1.49</u>

## 27 Commitments

### Operating lease commitments

	2013 \$'000	2012 \$'000
The estimated future amounts of operating lease commitments not provided for in the financial statements are payable:		
Within one year	3,442	5,851
One year or later and no later than five years	21,768	21,445
More than five years	-	3,324
	<u>25,210</u>	<u>30,620</u>

The Company leases property and equipment under operating leases expiring from one to five years. Leases of property generally provide the Company with a right of renewal at which time all terms are renegotiated. Lease payments comprise a base amount plus an incremental contingent rental. Contingent rentals are generally based on movements in the Consumer Price Index.

## 28 Dividends

### (a) Ordinary shares

The Group paid an ordinary dividend of \$0.0928 per ordinary share, amounting to \$130,000,000, to its shareholder, Genworth Financial Services Pty Limited on 14 June 2013. In 2012, the Company paid an ordinary dividend of \$0.0228 per ordinary share, amounting to \$32,000,000 to its shareholder on 21 December 2012.

### (b) Dividend franking account

In accordance with the tax consolidation legislation Genworth Financial New Holdings Pty Limited, as the head entity in the tax consolidated group, has assumed the benefit of available franking credits.

## 29 Financial risk management

The activities of the Company expose it to a variety of financial risks such as market risk (including currency risk, cash flow and fair value interest rate risk), credit risk and liquidity risk. The Company

has a Risk Management Strategy ("RMS") which is discussed in more detail in Note 4. The risk management framework recognises the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Company.

The key objectives of the Company's asset and liability management strategy are to ensure sufficient liquidity is maintained at all times to meet the Company's obligations, including settlement of its insurance liabilities and, within these parameters, to optimise investment returns for policyholders and shareholders.

**(a) Market risk**

*(i) Currency risk*

Currency risk is the risk of loss arising from an unfavourable movement in market exchange rates. The Company is exposed to currency risk on its investments in international receivables and payables denominated in a currency other than Australian dollars and the net investment in foreign branch operations. The currency giving rise to the risk is New Zealand dollars.

The potential impact on the Company's profit and loss and equity as a result of a 10% depreciation/appreciation of the Australian dollar at the reporting date, assuming all other variables remain constant, is shown below.

	2013		2012	
	+10%	-10%	+10%	-10%
	\$'000	\$'000	\$'000	\$'000
Impact to profit and loss and equity of 10% depreciation/ appreciation of Australian Dollar on New Zealand assets and liabilities.	399	(488)	1,047	(1,280)

*(ii) Cash flow and fair value interest rate risk*

The Company is exposed to interest rate risk arising on interest bearing assets. Assets with floating rate interest expose the Company to cash flow interest rate risk. Fixed interest rate assets expose the Company to fair value interest rate risk. The Company's strategy is to invest in high quality, liquid fixed interest securities and cash and to actively manage duration. The investment portfolios are actively managed to achieve a balance between cash flow interest rate risk and fair value interest rate risk bearing in mind the need to meet the liquidity requirements of the insurance business.

The Company is also exposed to interest rate risk on its term subordinated notes. The interest rate on these notes is reset quarterly. The Company manages the level of assets with similar maturities to offset this exposure.

The potential impact of movements in interest rates on the Company's profit and loss and equity are shown below.

	2013	2012
	\$'000	\$'000
+1% increase in interest rates	(57,600)	(67,987)
-1% decrease in interest rates	58,242	68,719

**(b) Credit risk exposures**

Credit risk is the risk of loss from a counterparty failing to meet their financial obligations. The Company's credit risk arises predominantly from investments and the amounts are as indicated by the carrying amounts of the financial assets.

The Company's investment portfolio comprises 98% (2012 98%) of total fixed interest and cash with counterparties having a rating of A- or better. The Company does not expect any investment counterparties to fail to meet their obligations given their strong credit ratings.

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if available) or to historical information about counterparty default rates. As at balance date there were no assets past due.

The ratings in the following table are the lower equivalent rating of either Standard & Poor's or Moody's.

	2013 \$'000	2012 \$'000
Cash at bank and short-term bank deposits		
AAA	1	1
AA	437,419	318,083
A	111,788	17,586
BBB	18,000	18,000
	567,208	353,670
Investments		
AAA	1,642,472	2,002,196
AA	950,913	697,501
A	417,511	439,532
BBB	60,751	53,923
	3,071,647	3,193,152
Accrued investment income		
AAA	19,497	24,682
AA	13,803	9,941
A	5,489	6,583
BBB	1,234	318
	40,023	41,524
Receivables without external credit rating	6,321	4,621

*Note: Investments are grouped by grade*

### (c) Liquidity risk

Liquidity risk is the risk of there being insufficient cash resources to meet payment obligations without affecting the daily operations or the financial condition of the Company.

Management of liquidity risk includes asset and liability management strategies. The assets held to back insurance liabilities consist predominantly of highly rated fixed income securities which can generally be readily sold or exchanged for cash. The assets are managed so as to effectively match the maturity profile of the assets with the expected pattern of claims payments.

The money market securities are restricted to investment grade securities with concentrations of investments managed as per the investment mandate. Details of the Company's investments are provided in Note 14.

2013	Less than 1 year	1 - 5 years	Total
Financial liabilities	\$'000	\$'000	\$'000
Payables	60,089	600	60,689
Reinsurance payable	67,346	41,765	109,111
Outstanding claims provision	188,091	52,055	240,146
	315,526	94,420	409,946

2012	Less than 1 year	1 - 5 years	Total
<i>Financial liabilities</i>	\$'000	\$'000	\$'000
Payables	88,004	6,850	94,854
Reinsurance payable	80,806	14,833	95,639
Outstanding claims provision	256,096	45,317	301,413
	424,906	67,000	491,906

(d) **Fair value measurements**

The Company's financial assets and liabilities are carried in the statement of financial position at amounts that approximate fair value.

The Company investments carried at fair value have been classified under the three levels of the IFRS fair value hierarchy as follows:

Level 1 - Quoted prices in an active market: Fair value investments which are quoted in active and known markets. The quoted prices are those at which transactions have regularly and recently taken place within such markets.

Level 2 - Valuation techniques with observable parameters: Fair value investments using inputs other than quoted prices within Level 1 that are observable either directly or indirectly.

Level 3 - Valuation techniques with significant unobservable parameters: Fair value investments using valuation techniques that include inputs that are not based on observable market data.

2013	Level 1	Level 2	Level 3	Total
	\$'000	\$'000	\$'000	\$'000
<b>Investments</b>				
Government and semi-government bonds	-	1,341,373	477	1,341,850
Corporate bonds	-	1,681,297	48,500	1,729,797
<b>Total</b>	-	3,022,670	48,977	3,071,647

2012	Level 1	Level 2	Level 3	Total
	\$'000	\$'000	\$'000	\$'000
<b>Investments</b>				
Government and semi-government bonds	-	1,289,973	403	1,290,376
Corporate bonds	-	1,854,276	48,500	1,902,776
<b>Total</b>	-	3,144,249	48,903	3,193,152

Note: Short term deposits have not been included in the above fair value assessment.

There is an insignificant proportion of investments, 2% (2012: 2%), for which a valuation methodology is used to determine the fair value. These assets are effectively marked to model rather than marked to market. Reasonable changes in the judgement applied in conducting these valuations would not have a significant impact on the statement of financial position.

The following table shows a reconciliation from the beginning balances to the ending balances for fair value measurements in Level 3 of the fair value hierarchy:

	Balance at 1 January 2013	Purchases	Disposals	Movement in fair value	Balance at 31 December 2013
2013	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Financial Instruments</b>					
Government and semi-government bonds	403	440	(425)	59	477
Corporate bonds	48,500	-	-	-	48,500
<b>Total</b>	48,903	440	(425)	59	48,977

	Balance at 1 January 2012	Purchases	Disposals	Movement in fair value	Balance at 31 December 2012
2012	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Financial Instruments</b>					
Government and semi- government bonds	400	-	-	3	403
Corporate bonds	48,500	-	-	-	48,500
<b>Total</b>	<b>48,900</b>	<b>-</b>	<b>-</b>	<b>3</b>	<b>48,903</b>

The interest bearing liabilities were initially measured at face value (net of transaction costs) but are subsequently measured at amortised cost. The Company considers the fair value of the interest bearing liabilities to be equal to that of the carrying value.

### 30 Notes to the statement of cash flows

#### (a) Reconciliation of cash

For the purposes of the statement of cash flows, cash includes cash on hand and at bank and short term deposits at call, net of outstanding bank overdrafts. Cash as at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the statement of financial position as follows:

	2013 \$'000	2012 \$'000
Cash assets (Note 11)	84,794	23,071
Short term deposits (Note 14)	482,414	330,599
	<u>567,208</u>	<u>353,670</u>

#### (b) Reconciliation of profit after income tax to net cash provided by operating activities

Profit after income tax	177,672	171,970
Add/(less) items classified as investing/financing activities:		
Gain on sale of investments	(666)	(8,531)
Unrealised losses/ (gains) on investments	59,172	(64,078)
Add non-cash items:		
Share based payments	(506)	485
Depreciation and amortisation	5,641	6,011
Net cash provided by operating activities before change in assets and liabilities	241,313	105,857
Change in assets and liabilities during the financial year:		
Decrease/ (increase) in receivables	10,955	(63,066)
Decrease in outstanding claims liability	(61,267)	(33,507)
(Decrease)/ increase in payables and borrowings	(19,941)	53,092
Decrease in deferred acquisition costs	9,119	3,946
Increase in deferred tax balances	(5,179)	(435)
Increase in employee benefits provision	341	429
Increase in unearned premiums	125,031	101,530
Net cash provided by operating activities	<u>300,371</u>	<u>167,846</u>

### 31 Key management personnel disclosures

The following were key management personnel of the Company at any time during the reporting period and unless otherwise indicated, were key management personnel for the entire period:

#### Directors of the Company

Ellie Comerford  
Anthony Gill  
Richard Grellman  
Ian MacDonald  
Samuel Marsico  
Leon Roday  
Stuart Take  
Gayle Tollifson  
Jerome Upton

#### Executives

Paul Caputo (Resigned 9 July 2013)  
Ellie Comerford  
Jon Downes (Appointed 23 September 2013)  
Paul Fegan (Appointed 7 January 2013 and resigned 5 December 2013)  
Tobin Fonseca  
Richard Galilee  
Conor O'Dowd (Appointed 18 November 2013)  
Jo Ann Rabitz  
Martha Ryan (Resigned 9 August 2013)  
Bridget Sakr

	2013 \$'000	2012 \$'000
<b>The key management personnel compensation is:</b>		
Short-term employee benefits	5,893	3,517
Post-employment benefits	259	310
Termination benefits	-	-
Equity compensation benefits	1,292	661
	<u>7,444</u>	<u>4,488</u>

### 32 Related party disclosures

#### Related party transactions

Transactions with related parties are undertaken on normal commercial terms and conditions.

During the year the Company paid \$4,340,000 (2012: \$42,485,000) to settle the final 2012 year tax liabilities to Genworth Financial New Holdings Pty Limited under the terms of the tax sharing agreement, and \$92,513,000 (2012: \$53,332,000) as interim tax funding amounts notified under the terms of the tax funding agreement.

The Company paid \$5,000,000 (2012: \$Nil) of intercompany payables to Genworth Financial Mortgage Insurance Holdings Pty Limited during the year. The Company settled \$2,000 (2012: \$61,000) of intercompany liabilities to Genworth Financial Mortgage Indemnity Limited respectively during the year.

#### Reinsurance policies

The Group has in place an excess of loss reinsurance contract with Brookfield Life Assurance Limited.

Reinsurance premiums of \$9,053,000 (2012: \$26,103,000) were ceded during the year. A premium of \$1,930,000 (2012: \$2,781,000) is payable for the contracts as at 31 December 2013.

### Corporate overhead

Effective 1 January 2013 the Company entered into a contractual arrangement with related Company Genworth Financial International Holdings Inc for the provision of IT services. The amount charged to the Company during the year was \$1,394,000. In addition the Company received a range of other services from Genworth Financial Inc. The amount charged to the Company during the year was \$2,861,000 (2012: \$3,585,000).

### Dividend

The Group paid an ordinary dividend of \$0.0928 per ordinary share, amounting to \$130,000,000, to its shareholder, Genworth Financial Services Pty Limited on 14 June 2013. In 2012, the Company paid an ordinary dividend of \$0.0228 per ordinary share, amounting to \$32,000,000 to its shareholder on 21 December 2012.

In 2012 the Company received from Genworth Financial Mortgage Indemnity Limited an ordinary dividend amounting to \$10,000,000

### Parent and ultimate parent entity

The immediate Australian parent entity of the Company is Genworth Financial Services Pty Limited. The ultimate parent entity is Genworth Financial Inc, a company incorporated in the United States of America.

### Other related party transactions

The Company has a services agreement with Genworth Financial Australia Holdings LLC ("LLC"), whereby LLC provides corporate advisory and treasury services to the Company. The amount charged to the Company during the year was \$2,685,000 (2012: \$2,099,000) with fees payable of \$203,000 (2012: \$647,000) as at 31 December 2013.

## 33 Controlled entity

Investment in controlled entity is carried at the cost of acquisition less accumulated impairment in the Company's financial statements.

<i>Name of entity</i>	<i>Country of incorporation</i>	<i>Class of shares</i>	<i>Equity holding (%)</i>	
			2013	2012
Genworth Financial Mortgage Indemnity Limited	Australia	Ordinary	100	100

## 34 Liability adequacy test

The liability adequacy test ("LAT") has identified a surplus for the portfolio of contracts that are subject to broadly similar risks.

The PoS adopted in performing the LAT is set at the 75<sup>th</sup> percentile (2012: 75<sup>th</sup> percentile).

For the purposes of the liability adequacy test, the present value of expected future cash flows for future claims, including the risk margin, for the Company are as follows:

	2013 \$'000	2012 \$'000
Discounted central estimate of premium liability	581,945	496,935
Risk margin – premium liability (75% PoS)	156,013	103,688
	<u>737,958</u>	<u>600,623</u>

### 35 Share-based payments

The ultimate parent entity grants share-based awards to employees of subsidiaries in the form of share appreciation rights (“SAR”) and RSUs under the Genworth Financial Inc Omnibus Incentive Plan.

For awards issued prior to 1 January 2006, share-based expense is recognised on a graded vesting attribution method over the awards’ respective vesting schedules. For awards issued after 1 January 2006, share-based expense is recognised evenly on a straight-line attribution method over the awards’ respective vesting periods.

On 15 February 2013, the ultimate parent granted 15,000 share appreciation rights (“SARs”) to employees and directors. The number of shares of stock delivered upon exercise is based on the increase in share price of the ultimate parent between grant date and the time of exercise. These SARs have a feature that places a cap on the amount of gain that can be recognised upon exercise of the SARs. Specifically, if the price of the Class A Common Stock reaches US\$75.00 (2012: \$75.00), any vested portion of the SAR will be automatically exercised.

The estimated fair value of share-based payment awards on the date of grant is calculated using the Black-Scholes Model. The Black-Scholes Model requires the input of certain assumptions that involve judgement. Management periodically evaluates the assumptions and methodologies used to calculate estimated fair value of share-based payments. Circumstances may change and additional data may become available over time, which could result in changes to these assumptions and methodologies.

The following table contains the SAR weighted-average grant-date fair value information and related valuation assumptions for the years ended 31 December:

	2013	2012
Estimated fair value per option	\$2.77	\$2.42
Valuation assumptions:		
Expected term (years)	6	6
Expected volatility	101.7%	99.8%
Expected dividend yield	0.5%	0.5%
Risk-free interest rate	1.1%	1.2%

One-fourth of the SARs vests on each of the first, second, third and fourth anniversaries of the Grant Date, provided that there has been continuous service with the Company or one of its Affiliates through such dates. Unvested SARs are immediately cancelled upon termination of service with the Company or its Affiliates before the expiry date, except under certain conditions.

On 15 February 2013 and 1 August 2013 the ultimate parent entity issued 198,100 and 13,500 RSUs respectively, with restriction periods ranging from three to eight years with a fair value of \$9.26 and \$11.71, measured at the market price of the non-restricted shares on the grant date.

One-fourth of the RSUs vest on each of the first, second, third and fourth anniversaries of the Grant Date, provided that there has been continuous service with the Company or one of its Affiliates through such dates. Unvested RSUs are immediately cancelled upon termination of service with the Company or its Affiliates, except under certain conditions.



Details of the number of employee options granted, exercised and forfeited or cancelled during the year were as follows:

2013								
Grant date	Expiry Date	Exercise Price	Balance at 1 January 2013 Number	Granted in the year Number	Exercised in the year Number	Cancelled/ forfeited in the year Number	Balance at 31 December 2013 Number	Vested and exercisable at end of the year Number
25/05/2004	25/05/2014	21.8292	24,680	-	-	250	24,430	24,430
20/07/2005	20/07/2015	35.9342	2,400	-	-	-	2,400	2,400
09/08/2006	09/08/2016	38.2066	7,500	-	-	900	6,600	6,600
13/02/2008	13/02/2018	25.5233	7,800	-	-	-	7,800	7,800
12/02/2009	12/02/2019	2.7538	24,500	-	2,600	1,400	20,500	20,500
19/08/2009	25/05/2014	8.7317	9,135	-	7,583	-	1,552	1,552
19/08/2009	20/07/2015	8.7317	2,864	-	2,466	-	398	398
19/08/2009	09/08/2016	8.7317	3,731	-	2,483	-	1,248	1,248
19/08/2009	03/10/2016	8.7317	1,110	-	-	-	1,110	1,110
19/08/2009	31/07/2017	8.7317	4,749	-	2,600	-	2,149	2,149
19/08/2009	13/02/2018	8.7317	7,550	-	3,800	-	3,750	3,750
12/02/2010	12/02/2020	15.8737	22,800	-	-	-	22,800	17,100
09/02/2011	09/02/2021	14.2729	12,000	-	-	-	12,000	6,000
14/02/2012	14/02/2022	9.9407	14,700	-	-	-	14,700	11,025
15/02/2013	15/02/2023	10.1422	-	15,000	-	-	15,000	-
Total			145,519	15,000	21,532	2,550	136,437	106,062
Weighted average exercise price			\$14.51	\$10.14	\$8.01	\$17.14	\$15.00	\$15.85

2012								
Grant date	Expiry Date	Exercise Price	Balance at 1 January 2012 Number*	Granted in the year Number	Exercised in the year Number	Cancelled/ forfeited in the year Number	Balance at 31 December 2012 Number	Vested and exercisable at end of the year Number
25/05/2004	13/09/2012	16.6223	3,757	-	-	3,757	-	-
	25/05/2014	18.7554	25,430	-	-	750	24,680	24,680
20/07/2005	20/07/2015	30.8743	2,400	-	-	-	2,400	2,400
09/08/2006	09/08/2016	32.8268	10,290	-	-	2,790	7,500	7,500
13/02/2008	13/02/2018	21.9294	7,800	-	-	-	7,800	6,240
12/02/2009	12/02/2019	2.3661	31,700	-	7,200	-	24,500	24,500
19/08/2009	25/05/2014	7.5022	9,135	-	-	-	9,135	9,135
19/08/2009	20/07/2015	7.5022	3,064	-	200	-	2,864	2,864
19/08/2009	09/08/2016	7.5022	3,931	-	200	-	3,731	3,731
19/08/2009	03/10/2016	7.5022	1,110	-	-	-	1,110	1,110
19/08/2009	31/07/2017	7.5022	5,466	-	717	-	4,749	4,749
19/08/2009	13/02/2018	7.5022	8,300	-	750	-	7,550	5,100
01/12/2009	01/12/2019	10.7723	15,000	-	-	15,000	-	-
01/12/2009	01/12/2019	10.7723	15,000	-	-	15,000	-	-
12/02/2010	12/02/2020	13.6385	22,800	-	-	-	22,800	11,400
09/02/2011	09/02/2021	12.2632	12,000	-	-	-	12,000	-
14/02/2012	14/02/2022	8.5409	-	14,700	-	-	14,700	-
Total			162,183	14,700	9,067	22,297	145,519	103,409
Weighted average exercise price			\$13.82	\$8.54	\$3.42	\$18.76	\$12.97	\$12.90

\*Balance at 1 January 2012 is adjusted for options granted in prior periods to employees who transferred into/ out of the Australian Company during the year.

Details of the number of employee RSUs granted, exercised and forfeited or cancelled during the year were as follows:

2013						
Grant date	Balance at 1 January 2013	Granted in the year	Exercised in the year	Cancelled/forfeited in the year	Balance at 31 December 2013	Vested and exercisable at end of the year
	Number	Number	Number	Number	Number	Number
03/01/2005	3,750	-	3,750	-	-	-
07/02/2007	2,500	-	-	-	2,500	-
13/02/2008	5,310	-	5,310	-	-	-
10/02/2010	13,829	-	6,915	916	5,998	-
01/11/2010	5,000	-	2,500	-	2,500	-
01/03/2011	15,000	-	5,000	-	10,000	-
02/09/2011	34,322	-	11,444	1,166	21,712	-
03/01/2012	15,000	-	3,750	-	11,250	-
06/01/2012	5,000	-	1,250	-	3,750	-
11/01/2012	25,000	-	6,250	-	18,750	-
14/02/2012	96,433	-	24,113	13,748	58,572	-
15/02/2013	-	198,100	-	24,500	173,600	-
1/08/2013	-	13,500	-	-	13,500	-
Total	221,144	211,600	70,282	40,330	322,132	-

2012						
Grant date	Balance at 1 January 2012*	Granted in the year	Exercised in the year	Cancelled/forfeited in the year	Balance at 31 December 2012	Vested and exercisable at end of the year
	Number	Number	Number	Number**	Number**	Number
03/01/2005	3,750	-	-	-	3,750	-
07/02/2007	3,750	-	1,250	-	2,500	-
31/07/2007	4,526	-	3,326	1,200	-	-
13/02/2008	5,910	-	-	600	5,310	-
12/02/2009	2,755	-	2,755	-	-	-
10/02/2010	26,523	-	8,844	3,850	13,829	-
01/11/2010	7,500	-	2,500	-	5,000	-
01/03/2011	20,500	-	5,000	500	15,000	-
02/09/2011	58,102	-	14,658	9,122	34,322	-
03/01/2012	-	15,000	-	-	15,000	-
06/01/2012	-	5,000	-	-	5,000	-
11/01/2012	-	25,000	-	-	25,000	-
14/02/2012	-	96,433	-	-	96,433	-
Total	133,316	141,433	38,333	15,272	221,144	-

\*Balance at 1 January 2012 is adjusted for options granted in prior periods to employees who transferred into/ out of the Australian Company during the year.

\*\*Cancellations during 2012 for the grant dates of 1/03/2011 and 02/09/2011 have been restated by an increased 500 and 124 respectively.

Total expenses arising from share-based payment transactions recognised during the period as part of employee benefit expense were as follows:

	2013 \$'000	2012 \$'000
Share-based payment expense	<u>172</u>	<u>802</u>

### **36 Events subsequent to reporting date**

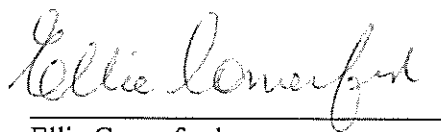
There has not been any matter or circumstance that has arisen since the end of the financial year to the date of this report that, in the opinion of the directors of the Company, would significantly affect the operations of the Company, the results of those operations or the state of affairs of the Company in future financial years.

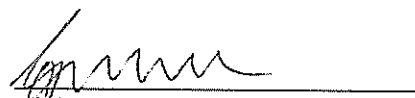
# Directors' declaration

In the opinion of the directors of Genworth Financial Mortgage Insurance Pty Limited (the "Company"):

- (a) the financial statements and notes set out on pages 5 to 42 are in accordance with the Corporations Act 2001, including:
  - (i) giving a true and fair view of the financial position of the Company as at 31 December 2013 and of its performance, as represented by the results of its operations and its cash flows for the year ended on that date; and
  - (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
- (b) the financial statements and notes also comply with International Financial Reporting Standards; and
- (c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in accordance with a resolution of the directors:

  
Ellie Comerford  
Director

  
Richard Grellman  
Director

Dated at Sydney, 12 February 2014.



## **Independent auditor's report to the members of Genworth Financial Mortgage Insurance Pty Limited**

### **Report on the financial report**

We have audited the accompanying financial report of Genworth Financial Mortgage Insurance Pty Limited (the Company), which comprises the statement of financial position as at 31 December 2013, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, notes 1 to 36 comprising a summary of significant accounting policies and other explanatory information and the directors' declaration.

### *Directors' responsibility for the financial report*

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement whether due to fraud or error. In note 1, the directors also state, in accordance with Australian Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

### *Auditor's responsibility*

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We performed the procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001* and Australian Accounting Standards, a true and fair view which is consistent with our understanding of the Company's financial position and of its performance.



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

*Independence*

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

*Auditor's opinion*

In our opinion:

(a) the financial report of Genworth Financial Mortgage Insurance Pty Limited is in accordance with the *Corporations Act 2001*, including:

- (i) giving a true and fair view of the Company's financial position as at 31 December 2013 and of its performance for the year ended on that date; and
- (ii) complying with Australian Accounting Standards and the Corporations Regulations 2001.

(b) the financial report also complies with International Financial Reporting Standards as disclosed in note 1.

KPMG

Ian Moyser  
Partner

Sydney

12 February 2014