**QBE INSURANCE (INTERNATIONAL) LIMITED**

**(A.C.N. 000 000 948)**

**FINANCIAL REPORT – 31 DECEMBER 2014**

**INDEX**



This financial report includes separate financial statements for QBE Insurance (International) Limited (the company) as an individual entity. All amounts in the financial report are presented in Australian dollars unless otherwise stated.

QBE Insurance (International) Limited is a company limited by shares, incorporated and domiciled in Australia. Its registered office is:

Level 27, 8-12 Chifley Square
Sydney NSW 2000
Australia

A description of the nature of the company's operations and its principal activities is included in the directors' report on pages 1 to 4, which is not part of this financial report.

The financial report was authorised for issue by the directors on 18 February 2015. The directors have the power to amend and reissue the financial report.

## QBE INSURANCE (INTERNATIONAL) LIMITED

### DIRECTORS' REPORT

For the year ended 31 December 2014

Your directors present their report on QBE Insurance (International) Limited (the company) as at 31 December 2014 and for the year then ended.

Directors

The following directors held office during the financial year and up to the date of this report:

S P Burns (appointed on 14 February 2014)
D L Fried
G J Gilbert
The Hon. N F H Greiner
A G McGrath
J D Neal (resigned on 14 February 2014)
D A M Ramsay (resigned on 14 February 2014)
J E Skinner
V J Walter

Principal activity

The principal activity of the company continued to be underwriting of general insurance. There were no significant changes to the principal activity during the year.

Results and review of operations

The results of the company for the year were as follows:

| | 2014 $M | 2013 $M |
|---|---|---|
| Gross written premium | **551.9** | 493.0 |
| Gross earned premium | **538.7** | 476.9 |
| Net earned premium | **338.2** | 288.7 |
| Net claims incurred | **(168.8)** | (115.6) |
| Net commission | **(56.7)** | (55.8) |
| Underwriting and other expenses | **(85.6)** | (66.1) |
| Net underwriting result | **27.1** | 51.2 |
| Net investment income on policyholders' funds | **5.0** | 8.8 |
| Insurance profit | **32.1** | 60.0 |
| Net investment income on shareholder's funds | **7.7** | 12.5 |
| Profit before income tax | **39.8** | 72.5 |
| Income tax expense | **(19.8)** | (16.5) |
| Net profit after tax | **20.0** | 56.0 |

The net combined operating ratio increased from 82.4% in 2013 to 92.0% in 2014.

Gross written premium increased 11.9% from $493.0 million in 2013 to $551.9 million in 2014, due to growth in Singapore and New Zealand. The loss ratio has increased from 40% to 50% mainly due to increased losses in the New Zealand operation.

## QBE INSURANCE (INTERNATIONAL) LIMITED

## DIRECTORS' REPORT

For the year ended 31 December 2014

Controlling entities

The entity is a company limited by shares, incorporated and domiciled in Australia. The parent entity is QBE Holdings (AAP) Pty Limited, incorporated in Australia, and the ultimate parent entity is QBE Insurance Group Limited (QBE Group), incorporated in Australia.

The controlling entity's registered office is at Level 27, 8-12 Chifley Square, Sydney, NSW 2000 Australia.

Employee numbers

At the reporting date the company employed 495 persons (2013: 475).

Dividends

The dividends paid during the year totalled $3.3 million (2013: $5.3 million).

Options

There were no options granted by the company during the year (2013: nil).

Likely developments

Information on likely developments in the company's operations in future financial years and the expected results of those operations has not been included in this report because disclosure of such information would be likely to result in unreasonable prejudice to the company.

Significant changes

There were no significant changes in the state of affairs of the company during the financial year.

Events subsequent to balance sheet date

At the date of this report, no matter or circumstance has arisen since 31 December 2014 that has significantly affected, or may significantly affect:

(i) the company's operations in future financial years;
(ii) the results of those operations in future financial years; or
(iii) the company's state of affairs in future financial years.

Environmental regulation

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

**QBE INSURANCE (INTERNATIONAL) LIMITED**

**DIRECTORS' REPORT**
For the year ended 31 December 2014

Directors' benefits

No director of the company has received or become entitled to receive a benefit (other than a remuneration benefit) by reason of a contract made or proposed by the company or a related entity with a director or with a firm of which the director is a member or with an entity in which the director has a substantial financial interest.

Indemnification and insurance

During the year, a related company paid insurance premiums in respect of a contract insuring directors and officers of the company. The officers of the company covered by the insurance contract include the directors listed on page 1 and the company secretaries, P E Barnes, P Smiles and A R Croy. In accordance with normal commercial practice, disclosure of the total amount of premium payable under, and the nature of liabilities covered by, the insurance contract are prohibited by a confidentiality clause in the contract.

Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the Corporations Act 2001 is set out on page 4.

Rounding of amounts

The company is of a kind referred to in the ASIC class order 98/100, dated 10 July 1998 (as amended by class order 04/667 dated 15 July 2004) relating to the "rounding off" of amounts in the directors' report. Amounts in the directors' report have been rounded off in accordance with that class order to the nearest one hundred thousand dollars or, in certain cases, to the nearest thousand dollars in accordance with that class order.

Auditors

PricewaterhouseCoopers continues in office in accordance with Section 327 of the Corporations Act 2001.

This report is made in accordance with a resolution of the directors.

Director ..................................................

Director ..................................................

Sydney
18 February 2015

pwc

## Auditor's Independence Declaration

As lead auditor for the audit of QBE Insurance (International) Limited for the year ended 31 December 2014, I declare that to the best of my knowledge and belief, there have been:

a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and

b) no contraventions of any applicable code of professional conduct in relation to the audit.

R Balding
Partner
PricewaterhouseCoopers

Sydney
18 February 2015

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## QBE INSURANCE (INTERNATIONAL) LIMITED

### STATEMENT OF COMPREHENSIVE INCOME
For the year ended 31 December 2014

| | NOTE | 2014 $M | 2013 $M |
|---|---|---|---|
| Gross written premium | | **551.9** | 493.0 |
| Unearned premium movement | | **(13.2)** | (16.1) |
| Gross earned premium revenue | 5(A) | **538.7** | 476.9 |
| Outward reinsurance premium | | **(197.8)** | (173.0) |
| Deferred reinsurance premium movement | | **(2.7)** | (15.2) |
| Outward reinsurance premium expense | 5(B) | **(200.5)** | (188.2) |
| Net earned premium | | **338.2** | 288.7 |
| Gross claims incurred | 5(B) | **(290.4)** | (194.8) |
| Reinsurance and other recoveries revenue | 5(A) | **121.6** | 79.2 |
| Net claims incurred | 6(A) | **(168.8)** | (115.6) |
| Gross commission expense | 5(B) | **(74.3)** | (69.2) |
| Reinsurance commission revenue | 5(A) | **17.6** | 13.4 |
| Net commission | | **(56.7)** | (55.8) |
| Other acquisition costs | 5(B) | **(26.8)** | (21.2) |
| Underwriting and other expenses | 5(B) | **(58.8)** | (44.9) |
| **Underwriting result** | | **27.1** | 51.2 |
| Investment and other income – policyholders' funds | | **5.1** | 9.0 |
| Investment expenses - policyholders' funds | | **(0.1)** | (0.2) |
| **Insurance profit** | | **32.1** | 60.0 |
| Investment income and other income – shareholder's funds | | **8.1** | 12.8 |
| Investment expenses – shareholder's funds | | **(0.4)** | (0.3) |
| Profit before income tax | | **39.8** | 72.5 |
| Income tax expense | 7(A) | **(19.8)** | (16.5) |
| Profit after income tax | | **20.0** | 56.0 |
| **Other comprehensive income** | | | |
| *Items that may be reclassified to profit or loss* | | | |
| Net movement in foreign currency translation reserve | | **12.8** | 42.8 |
| Other comprehensive income after income tax | | **12.8** | 42.8 |
| Total comprehensive income after income tax | | **32.8** | 98.8 |
| | | | |
| Profit after income tax attributable to: | | | |
| Ordinary equity holder of the company | | **20.0** | 56.0 |
| | | **20.0** | 56.0 |
| | | | |
| Total comprehensive income after tax attributable to: | | | |
| Ordinary equity holder of the company | | **32.8** | 98.8 |
| | | **32.8** | 98.8 |

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

QBE INSURANCE (INTERNATIONAL) LIMITED

## BALANCE SHEET

As at 31 December 2014

| | NOTE | 2014 $M | 2013 $M |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and cash equivalents | 8 | **96.0** | 61.6 |
| Investments | 9 | **676.4** | 715.6 |
| Derivative financial instruments | 10 | **0.6** | 0.8 |
| Trade and other receivables | 11 | **341.8** | 294.6 |
| Deferred insurance costs | 12 | **86.8** | 81.9 |
| Reinsurance and other recoveries on outstanding claims | 19(A) | **285.2** | 498.6 |
| Property, plant and equipment | 13 | **3.5** | 3.8 |
| Deferred tax assets | 14 | **4.2** | 4.6 |
| Investments in controlled entities | 15 | **72.3** | 72.5 |
| Intangible assets | 16 | **21.0** | 18.1 |
| Total assets | | **1,587.8** | 1,752.1 |
| **LIABILITIES** | | | |
| Derivative financial instruments | 10 | **5.2** | 1.7 |
| Trade and other payables | 17 | **183.0** | 213.5 |
| Current tax liabilities | | **6.8** | 9.8 |
| Unearned premium | 18 | **304.6** | 280.7 |
| Outstanding claims | 19(A) | **561.3** | 751.3 |
| Provisions | 20 | **2.5** | 2.3 |
| Deferred tax liabilities | 14 | **13.4** | 11.3 |
| Total liabilities | | **1,076.8** | 1,270.6 |
| Net assets | | **511.0** | 481.5 |
| **EQUITY** | | | |
| Share capital | 21(A) | **321.2** | 230.0 |
| Reserves | 21(D) | **60.0** | 47.2 |
| Retained profits | | **129.8** | 113.1 |
| Shareholder's funds | | **511.0** | 390.3 |
| Mandatory convertible securities | 22 | **-** | 91.2 |
| Total equity | | **511.0** | 481.5 |

The balance sheet should be read in conjunction with the accompanying notes.

## QBE INSURANCE (INTERNATIONAL) LIMITED

### STATEMENT OF CHANGES IN EQUITY
For the year ended 31 December 2014

| 2014 | SHARE CAPITAL $M | MANDATORY CONVERTIBLE SECURITIES $M | RESERVES $M | RETAINED PROFITS $M | TOTAL EQUITY $M |
|---|---|---|---|---|---|
| At 1 January | **230.0** | **91.2** | **47.2** | **113.1** | **481.5** |
| Profit after income tax | - | - | - | **20.0** | **20.0** |
| Movement in foreign currency translation reserve | - | - | **12.8** | - | **12.8** |
| Total comprehensive income | - | - | **12.8** | **20.0** | **32.8** |
| **Transactions with owners in their capacity as owners** | | | | | |
| Mandatory convertible securities | **91.2** | **(91.2)** | - | - | - |
| Dividends paid on ordinary shares | - | - | - | **(3.3)** | **(3.3)** |
| At 31 December | **321.2** | - | **60.0** | **129.8** | **511.0** |

| 2013 | SHARE CAPITAL $M | MANDATORY CONVERTIBLE SECURITIES $M | RESERVES $M | RETAINED PROFITS $M | TOTAL EQUITY $M |
|---|---|---|---|---|---|
| At 1 January | 230.0 | 91.2 | 4.4 | 62.4 | 388.0 |
| Profit after income tax | - | - | - | 56.0 | 56.0 |
| Movement in foreign currency translation reserve | - | - | 42.8 | - | 42.8 |
| Total comprehensive income | - | - | 42.8 | 56.0 | 98.8 |
| **Transactions with owners in their capacity as owners** | | | | | |
| Mandatory convertible securities | - | - | - | - | - |
| Dividends paid on ordinary shares | - | - | - | (5.3) | (5.3) |
| At 31 December | 230.0 | 91.2 | 47.2 | 113.1 | 481.5 |

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

## QBE INSURANCE (INTERNATIONAL) LIMITED

### STATEMENT OF CASH FLOWS
For the year ended 31 December 2014

| | NOTE | 2014 $M | 2013 $M |
|---|---|---|---|
| **OPERATING ACTIVITIES** | | | |
| Premium received | | **548.2** | 403.8 |
| Reinsurance and other recoveries received | | **330.1** | 209.9 |
| Outwards reinsurance paid | | **(185.7)** | (184.4) |
| Claims paid | | **(497.6)** | (337.2) |
| Insurance costs paid | | **(86.7)** | (80.1) |
| Other underwriting costs | | **(85.0)** | (22.3) |
| Interest received | | **11.0** | 7.6 |
| Dividends received | | **-** | 13.0 |
| Retirement benefit paid | | **(0.5)** | (0.3) |
| Other operating income | | **-** | 1.2 |
| Other operating payments | | **(2.8)** | (0.1) |
| Income taxes paid | | **(23.4)** | (6.2) |
| Net receipts from related entities | | **27.3** | 35.3 |
| Net cash flows from operating activities | 8(A) | **34.9** | 40.2 |
| **INVESTING ACTIVITIES** | | | |
| Proceeds on sale of risk assets | | **767.0** | 863.9 |
| Proceeds on disposal of investments in controlled entities | | **-** | 0.8 |
| Payments for purchase of risk assets | | **(708.5)** | (926.3) |
| Payments for purchase of investments in controlled entities | | **-** | (0.6) |
| Payment for purchase of intangibles | | **-** | (1.6) |
| Payments for purchase of plant and equipment | | **(4.2)** | (1.0) |
| Payment for purchase of other financial assets | | **(54.4)** | - |
| Net cash flows from investing activities | | **(0.1)** | (64.8) |
| **FINANCING ACTIVITIES** | | | |
| Dividends paid | | **(3.3)** | (5.3) |
| Net cash flows from financing activities | | **(3.3)** | (5.3) |
| Net movement in cash and cash equivalents | | **31.5** | (29.9) |
| Cash and cash equivalents at the beginning of the financial year | | **61.6** | 82.5 |
| Effect of exchange rate changes | | **2.9** | 9.0 |
| Cash and cash equivalents at the end of the financial year | 8 | **96.0** | 61.6 |

During the year, $91.2 million mandatory convertible securities were converted into ordinary shares of the company. Refer to note 21 and note 22.

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

## NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2014

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

### (A) Basis of preparation

This general purpose financial report has been prepared in accordance with Australian Accounting Standards, and interpretations of the Australian Accounting Standards Board (AASB) and the *Corporation Act 2001*. The company is a for-profit entity for the purpose of preparing the financial statements.

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies are consistent with those of the previous financial year except as set out below.

### (i) New and amended standards adopted by the company

The company mandatorily adopted the following accounting policies which became effective for annual reporting periods commencing on 1 January 2014. These standards have introduced new disclosures but did not materially affect the amounts recognised in the financial statements.

| Title | |
|---|---|
| AASB 1031 | Materiality |
| AASB 2011-4 | Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements |
| AASB 2012-3 | Amendments to Australian Accounting Standards – Offsetting Financial Assets and Financial Liabilities |
| AASB 2013-4 | Amendments to Australian Accounting Standards – Novation of Derivatives and Continuation of Hedge Accounting |
| AASB 2013-9 | Amendments to Australian Accounting Standards – conceptual framework, materiality and financial instruments : Part B |
| Interpretation 21 | Levies |

### (ii) Statement of compliance

The financial report complies with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board and Australian Accounting Standards as issued by the AASB.

### (iii) Historical cost convention

These financial statements have been prepared under the historical cost basis, except for financial assets at fair value through profit and loss, derivative assets and liabilities, investment properties and owner occupied properties.

### (iv) Critical accounting estimates and judgement

The preparation of the financial statements requires the use of certain critical accounting estimates. It also requires management to exercise judgement in the process of applying the company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions or estimates are significant, are disclosed in note 3.

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

### (B) Principles of consolidation

These financial statements are separate financial statements and the company is exempted from preparing consolidated financial statements under AASB 127: Consolidated and Separate Financial Statements. The ultimate parent company, QBE Insurance Group Limited (QBE Group) (incorporated in Australia) produces consolidated financial statements in accordance with IFRS for public use, which can be obtained at www.qbe.com or Level 27, 8-12 Chifley Square, Sydney, NSW 2000 Australia.

Investments in controlled entities are held at cost and a list of controlled entities is set out in note 15. Dividends received from controlled entities are recognised in profit or loss, rather than being deducted from the carrying amount of these investments.

### (C) Premium revenue

Premium comprises amounts charged to policyholders, excluding taxes collected on behalf of third parties. The earned portion of premium received and receivable, including unclosed business, is recognised as revenue. Premium on unclosed business is brought to account based upon the pattern of booking of renewals and new business.

### (D) Unearned premium

Unearned premium is calculated based on the term of the risk and in accordance with the expected pattern of the incidence of risks underwritten, using either the daily pro-rata method or the 24ths method, adjusted where appropriate for seasonality.

At each balance sheet date, the adequacy of the unearned premium liability is assessed on a net of reinsurance basis against the present value of the expected future cash flows relating to potential future claims in respect of the relevant insurance contracts, plus an additional risk margin to reflect the inherent uncertainty of the central estimate. The assessment is carried out at the regional business segment level, being a portfolio of contracts subject to broadly similar risks and which are managed together as a single portfolio. If the present value of the expected future cash flows relating to future claims plus the additional risk margin exceeds the unearned premium liability less related intangible assets and related deferred acquisition costs, then the unearned premium liability is deemed to be deficient. The resulting deficiency is recognised immediately through the profit or loss.

### (E) Outward reinsurance

Premium ceded to reinsurers is recognised as an expense from the attachment date over the period of indemnity of the reinsurance contract in accordance with the expected pattern of the incidence of risk. Accordingly, a portion of outward reinsurance premium is treated as a prepayment at the balance sheet date.

### (F) Claims

The provision for outstanding claims is measured as the central estimate of the present value of expected future claims payments plus a risk margin. The expected future payments include those in relation to claims reported but not yet paid; claims incurred but not reported (IBNR); claims incurred but not enough reported (IBNER); and estimated claims handling costs. Claims expense represents claim payments adjusted for the movement in the outstanding claims liability.

The expected future payments are discounted to present value using a risk-free rate.

A risk margin is applied to the central estimate, net of reinsurance and other recoveries, to reflect the inherent uncertainty in the central estimate.

### (G) Reinsurance and other recoveries

Reinsurance and other recoveries on paid claims, reported claims not yet paid, IBNR and IBNER are recognised as revenue.

Amounts recoverable are assessed in a manner similar to the assessment of outstanding claims. Recoveries are measured as the present value of the expected future receipts, calculated on the same basis as the provision for outstanding claims.

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

### (H) Acquisition costs

Acquisition costs (which include commission costs) are the costs associated with obtaining and recording insurance contracts. Acquisition costs are capitalised when they relate to the acquisition of new business or the renewal of existing business and are referred to as deferred acquisition costs. These costs are amortised on the same basis as the earning pattern of the premium, over the period of the insurance contract to which they relate. At the reporting date, deferred acquisition costs represent the capitalised costs that relate to the unearned premium. Acquisition costs are deferred in recognition of their future benefit and are measured at the lower of cost and recoverable amount.

### (I) Investment income

Interest income is recognised using the effective interest rate method. Dividends are recognised when the right to receive payment is established. Investment income includes realised and unrealised gains or losses on financial assets which are reported on a combined basis as fair value gains or losses on financial assets.

### (J) Taxation

The income tax expense or revenue for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction, adjusted for changes in deferred tax assets and liabilities attributable to temporary differences and unused tax losses.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill or if they arise from the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and is expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

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

Deferred tax assets and liabilities are not recognised for temporary differences between the carrying amount and tax bases of investments in controlled entities where the parent entity is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

The company has implemented the tax consolidation legislation. All entities in the tax-consolidated group continue to account for their own current and deferred tax amounts. These tax amounts are measured as if each entity continues to be a stand-alone tax payer in its own right. Details of the tax funding and tax sharing agreements are included in note 7(B) to the financial statements.

Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, as appropriate.

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

### (K) Insurance profit

Insurance profit is derived by adding investment income on assets backing policyholders' funds to the underwriting result.

### (L) Cash and cash equivalents

Cash and cash equivalents includes cash at bank and on hand and deposits at call which are readily convertible to cash on hand and which are used for operational cash requirements.

### (M) Investments

Investments comprise interest-bearing assets, equities and equity derivative financial instruments. Investments are designated as fair value through profit or loss on initial recognition. They are initially recorded at fair value, being the cost of acquisition excluding transaction costs, and are subsequently remeasured to fair value at each reporting date. The policy of management is to designate a group of financial assets or financial liabilities as fair value through profit or loss when that group is both managed and its performance evaluated on a fair value basis for both internal and external reporting in accordance with the company's documented investment strategy.

For securities traded in an active market, the fair value is determined by reference to quoted market prices. Where quoted market prices in active markets are not available, fair value is determined using valuation techniques incorporating inputs that are observable for the asset. In the absence of quoted market prices in active markets and observable market inputs, valuation techniques or models which are based on unobservable inputs may be used.

All purchases and sales of investments that require delivery of the asset within the time frame established by regulation or market convention ("regular way" transactions) are recognised at trade date, being the date on which the company commits to buy or sell the asset. Investments are derecognised when the right to receive future cash flows from the asset has expired or has been transferred and the company has transferred substantially all the risks and rewards of ownership.

### (N) Derivative financial instruments

The company is subject to currency, interest rate, price, credit and liquidity risks. Derivative financial instruments (derivatives) may be used to manage these risks.

Derivatives are initially recognised at fair value, being generally the transaction price on the date a derivative contract is entered into, and are subsequently remeasured to their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and the nature of the item being hedged. Derivatives which are not part of a hedging relationship are valued at fair value through profit or loss.

For derivatives traded in an active market, the fair value of derivatives presented as assets is determined by reference to published closing bid price quotations and the fair value of derivatives presented as liabilities is determined by reference to published closing ask price quotations. For derivatives that are not traded or which are traded in a market that is not sufficiently active, fair value is determined using generally accepted valuation techniques.

### (O) Trade and other receivables

Trade and other receivables are subsequently measured at amortised cost less any impairment amount. A provision for impairment is established when there is objective evidence that the company will not be able to collect all amounts due according to the original term of the receivable. Any increase or decrease in the provision for impairment is recognised in profit or loss within underwriting expenses. When a receivable is uncollectible, it is written off against the provision for impairment account. Subsequent recoveries of amounts previously written off are credited against underwriting expenses in profit or loss.

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

### (P) Property, plant and equipment

All plant and equipment is stated at historical cost less accumulated depreciation and impairment.

Leasehold improvements, office equipment (including IT hardware and software), fixtures and fittings and motor vehicles are depreciated using the straight line method over the estimated useful life to the company of each class of asset. Estimated useful lives are between 3 and 10 years for all classes.

An asset's carrying amount is written down to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Refer note 1(R).

### (Q) Intangible assets

#### (i) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the company's share of the net identifiable assets acquired. For the purpose of impairment testing, goodwill is allocated to cash generating units, or groups of cash generating units, that are expected to benefit from the synergies of the business combination. For this purpose, the cash generating unit, or group of units, is determined principally by reference to how goodwill is monitored by management. The recoverability of the goodwill is tested annually for impairment or more frequently when changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised as the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

#### (ii) Identifiable intangible assets

Identifiable intangible assets are measured at cost. Those with a finite useful life are amortised over their estimated useful life in accordance with the pattern of expected benefit. Identifiable intangible assets with an indefinite useful life are not subject to amortisation but are tested for impairment annually or more often if there is an indication of impairment. Identifiable intangible assets with a finite useful life are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

### (R) Impairment of assets

Assets that have an indefinite useful life are tested annually for impairment or more frequently when changes in circumstances indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised as the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped in cash generating units which are the lowest levels for which there are separately identifiable cash flows. Impairment testing of goodwill is explained in note 1(Q)(i).

### (S) Trade and other payables

Trade and other payables are measured at cost and are settled under standard terms and conditions. Inter-company payables are measured at cost and are repayable on demand.

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

### (T) Foreign currency

#### (i) Functional and presentation currency

The company's financial statements are presented in Australian dollars, being the functional and presentation currency of the company.

#### (ii) Translation of foreign currency transactions and balances

Items included in the financial statements of overseas operations are measured using the currency of the primary economic environment in which the entity operates (the functional currency). Foreign currency transactions are translated into functional currencies at the spot rates of exchange applicable at the dates of the transactions. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated at the rates of exchange prevailing at that date. Resulting exchange gains and losses are included in profit or loss.

#### (iii) Translation of overseas operations

The results and balance sheets of all overseas operations that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- income, expenses and other current period movements in comprehensive income are translated at cumulative average rates of exchange; and

- other balance sheet items are translated at the closing balance date rates of exchange.

Exchange differences arising from the translation of the net investment in overseas operations, are recognised as other comprehensive income and taken to shareholder's equity. When an overseas operation is sold, these exchange differences are reversed out of comprehensive income and recognised in profit or loss as part of the gain or loss on sale.

#### (iv) Hedging transactions

Derivatives may be used to hedge the foreign exchange risk relating to certain transactions.

#### (v) Exchange rates

The principal exchange rates used in preparation of the financial statement were:

| | 2014 | | 2013 | |
|---|---|---|---|---|
| | PROFIT AND LOSS | BALANCE SHEET | PROFIT AND LOSS | BALANCE SHEET |
| NZ$/A$ | **0.919** | **0.955** | 0.850 | 0.921 |
| SGD/A$ | **0.878** | **0.925** | 0.833 | 0.887 |
| €/A$ | **1.476** | **1.482** | 1.385 | 1.541 |

### (U) Equity

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

### (V) Dividends

Provision is made for dividends which are declared, being appropriately authorised and no longer at the discretion of the company, on or before the end of the financial year but not distributed at the balance sheet date.

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

### (X) Employee benefits

#### (i) Superannuation

The company participates in a number of superannuation plans and contributes to these plans in accordance with plan rules and actuarial recommendations, which are designed to ensure that each plan's funding provides sufficient assets to meet its liabilities.

**Defined contribution plans**

Defined contribution plans are post-employment benefit plans under which an entity pays a fixed contribution into a fund during the course of employment and has no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. For defined contribution plans, contributions are expensed as incurred.

#### (ii) Share based payment

The employees of the company participate in an equity settled, share based compensation plan of QBE Insurance Group Limited. For all other options and conditional rights, the fair value of the employee services received in exchange for the grant of those instruments is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the instruments granted, excluding the impact of any non-market vesting conditions. The fair value at grant date of the options and conditional rights is calculated using a binomial model. The fair value of each instrument is expensed evenly over the period between grant and vesting dates. Non-market vesting conditions are included in assumptions about the number of instruments that are expected to become exercisable.

At each balance sheet date, the company revises its estimates of the number of options that are expected to become exercisable due to the achievement of vesting conditions. The company recognises the impact of the revision of original estimates, if any, in profit or loss with a corresponding adjustment to equity.

#### (iii) Profit sharing and bonus plans

The company recognises a liability and an expense for bonuses and profit sharing based on a formula that takes into consideration the profit attributable to the company's shareholders.

#### (iv) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date or when an employee accepts voluntary redundancy in exchange for these benefits. The company recognises termination benefits when it has demonstrably committed to either:

- terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or
- providing termination benefits as a result of an offer made to encourage voluntary redundancy.

#### (v) Long service leave

The provision for long service leave is measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Benefits falling due more than 12 months after the balance sheet date are discounted to present value.

### (Y) Leases

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

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

### (Z) Goods and services tax (GST)

Revenues, expenses and assets (except receivables) are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Taxation Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of expense. Receivables and payables in the balance sheet are shown inclusive of GST.

The net amount of GST recoverable from, or payable to, the Australian Taxation Office is included with other receivables or payables in the balance sheet.

Cash flows are presented on a gross basis. The GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to the taxation authority, are presented as operating cash flow.

QBE Insurance (International) Limited is part of a GST group headed by QBE Management Services Pty Limited, a related entity.

### (AA) Rounding of amounts

The company is of a kind referred to in the ASIC class order 98/100 dated 10 July 1998 (as amended by class order 04/667 dated 15 July 2004) relating to the "rounding off" of amounts in the financial statements. Amounts in the financial statements have been rounded off in the financial statements to the nearest one hundred thousand dollars or, in certain cases, to the nearest thousand dollars in accordance with the class order.

### (AB) Comparatives

Where appropriate, prior period comparatives have been reclassified in this financial report to ensure comparability in the current reporting period. The reclassification was necessary to provide the readers of the financial report with a greater understanding of the company's financial statements.

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

### (X) Employee benefits
### (i) Superannuation
The company participates in a number of superannuation plans and contributes to these plans in accordance with plan rules and actuarial recommendations, which are designed to ensure that each plan's funding provides sufficient assets to meet its liabilities.

**Defined contribution plans**
Defined contribution plans are post-employment benefit plans under which an entity pays a fixed contribution into a fund during the course of employment and has no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. For defined contribution plans, contributions are expensed as incurred.

### (ii) Share based payment
The employees of the company participate in an equity settled, share based compensation plan of QBE Insurance Group Limited. For all other options and conditional rights, the fair value of the employee services received in exchange for the grant of those instruments is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the instruments granted, excluding the impact of any non-market vesting conditions. The fair value at grant date of the options and conditional rights is calculated using a binomial model. The fair value of each instrument is expensed evenly over the period between grant and vesting dates. Non-market vesting conditions are included in assumptions about the number of instruments that are expected to become exercisable.

At each balance sheet date, the company revises its estimates of the number of options that are expected to become exercisable due to the achievement of vesting conditions. The company recognises the impact of the revision of original estimates, if any, in profit or loss with a corresponding adjustment to equity.

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The company recognises a liability and an expense for bonuses and profit sharing based on a formula that takes into consideration the profit attributable to the company's shareholders.

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Termination benefits are payable when employment is terminated before the normal retirement date or when an employee accepts voluntary redundancy in exchange for these benefits. The company recognises termination benefits when it has demonstrably committed to either:

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The provision for long service leave is measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Benefits falling due more than 12 months after the balance sheet date are discounted to present value.

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

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

### (Z) Goods and services tax (GST)

Revenues, expenses and assets (except receivables) are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Taxation Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of expense. Receivables and payables in the balance sheet are shown inclusive of GST.

The net amount of GST recoverable from, or payable to, the Australian Taxation Office is included with other receivables or payables in the balance sheet.

Cash flows are presented on a gross basis. The GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to the taxation authority, are presented as operating cash flow.

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### (AA) Rounding of amounts

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### (AB) Comparatives

Where appropriate, prior period comparatives have been reclassified in this financial report to ensure comparability in the current reporting period. The reclassification was necessary to provide the readers of the financial report with a greater understanding of the company's financial statements.

## 2. NEW ACCOUNTING STANDARDS AND AMENDMENTS

| TITLE | | OPERATIVE DATE |
|---|---|---|
| AASB 9 | Financial Instruments | 1 January 2018 |
| AASB 9 (revised) | Financial Instruments | 1 January 2018 |
| 2009-11 | Amendments to Australian Accounting Standards arising from AASB 9 | 1 January 2018 |
| 2010-7 | Amendments to Australian Accounting Standards arising from AASB 9 (December 2010) | 1 January 2018 |
| 2013-9 | Amendments to Australian Accounting Standards – Conceptual Framework, materiality and financial instruments: Part C | 1 January 2015 |
| 2014-1 | Amendments to Australian Accounting Standards (Part A – Annual Improvements) | 1 January 2015 |
| 2014-1 | Amendments to Australian Accounting Standards (Part E – Financial Instruments) | 1 January 2015 |
| 2014-4 | Amendments to Australian Accounting Standards – Clarification of Acceptable Methods of Depreciation and Amortisation | 1 January 2016 |
| IFRS 15 | Revenue from Contracts with Customers | 1 January 2017 |
| Various | Annual Improvements to IFRSs 2012-2014 cycle | 1 January 2016 |

The Australian accounting standards and amendments detailed in the table above are not mandatory for the company until the operative dates stated; however, early adoption is permitted.

The company will apply the standards and amendments detailed above for the reporting periods beginning on the operative dates set out above. An initial assessment of the financial impact of the standards and amendments has been undertaken and they are not expected to have a material impact on the company's financial statements or accounting policies. QBE Group is in the process of assessing the potential impact of AASB 9.

## 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The company is an international general insurance entity, underwriting most major commercial and personal lines classes of business through operations in 8 countries. The analysis of the company's gross written premium and net earned premium from insurance and reinsurance business is shown in note 5(A). The head office function is located in Australia and exists to support the activities of overseas operations.

In view of the geographic and product diversity, the company has developed a strong, centralised risk management and policy framework, designed to ensure consistency of approach across a number of operational activities, subject to the specific requirements of local markets, legislation and regulation. Such operational activities include underwriting, claims management, actuarial assessment of the claims provisions and investment management. In addition, assessment of the net outstanding claims provision set at a regional level is subject to detailed head office review. The probability of adequacy derived from the company's insurance liabilities is measured by the Appointed Actuary.

Given the centralised approach to many of company's activities and the product and geographic diversification, sensitivity analyses in respect of critical accounting estimates and judgments are presented at the company level in order to provide information and analysis which is meaningful, relevant, reliable and comparable year on year. Sensitivity disclosure at business segment or product level would not provide a meaningful overview given the complex interrelationships between the variables underpinning the company's operations. The company makes estimates and judgments in respect of the reported amounts of certain assets and liabilities. These estimates and judgments are determined by qualified and experienced employees with reference to historical data and reasoned expectations of future events and are continually updated. The key areas in which critical estimates and judgments are applied are described as follows:

### (A) Outstanding claims provision

The company's net outstanding claims provision comprises:

- the gross central estimate of expected future claims payments;
- amounts recoverable from reinsurers based on the gross central estimate;
- a reduction to reflect the discount to present value using risk-free rates of return to reflect the time value of money; and
- a risk margin that reflects the inherent uncertainty in the net discounted central estimate.

A net discounted central estimate is intended to represent the mean of the distribution of the expected future cash flows. As the company requires a higher probability that estimates will be adequate over time, a risk margin is added to the net discounted central estimate to determine the outstanding claims provision.

### (i) Central estimate

The provision for expected future payments includes those in relation to claims reported but not yet paid; claims incurred but not reported (IBNR); claims incurred but not enough reported (IBNER); and estimated claims handling costs, being the direct expenses incurred in the settlement of claims.

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 claims is generally available. Liability and other long tail classes of business, where claims settlement may not happen for many years after the event giving rise to the claim, typically display greater variability between initial estimates and final settlement due to delays in reporting claims, uncertainty in respect of court awards and future claims inflation. Claims in respect of property and other short tail classes are typically reported and settled sooner after the claim event, giving rise to more certainty. The estimation techniques and assumptions used in determining the central estimate are described below.

The company's process for establishing the central estimate involves extensive consultation with internal and external actuaries, claims managers, underwriters and other senior management. This process includes half yearly internal claims provisioning committee meetings attended by the senior management and the Appointed Actuary and detailed review by external actuaries at least annually. The risk management procedures related to the actuarial function are explained further in note 4.

## 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

### (A) Outstanding claims provision (continued)

#### (i) Central estimate (continued)

The determination of the amounts that the company will ultimately pay for claims arising under insurance and reinsurance contracts involves a number of critical assumptions. Some of the uncertainties impacting these assumptions are as follows:

- changes in patterns of claims incidence, reporting and payment;
- volatility in the estimation of future costs for long tail insurance classes due to the longer period of time that elapses before a definitive determination of the ultimate claims cost can be made;
- incidence of catastrophic events close to the balance sheet date;
- changes in the legal environment, including the interpretation of liability laws and the quantum of damages; and
- social and economic trends, for example price and wage inflation and interest rates.

The potential impact of changes in key assumptions used in the determination of the central estimate and the probability of adequacy of the central estimate on the company's profit or loss are summarised in note 3(A)(v).

Central estimates for each class of business are determined by reference to a variety of estimation techniques, generally based on a statistical analysis of historical experience which assumes an underlying pattern of claims development and payment. The final selected central estimates are based on a judgemental consideration of the results of each method and qualitative information, for example, the class of business, the maturity of the portfolio and the expected term to settlement of the class. Projections are based on both historical experience and external benchmarks where relevant.

Central estimates are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts recoverable from reinsurers based on the gross central estimate.

The net central estimate is discounted at risk-free rates of return to reflect the time value of money. Details of the key assumptions applied in the discounting process are summarised in note 3(A)(iv).

#### (ii) Assets arising from contracts with reinsurers

Assets arising from contracts with the company's reinsurers are determined using the same methods described above. In addition, the recoverability of these assets is assessed at each balance sheet date to ensure that the balances properly reflect the amounts that will ultimately be received, taking into account counterparty credit risk and the contractual terms of the reinsurance contract. Counterparty and credit risk in relation to reinsurance assets is considered in note 4(C)(ii).

#### (iii) Risk margin

Risk margins are determined by management and are held to mitigate the potential for uncertainty in the central estimate. The determination of the appropriate level of risk margin takes into account similar factors to those used to determine the central estimate, such as:

- mix of business, in particular the mix of short tail and long tail business and the overall weighted average term to settlement;
- prior accident year claims development; and
- the level of uncertainty in the net discounted central estimate due to actuarial estimation, data quality issues, variability of key discount and inflation assumptions and possible economic legislative changes.

The variability by class of business uses techniques similar to those used in determining the central estimate. These techniques determine a range of possible outcomes of ultimate payments and assign a likelihood to outcomes at different levels. These techniques use standard statistical distributions, and the measure of variability is referred to as the coefficient of variation. The potential impact of changes in the coefficient of variation assumptions on the company's profit or loss is summarised in note 3(A)(v).

## 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

### (A) Outstanding claims provision (continued)

### (iii) Risk margin (continued)

The appropriate risk margin for two or more classes of business combined is likely to be less than the sum of the risk margins for the individual classes. This reflects the benefit of diversification in general insurance. The statistical measure used to determine diversification is called the correlation. The higher the correlation between two classes of business, the more likely it is that a negative outcome in one class will correspond to a negative outcome in the other class. For example, high correlation exists between classes of business affected by court cases involving bodily injury claims such as motor third party liability, workers' compensation and public liability.

The risk margin for the company is determined by analysing the variability of each class of business and the correlation between classes of business and divisions. Correlations are determined for aggregations of classes of business, where appropriate, at the divisional level. Whilst there are estimation techniques for determining correlations, they are difficult to apply. The correlations adopted by the company are normally derived from industry analysis, the company's historical experience and the judgement of experienced and qualified actuaries.

The probability of adequacy is a statistical measure of the relative adequacy of the outstanding claims provision and is derived from the comparison of the risk margin with the net discounted central estimate. Using a range of outcomes, it allows a determination of the probability of adequacy represented by a risk margin. For example, a 90% probability of adequacy indicates that the outstanding claims provision is expected to be adequate nine times in 10. The probability of adequacy is not of itself an accounting policy or estimate as defined by AASB 108: Accounting Policies, Changes in Accounting Estimates and Errors. The appropriate level of risk margin is not determined by reference to a fixed probability of adequacy.

### (iv) Financial assumptions used to determine the outstanding claims provision

**Discount rates**

AASB 1023: General Insurance Contracts (AASB 1023) requires that the outstanding claims provision shall be discounted for the time value of money using risk-free rates that are based on current observable, objective rates that relate to the nature, structure and terms of the future obligations. The standard also states that government bond rates may be an appropriate starting point in determining a risk-free rate. The company generally uses currency specific risk-free rates to discount the outstanding claims provision.

The weighted average risk-free rates used to discount the outstanding claims provision are summarised below.

| | | **2014 %** | | **2013 %** |
|---|---|---|---|---|
| | **SUCCEEDING YEAR** | **SUBSEQUENT YEARS** | **SUCCEEDING YEAR** | **SUBSEQUENT YEARS** |
| New Zealand | **3.54** | **3.56-3.76** | 2.90 | 3.29-4.70 |
| Asia | **0.06-0.77** | **0.36-2.36** | 0.08-0.30 | 0.23-2.61 |
| Pacific | **-0.07-2.4** | **-0.11-2.78** | 0.05-2.45 | 0.16-4.30 |

## 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

### (A) Outstanding claims provision (continued)

### (iv) Financial assumptions used to determine the outstanding claims provision (continued)

**Weighted average term to settlement**

The relevant discount rate is applied to the anticipated cash flow profile of the central estimate, including related reinsurance recoveries, determined by reference to a combination of historical analysis and current expectations of when claims and recoveries will be settled. Details of the weighted average term to settlement of the company's claims provision, analysed by region and currency, are summarised below.

| | 2014 YEARS | | | | 2013 YEARS | | | |
|---|---|---|---|---|---|---|---|---|
| | NZD | SGD | Other | Total | NZD | SGD | Other | Total |
| Asia | - | **1.19** | **1.11** | **1.19** | - | 1.21 | 1.07 | 1.21 |
| New Zealand | **1.47** | - | - | **1.47** | 1.65 | - | - | 1.65 |
| Pacific | - | - | **2.31** | **2.31** | - | - | 2.23 | 2.23 |

### (v) Impact of changes in key variables on the outstanding claims provision

The impact of changes in key variables used in the calculation of the outstanding claims provision is summarised in the table below. Each change has been calculated in isolation from the other changes and each change shows the after tax impact on profit assuming that there is no change to any of the other variables. In practice, this is considered unlikely to occur as, for example, an increase in interest rates is normally accompanied by an increase in the rate of inflation. As can be seen from the table below, the impact of a change in discount rates is largely offset by the impact of a change in the rate of inflation.

The sensitivities below assume that all changes directly impact profit after tax. In practice, however, it is likely that if the central estimate was to increase by 5%, at least part of the increase would result in a decrease in the probability of adequacy. Likewise, if the coefficient of variation were to increase by 1%, it is likely that the probability of adequacy would reduce from its current level and that the change would therefore impact the amount of risk margins held rather than net profit after income tax or equity.

The impact of a change in interest rates on profit after tax due to market value movement on fixed interest securities is shown in note 4(D)(ii).

## 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

### (A) Outstanding claims provision (continued)
### (v) Impact of changes in key variables on the outstanding claims provision (continued)

| | SENSITIVITY<br>% | PROFIT (LOSS)[1]<br>2014<br>$M | <br>2013<br>$M |
|---|---|---|---|
| Central estimate | +5.0 | **(9.6)** | (8.8) |
| | -5.0 | **9.6** | 8.8 |
| Risk margin | +5.0 | **(1.3)** | (1.3) |
| | -5.0 | **1.3** | 1.3 |
| Inflation rate | +0.5 | **(1.4)** | (1.3) |
| | -0.5 | **1.4** | 1.3 |
| Discount rate | +0.5 | **1.4** | 1.3 |
| | -0.5 | **(1.4)** | (1.4) |
| Coefficient of variation | +1.0 | **(2.6)** | (2.5) |
| | -1.0 | **2.6** | 2.5 |
| Probability of adequacy | +1.0 | **(1.5)** | (1.6) |
| | -1.0 | **1.3** | 1.4 |
| Weighted average term to settlement years | +10.0 | **(0.5)** | (0.8) |
| | -10.0 | **0.5** | 0.8 |

[1] Net of tax at the company's prima facie rate of 30%

### (B) Liability adequacy test
At each balance date, the adequacy of the unearned premium liability is assessed on a net of reinsurance basis against the present value of the expected future cash flows relating to potential future claims, plus a risk margin to reflect the inherent uncertainty of the central estimate (refer note 18(D)). Future claims are those claims expected to arise from claims events occurring after the balance sheet date. The assessment is carried out using the same methods described in note 3(A) above.

AASB 1023 requires that this test be carried out at the level of a "portfolio of contracts that are subject to broadly similar risks and are managed together in a single portfolio". As AASB 1023 does not explicitly define "broadly similar risks" or "managed together as a single portfolio", the company has interpreted these terms in a way that reflects our day to day approach to managing the various risks to which the company is exposed that is at the regional segment level. The company's operating segments are structured in a way that facilitates the efficient and effective management of our insurance businesses, and recognises that these businesses are subject to broadly similar risks such as the interest and inflation rate environment; pricing risk; credit risk; social and political risk such as unemployment and social unrest; and common insurance risks such as exposure to weather-related or other natural catastrophe risks.

### (C) Intangible assets
Goodwill and identifiable intangibles assets with an indefinite useful life are tested annually for impairment, or more frequently when changes in circumstances indicate that the carrying amount may not be recoverable. Identifiable intangibles assets subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The impairment review is based on the net present value of estimated future cash flows of the relevant asset, the relevant cash generating unit or relevant group of cash generating units. For details of key assumptions and estimates used, refer to note 16(B).

## 4. RISK MANAGEMENT

QBE Group's risk management policy, strategy and framework are embedded in the head office and in each of the divisional operations, ensuring a consistent approach to managing risk across the organisation. The board annually approves a comprehensive risk management strategy (RMS), including a risk appetite statement and a reinsurance management strategy (REMS), both of which are lodged with the Australian Prudential Regulation Authority (APRA).

As a member of the QBE Group, the company has adopted the risk management policy of QBE Group where applicable. The company's risk management policy objectives are to:

- achieve competitive advantage through better understanding the risk environment in which QBE operates;
- optimise risk and more effectively allocate capital and resources by assessing the balance of risk and reward; and
- avoid unwelcome surprises by reducing uncertainty and volatility.

It is QBE Group's policy to adopt a rigorous approach to managing risk throughout the company. Risk management is a continuous process and an integral part of quality business management. QBE Group's approach is to integrate risk management into the broader management processes of the organisation. It is QBE Group's philosophy to ensure that risk management remains embedded in the business and that the risk makers or risk takers are themselves the risk managers. Specifically, the management of risk must occur at each point in the business management cycle.

Risk management is a key part of our governance structure and our strategic and business planning. It underpins the setting of limits and authorities and it is embedded in the monitoring and evaluation of performance. This holistic approach to risk management allows all of the company's risks to which the company is exposed to be managed in an integrated manner.

QBE Group's global risk management framework sets out the approach to managing key risks and meeting strategic objectives whilst taking into account the creation of value for our shareholders. The framework is made up of complementary elements that are embedded throughout the business management cycle and culture. Key aspects include: governance, risk appetite, delegated authorities, risk policies, measurement and modelling, risk and control self assessment, risk treatment, optimisation and ongoing improvement through action plans, risk and performance monitoring.

A fundamental part of the company's overall risk management strategy is the effective governance and management of the risks that impact the amount, timing and uncertainty of cash flows from insurance contracts. The operating activities of the company expose it to risks such as market risk, credit risk and liquidity risk and operational risk. The company's risk management framework recognises the unpredictability of financial markets and seeks to manage potential adverse effects on its financial performance. The company has established internal controls to manage risk in the key areas of exposure relevant to its business.

QBE Group's risk profile is described under the following broad risk categories:

- Strategic risk
- Insurance risk
- Credit risk
- Market risk
- Liquidity risk
- Operational risk
- Group risk.

## 4. RISK MANAGEMENT (CONTINUED)

Each of these is described more fully in sections (A) to (G) below.

### (A) Strategic risk

Strategic risk refers to the current and prospective impact on earnings and or capital arising from strategic business decisions, implementation of decisions and responsiveness to external change. This includes risks associated with business strategy and change, investment strategy and corporate governance. Of particular relevance is capital management risk.

### (i) Acquisition risk

Acquisition risks are principally managed by QBE Group's control over the selection of potential acquisitions, due diligence, negotiation of warranties and indemnities and subsequent integration processes. QBE Group has experienced due diligence teams in each operating divisions and has documented minimum requirements for carrying out due diligence.

### (ii) Capital management risk

Australian and overseas controlled entities are subject to extensive prudential and other forms of regulation in the jurisdictions in which they conduct business. Prudential regulation is generally designed to protect policyholders. Regulation covers a number of areas including solvency, change in control and capital movement limitations. The regulatory environment in Australia and overseas continues to evolve in response to economic, political and industry developments. QBE Group works closely with regulators and monitors regulatory developments across its global operations to assess their potential impact on its ability to meet solvency and other requirements. Refer to note 21(E).

### (B) Insurance risk

Insurance risk is the risk of fluctuations in the timing, frequency and severity of insured events and claims settlements, relative to the expectations. This includes underwriting, insurance concentrations and reserving and reinsurance. The risks inherent in any single insurance contract are the possibility of the insured event occurring and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, these risks are random and unpredictable. In relation to the pricing of individual insurance contracts and the determination of the level of the outstanding claims provision in relation to a portfolio of insurance contracts, the principal risk is that the ultimate claims payments will exceed the carrying amount of the provision established.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability around the expected outcome will be. In addition, a more diversified insurance and reinsurance company is less likely to be affected by a change in any one specific portfolio. The company has developed its underwriting strategy to diversify the type of insurance risks accepted and, within each of these categories, to achieve a sufficiently large population of risks to reduce the variability of the expected outcome.

QBE Group has established the following protocols to manage its insurance risk across the underwriting, claims, and outwards reinsurance.

## 4. RISK MANAGEMENT (CONTINUED)

### (B) Insurance risk (continued)
### (i) Underwriting risks
**Selection and pricing of risks**
Underwriting authority is delegated to experienced underwriters for the forthcoming year following a detailed retrospective and prospective analysis of each class of business as part of the company's annual business planning process. Delegated authorities reflect the level of risk which QBE Group is prepared to take. The authorities include reference to some combination of:

- return on risk adjusted equity;
- gross written premium;
- premium per contract;
- sum insured per contract;
- aggregate exposures per zone;
- probable maximum loss and realistic disaster scenarios (RDSs);
- levels and quality of reinsurance protection;
- geographic exposures; and/or
- classes of business and types of product that may be written.

Limits in respect of each of the above are set at a portfolio, divisional and company-wide level and are included within business plans for individual classes of business.
Insurance and reinsurance policies are written in accordance with local management practices and regulations within each jurisdiction taking into account the company's risk appetite and underwriting standards. Non-standard and long-term policies may only be written if expressly included in the delegated authorities. No individual long-term or non-standard policy is material to the company.

Pricing of risks is controlled by the use of in-house pricing models relevant to specific portfolios and the markets in which company operates. Experienced underwriters and actuaries maintain historical pricing and claims analysis for each portfolio and this is combined with a detailed knowledge of the current developments in the respective markets and classes of business.

**Concentration risk**
The company's exposure to concentrations of insurance risk is mitigated by a portfolio diversified across 8 countries and hundreds of classes of business. Product diversification is achieved through a strategy of developing strong underwriting skills in a wide variety of classes of business. A combination of core and speciality products under the control of employees skilled in underwriting such products allows QBE to lead underwrite in many of the markets in which it operates.
The table below demonstrates the diversity of the company's operations.

| GROSS EARNED PREMIUM | 2014 $M | 2013 $M |
|---|---|---|
| Property | **190.7** | 169.2 |
| Marine, energy and aviation | **82.2** | 83.7 |
| Public/product liability | **67.9** | 60.0 |
| Professional indemnity | **44.0** | 39.6 |
| Motor and motor casualty | **50.2** | 38.4 |
| Accident and health | **31.7** | 37.2 |
| Financial and credit | **20.0** | 21.2 |
| Engineering | **27.7** | 7.4 |
| Workers' compensation | **23.8** | 19.3 |
| Other | **0.5** | 0.9 |
| | **538.7** | 476.9 |

## 4. RISK MANAGEMENT (CONTINUED)

### (B) Insurance risk (continued)

#### (i) Underwriting risks (continued)

The company has potential exposure to catastrophe losses that may impact more than one operating division. Each year, the company sets its tolerance to concentration risk. Realistic disaster scenarios (RDSs), using industry standard and QBE Group determined probable maximum losses and various catastrophe models are calculated for each portfolio as part of the business planning process. These RDSs are aggregated across all portfolios and divisions to determine the company's maximum event retention (MER) which is the estimated maximum net claim from a one in 250 year natural catastrophes event. The company also assesses aggregated regional exposure levels. The concentrations must be less than the company's concentration risk limits, otherwise steps such as the purchase of additional reinsurance are taken to limit the exposure.

#### (ii) Claims management and claims estimation risks

The company's approach to determining the outstanding claims provision and the related sensitivities are set out in note 3. The company seeks to ensure the adequacy of its outstanding claims provision by reference to the following controls:

- experienced claims managers work with underwriters on coverage issues and operate within the levels of authority delegated to them in respect of the settlement of claims;
- processes exist to ensure that all claims advices are captured and updated on a timely basis with a realistic assessment of the ultimate claims cost;
- initial IBNR estimates are set by experienced internal actuaries in conjunction with the local product managers and underwriters for each class of business in each business unit. The valuation of the central estimate is primarily performed by actuaries who are not involved in the pricing function and who therefore provide an independent assessment;
- the determination of the risk margin is performed by senior management and the board with input from the Appointed Actuary;
- the aggregate outstanding claims provision for each controlled entity is assessed in a series of internal claims review meetings which are attended by senior management and the Appointed Actuary in order to ensure consistency of provisioning practices across all countries; and
- all the company's central estimate is reviewed by external actuaries at least annually.

Despite the rigour involved in the establishment and review of the outstanding claims provision, the provision is subject to significant uncertainty for the reasons provided in note 3.

#### (iii) Outwards reinsurance

The company limits its exposure to an individual catastrophe or an accumulation of claims by reinsuring a portion of risks underwritten. In this way, the company can control exposure to insurance losses, reduce volatility of reported results and protect capital.

Effective governance and management of reinsurance protection is a fundamental part of the company's risk management practices. QBE Group has in place systems, internal controls and processes to ensure that its reinsurance arrangements are appropriate to enable the company to meet its obligations to policyholders, whilst protecting the wealth of its shareholders. This framework is outlined in the company's REMS which states that the company's maximum risk tolerance for an individual natural catastrophe at a 1 in 250 year probability is 8.25% of budgeted net earned premium.

The senior authority for purchasing reinsurance is the chief executive officer and/or the chief reinsurance officer, who generally act after consultation with and based on recommendations from the Group reinsurance forum (GRF).

The GRF determines the company's exposure to and appetite for catastrophes and individual risks net of reinsurance as part of the business planning process. The resulting strategy is recommended to the chief executive officer (previously the chief executive officer and/or the chief executive officer of global underwriting operations), who provides the final approval on the reinsurance purchasing strategy. The GRF monitors and reports on placement of reinsurance and oversees the relevant committees that monitor concentration risk, reinsurance credit risk and commutation risks, as well as the processes for evaluating the effectiveness of reinsurances purchased. Reinsurance counterparty credit risk is considered in note 4(C)(ii).

## 4. RISK MANAGEMENT (CONTINUED)

### (B) Insurance risk (continued)
### (iii) Outwards reinsurance (continued)
The company purchases significant levels of external reinsurance protection to ensure that the company's net retention is aligned with its risk tolerance. In addition, QBE Group retains a portion of its reinsurance placements through its captive, Equator Reinsurances Limited (Equator Re). Reinsurance cover provided by Equator Re gives reinsurance protection to the company enabling QBE Group to more effectively manage capital.

### (C) Credit risk
Credit risk is the risk of default by borrowers and transactional counterparties as well as the loss of value of assets due to deterioration in credit quality. Exposure to credit risk results from financial transactions with securities issuers, debtors, borrowers, brokers, policyholders, reinsurers and guarantors.

The company's credit risk arises mainly from investment and reinsurance protection activities. The following policies and procedures are in place to mitigate the company's exposure to credit risk:

- A QBE Group-wide investment credit risk policy is in place which defines what constitutes credit risk for QBE group and establishes tolerance levels. Compliance with the policy is monitored and exposures and breaches are reported to the QBE Group investment committee.
- Net exposure limits are set for each counterparty or group of counterparties in relation to investments, cash deposits and forward foreign exchange exposures. The policy also sets out minimum credit ratings for investments.
- QBE Group has strict guidelines covering the limits and terms of net open derivative positions and the counterparties with which the company may transact. The company does not expect any investment counterparties to fail to meet their obligations given their strong credit ratings and therefore does not require collateral or other security to support derivatives. The company only uses derivatives in highly liquid markets.
- Credit risk in respect of premium debtors and reinsurance receivables is actively monitored. Strict controls are maintained over counterparty exposures. The provision for impairment is formally assessed by management at least four times a year.

### (i) Investment counterparty credit risk
The following table provides information regarding the company's aggregate credit risk exposure at the balance sheet date in respect of the major classes of financial assets. Trade and other receivables are excluded from this analysis on the basis that they comprise of smaller credit risk items which generally cannot be rated and are not individually material. The analysis classifies the assets according to Moody's counterparty credit ratings. Aaa is the highest possible rating. Rated assets falling outside the range of Aaa to Baa are classified as speculative grade.

| | CREDIT RATING | | | | | | |
|---|---|---|---|---|---|---|---|
| | Aaa | Aa | A | Baa | SPECULATIVE GRADE | NOT RATED | TOTAL |
| | $M | $M | $M | $M | $M | $M | $M |
| **At 31 December 2014** | | | | | | | |
| Cash and cash equivalents | - | **27.4** | **65.9** | - | - | **2.7** | **96.0** |
| Interest-bearing investments | **226.8** | **377.9** | **69.7** | - | - | **2.0** | **676.4** |
| Derivative financial instruments | - | **0.5** | **0.1** | - | - | - | **0.6** |
| **At 31 December 2013** | | | | | | | |
| Cash and cash equivalents | 0.2 | 19.9 | 37.5 | - | - | 4.0 | 61.6 |
| Interest-bearing investments | 274.0 | 415.1 | 25.3 | - | - | 1.2 | 715.6 |
| Derivative financial instruments | - | 0.2 | 0.6 | - | - | - | 0.8 |

## 4. RISK MANAGEMENT (CONTINUED)
### (C) Credit risk (continued)
### (i) Investment counterparty credit risk (continued)
The following table provides information regarding the ageing of the company's financial assets that are past due but not impaired at the balance sheet date.

| | | PAST DUE BUT NOT IMPAIRED | | | | |
|---|---|---|---|---|---|---|
| | NEITHER PAST DUE NOR IMPAIRED | 0 TO 3 MTHS | 3 TO 6 MTHS | 6 MTHS TO 1 YEAR | GREATER THAN 1 YEAR | TOTAL |
| | $M | $M | $M | $M | $M | $M |
| **At 31 December 2014** | | | | | | |
| Amounts due from related entities | **121.8** | - | - | - | - | **121.8** |
| Premium receivable [1] | **71.2** | **25.6** | **11.0** | **2.4** | - | **110.2** |
| Other receivables | **16.6** | - | - | - | - | **16.6** |
| Amount due from controlled entities | **20.6** | - | - | - | - | **20.6** |
| **At 31 December 2013** | | | | | | |
| Amounts due from related entities | 116.8 | - | - | - | - | 116.8 |
| Premium receivable [1] | 67.1 | 28.3 | 10.3 | 1.9 | - | 107.6 |
| Other receivables | 7.0 | - | - | - | 0.5 | 7.5 |
| Amount due from controlled entities | 15.9 | - | - | - | - | 15.9 |

[1] Net of a provision for impairment

### (ii) Reinsurance counterparty credit risk
The company's objective is to maximise placement of reinsurance with highly rated counterparties. Concentration of risk with reinsurance counterparties is monitored strictly and regularly by the company's security committee and is controlled by reference to the following protocols:

- Treaty or facultative reinsurance is placed in accordance with the requirements of the company's reinsurance management strategy and Group security committee guidelines;
- Reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historical losses and potential future losses based on RDSs and the company's Insurance Concentration Risk Charge (ICRC);
- Exposure to reinsurance counterparties and the credit quality of those counterparties is actively monitored.

Credit risk exposures are calculated regularly and compared with authorised credit limits. In certain cases, the company requires letters of credit or other collateral arrangements to be provided to guarantee the recoverability of the amount involved. The company holds $144.9 million (2013: $257.9 million) in collateral to support reinsurance arrangements. The credit rating analysis below includes the impact of such security arrangements. In some cases, further security has been obtained in the form of trust arrangements, reinsurer default protection and other potential offsets. This additional security has not been included in the credit rating analysis set out below.

**4. RISK MANAGEMENT (CONTINUED)**
**(C) Credit risk (continued)**
**(ii) Reinsurance counterparty credit risk (continued)**

The following table provides information about the quality of the company's credit risk exposure in respect of undiscounted reinsurance and other recoveries on outstanding claims at the balance sheet date. The analysis classifies the assets according to Standard and Poor's counterparty ratings. AAA is the highest possible rating. Rated assets falling outside the range of AAA to BBB are classified as speculative grade.

| | CREDIT RATING | | | | | | |
|---|---|---|---|---|---|---|---|
| | AAA | AA | A | BBB | SPECULATIVE GRADE | NOT RATED | TOTAL |
| | $M | $M | $M | $M | $M | $M | $M |
| **As at 31 December 2014** | | | | | | | |
| Reinsurance recoveries on outstanding claims[1] | - | **100.5** | **188.3** | **0.2** | - | **6.2** | **295.2** |
| Reinsurance recoveries on paid claims[1] | - | **25.1** | **9.3** | - | - | **0.2** | **34.6** |
| **As at 31 December 2013** | | | | | | | |
| Reinsurance recoveries on outstanding claims[1] | - | 244.1 | 267.9 | 0.5 | - | 10.7 | 523.2 |
| Reinsurance recoveries on paid claims[1] | - | 13.7 | 4.8 | - | - | - | 18.5 |

[1] Net of a provision for impairment

The following table provides further information regarding the aging of reinsurance recoveries on paid claims at the balance sheet date.

| | | | PAST DUE | | | | |
|---|---|---|---|---|---|---|---|
| | | NEITHER PAST DUE NOR IMPAIRED | 0 TO 3 MTHS | 3 TO 6 MTHS | 6 MTHS TO 1 YEAR | GREATER THAN 1 YEAR | TOTAL |
| | | $M | $M | $M | $M | $M | $M |
| Reinsurance recoveries on paid claims[1] | **2014** | **5.2** | **29.3** | - | **0.1** | - | **34.6** |
| | **2013** | 16.2 | - | 0.1 | - | 2.2 | 18.5 |

[1] Net of a provision for impairment

**(D) Market risk**

Market risk is the risk of variability in the value of, and returns on, investments and the risk associated with variability of interest rates, credit spreads, foreign exchange rates and economy-wide inflation on both assets and liabilities, excluding insurance liabilities.

Market risk comprises three types of risk: currency risk (due to fluctuations in foreign exchange rates); interest rate risk (due to fluctuations in market interest rates); and price risk (due to fluctuations in market prices). Within each of these categories, risks are evaluated before considering the effect of mitigating controls. The existence and effectiveness of such mitigating controls are then measured to ensure that residual risks are managed within the company's risk appetite.

## 4. RISK MANAGEMENT (CONTINUED)

### (D) Market risk (continued)

### (i) Currency risk

The company's exposure to currency risk generally arises as a result of either the translation of foreign currency amounts back to the functional currency of a controlled entity (operational currency risk) or due to the translation of the company's net investment in foreign operations to the company's presentation currency of Australian dollars.

**Operational currency risk**

The company is exposed to currency risk in respect of its operational net foreign currency exposures within each of its controlled entities. This risk is managed as follows:

- The company manages the volatility arising from changes in foreign exchange rates by matching liabilities with assets of the same currency, as far as is practicable, thus ensuring that any exposures to foreign currencies are minimised.
- Forward foreign exchange contracts are used where possible to protect residual currency positions. These forward foreign exchange contracts are accounted for in accordance with the derivatives accounting policy set out in note 1(N).

Foreign exchange gains or losses arising from operational foreign currency exposures are reported in profit or loss consistent with the gains or losses from the related forward foreign exchange contracts. The risk management process covering the use of forward foreign exchange contracts involves close senior management scrutiny, including regular board and other management reporting. All forward foreign exchange contracts are subject to delegated authority levels provided to management and the levels of exposure are reviewed on an ongoing basis.

The company's aim is to mitigate, where possible, its operational foreign currency exposures at a controlled entity level. From time to time, the company may maintain an operational foreign currency exposure to offset currency volatility arising from translation of foreign currency forecast profits, subject to senior management approval and adherence to board approved limits.

The analysis below demonstrates the impact on profit after income tax of a 10% strengthening or weakening of the Australian dollar against the major currencies to which the company is exposed. The sensitivity is measured with reference to the company's residual (or unmatched) operational foreign currency exposures at the balance sheet date. Operational foreign exchange gains or losses are recognised in profit or loss in accordance with the policy set out in note 1(T). The sensitivities provided demonstrate the impact of a change in one key variable in isolation whilst other assumptions remain unchanged. The matching of foreign currency assets and liabilities is actively managed.

The sensitivities shown in the table below are relevant only at the balance sheet date, as any unmatched exposures are actively monitored by management and the exposure matched and therefore assumes no response by management to movements in a variable.

## 4. RISK MANAGEMENT (CONTINUED)

### (D) Market risk (continued)
### (i) Currency risk (continued)
**Operational currency risk (continued)**

| | 2014 $M | | | 2013 $M | | |
|---|---|---|---|---|---|---|
| | RESIDUAL EXPOSURE | SENSITIVITY | PROFIT (LOSS)[1] | RESIDUAL EXPOSURE | SENSITIVITY | PROFIT (LOSS)[1] |
| EXPOSURE CURRENCY | $M | % | $M | $M | % | $M |
| NZ dollar | 184.5 | +10 | 12.3 | 114.3 | +10 | 7.4 |
| | | -10 | (12.3) | | -10 | (7.4) |
| Singapore dollar | 92.6 | +10 | 6.0 | 9.5 | +10 | 0.6 |
| | | -10 | (6.0) | | -10 | (0.6) |
| Euro | 46.0 | +10 | 4.8 | 25.1 | +10 | 2.7 |
| | | -10 | (4.8) | | -10 | (2.7) |

[1] Net of tax at the company's prima facie rate of 30%

### (ii) Interest rate risk
Financial instruments with a floating interest rate expose the company to cash flow interest rate risk, whereas fixed interest rate instruments expose the company to fair value interest rate risk.

QBE Group's risk management approach is to minimise interest rate risk by actively managing investment portfolios to achieve a balance between cash flow interest rate risk and fair value interest rate risk. The company predominately invests in high quality, liquid interest-bearing securities and cash and may use derivative financial instruments to manage the interest rate risk of the fixed interest portfolio. The risk management processes over these derivative financial instruments include close senior management scrutiny, including appropriate board and other management reporting. Derivatives are used only for approved purposes and are subject to delegated authority levels provided to management. The level of derivative exposure is reviewed on an ongoing basis. Appropriate segregation of duties exists with respect to derivative use and compliance with policy, limits and other requirements is closely monitored.

The claims provision is discounted to present value by reference to risk-free interest rates. The company is therefore exposed to potential underwriting result volatility as a result of interest rate movements. In practice, however, an increase or decrease in interest rates is normally offset by a corresponding increase or decrease in inflation. Details are provided in note 3(A)(v). The company maintains a relatively short duration for assets backing policyholders' funds in order to minimise any further potential volatility affecting insurance profit.

The contractual maturity profile of the company's interest-bearing financial assets and hence its exposure to interest rate risk, and the effective weighted average interest rate for interest-bearing financial assets is analysed in the table below. The table includes investments at the maturity date of the security; however, many of the longer dated securities have call dates of relatively short duration. At 31 December 2014, the average modified duration of cash and fixed interest securities was 0.66 years (2013: 0.29 years).

## 4. RISK MANAGEMENT (CONTINUED)

### (D) Market risk (continued)
### (ii) Interest rate risk (continued)

| | | INTEREST–BEARING FINANCIAL ASSETS MATURING IN | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | 1 YEAR OR LESS | 1 TO 2 YEARS | 2 TO 3 YEARS | 3 TO 4 YEARS | 4 TO 5 YEARS | OVER 5 YEARS | TOTAL |
| **At 31 December 2014** | | | | | | | | |
| Fixed rate | $M | **442.1** | **31.9** | **64.8** | **10.6** | **41.5** | **1.9** | **592.8** |
| Weighted average interest rate | % | **1.61** | **3.77** | **2.44** | **4.53** | **4.46** | **3.11** | **2.07** |
| Floating rate | $M | **110.0** | **44.5** | **14.3** | **6.8** | **-** | **4.0** | **179.6** |
| Weighted average interest rate | % | **1.15** | **3.03** | **3.61** | **4.38** | **-** | **1.48** | **1.94** |
| Forward foreign exchange contracts | $M | **0.6** | **-** | **-** | **-** | **-** | **-** | **0.6** |
| **At 31 December 2013** | | | | | | | | |
| Fixed rate | $M | 581.6 | 15.4 | 2.0 | 4.1 | 0.1 | 1.8 | 605.0 |
| Weighted average interest rate | % | 1.36 | 3.53 | 0.86 | 0.86 | 5.83 | 3.15 | 1.42 |
| Floating rate | $M | 61.7 | 46.9 | 37.9 | 13.4 | 7.5 | 4.8 | 172.2 |
| Weighted average interest rate | % | 1.08 | 2.57 | 2.43 | 3.44 | 3.54 | 1.39 | 2.08 |
| Forward foreign exchange contracts | $M | 0.8 | - | - | - | - | - | 0.8 |

All financial assets are measured at fair value through profit or loss. Movements in interest rates impact the value of interest-bearing financial assets and therefore impact reported profit after tax. The impact of a 0.5% increase or decrease in interest rates on interest-bearing financial assets owned by the company at the balance sheet date is shown in the table below.

| | SENSITIVITY | PROFIT (LOSS)[1] 2014 | PROFIT (LOSS)[1] 2013 |
|---|---|---|---|
| | % | $M | $M |
| Interest rate movement – interest-bearing financial assets | +0.5 | **(2.5)** | (1.1) |
| | -0.5 | **2.1** | 0.9 |

[1] Net of tax at the company's prima facie rate of 30%

## 4. RISK MANAGEMENT (CONTINUED)

### (D) Market risk (continued)
### (iii) Price risk
Price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded on the market.

The company is exposed to price risk on its investment in equities and may use derivative financial instruments to manage this exposure. The risk management processes over these derivative financial instruments are the same as those explained in note 4(D)(i) in respect of interest rate derivative financial instruments. Exposure is also managed by diversification across worldwide markets and currencies.

At 31 December 2014, the company did not hold any investments in listed equities (2013: nil).

The company is also exposed to price risk on its investment in fixed interest and floating rate securities. All corporate securities are measured at fair value through profit or loss. Movements in credit spreads impact the value of corporate fixed interest and floating rate securities and therefore impact reported profit after tax.

This risk is managed by investing in high quality, liquid interest-bearing corporate securities and by managing the credit spread duration of the corporate securities portfolio.

The impact of a 0.5% increase or decrease in credit spreads on fixed interest and floating rate securities owned by the company at the balance sheet date is shown in the table below.

| | | PROFIT (LOSS)[1] | |
|---|---|---|---|
| | SENSITIVITY | 2014 | 2013 |
| | % | $M | $M |
| Credit spread movement – corporate interest-bearing financial assets | +0.5 | **(1.9)** | (1.4) |
| | -0.5 | **1.6** | 1.2 |

[1] Net of tax at the company's prima facie rate of 30%

## 4. RISK MANAGEMENT (CONTINUED)

### (E) Liquidity risk

Liquidity risk is the risk of insufficient liquid assets to meet liabilities as they fall due to policyholders and other creditors. This includes the risk associated with asset liability management. The key objective of the company's asset and liability management strategy is to ensure sufficient liquidity is maintained at all times to meet the company's obligations including its settlement of insurance liabilities and, within these parameters, to optimise investment returns for policyholders and shareholders.

Liquidity must be sufficient to meet both planned and unplanned cash requirements. The company is exposed to liquidity risk mainly through its obligations to make payments in relation to its insurance activities.

In addition to treasury cash held for working capital requirements, and in accordance with the company's liquidity policy, a minimum percentage of consolidated investments and cash is held in liquid, short-term money market securities to ensure that there are sufficient liquid funds available to meet insurance and investment obligations. The company has a strong liquidity position. The maturity of the company's interest-bearing financial assets is included in the table in note 4(D)(ii).

The company limits the risk of liquidity shortfalls resulting from mismatches in the timing of claims payments and receipts of claims recoveries by negotiating cash call clauses in reinsurance contracts and seeking accelerated settlements for large reinsurance recoveries.

The following tables summarise the contractual maturity profile of certain of the company's financial liabilities based on the remaining contractual obligations.

| | 1 YEAR OR LESS $M | 1 TO 3 YEARS $M | 3 TO 5 YEARS $M | OVER 5 YEARS $M | NO TERM $M | TOTAL $M |
|---|---|---|---|---|---|---|
| **At 31 December 2014** | | | | | | |
| Trade payables | **12.3** | **1.0** | - | - | - | **13.3** |
| Amounts due to related entities | **144.8** | - | - | - | - | **144.8** |
| Other payables | **16.8** | - | - | - | - | **16.8** |
| Accrued expenses | **8.1** | - | - | - | - | **8.1** |
| Financial guarantees | | **16.3** | - | - | - | **16.3** |
| Provisions | **2.3** | **0.2** | - | - | - | **2.5** |
| **At 31 December 2013** | | | | | | |
| Trade payables | 14.1 | - | 0.5 | - | - | 14.6 |
| Amounts due to related entities | 104.0 | - | - | - | - | 104.0 |
| Other payables | 83.4 | - | - | - | - | 83.4 |
| Accrued expenses | 11.5 | - | - | - | - | 11.5 |
| Financial guarantees | - | 2.3 | 13.4 | - | - | 15.7 |
| Provisions | 2.0 | 0.3 | - | - | - | 2.3 |

The company has no significant concentration of liquidity risk.

The maturity profile of the company's net outstanding claims provision is analysed in note 19(B).

## 4. RISK MANAGEMENT (CONTINUED)

### (F) Operational risk

Operational risk is the risk of financial loss resulting from inadequate or failed internal processes, people and systems or from external events (including legal risk). The QBE Group manages operational risk within the same risk management framework as its other risks. The risk assessment and monitoring framework involves on-going:

- identification and review of the key risks to the company;
- definition of the acceptable level of risk appetite and tolerance;
- assessment of those risks throughout the company in terms of the acceptable level of risk (risk tolerance) and the residual risk remaining after having considered risk treatment;
- assessment of whether each risk is within the acceptable level of risk, or requires appropriate action be taken to mitigate any excess risk;
- transparent monitoring and reporting of risk management related matters on a timely basis; and
- setting the audit framework and resulting internal audit plan on a risk basis.

One of the cornerstones of the QBE Group's risk management framework is the recruitment and retention of high quality people who are entrusted with appropriate levels of autonomy within the parameters of disciplined risk management practices.

The company operates a system of delegated authorities based on expertise and proven performance, and compliance is closely monitored. Other controls include effective segregation of duties, access controls and authorisation and reconciliation procedures.

### (G) Group risk

Group risk is defined as the risk to a division as a result of being part of the wider Group, including the financial impact and loss of support from the parent company.

## 5. INCOME AND EXPENSES

### (A) Income summary

| | 2014 $M | 2013 $M |
|---|---|---|
| **Gross earned premium revenue** | | |
| Direct and facultative | **538.7** | 476.9 |
| Inward reinsurance | - | - |
| | **538.7** | 476.9 |
| **Other revenue** | | |
| Reinsurance and other recoveries revenue | **121.6** | 79.2 |
| Reinsurance commission revenue | **17.6** | 13.4 |
| | **677.9** | 569.5 |
| **Other income** | | |
| Dividends received or receivable | - | 13.0 |
| Interest received or receivable | **10.7** | 7.6 |
| Net fair value gains on financial | **4.2** | 2.7 |
| Realised gain on sales of related entities | - | 0.2 |
| | **14.9** | 23.5 |
| Income | **692.8** | 593.0 |

### (B) Expenses summary

| | 2014 $M | 2013 $M |
|---|---|---|
| Outward reinsurance premium expense | **200.5** | 188.2 |
| Gross claims incurred | **290.4** | 194.8 |
| Gross commission expense | **74.3** | 69.2 |
| Other acquisition costs | **26.8** | 21.2 |
| Underwriting and other expenses | **58.8** | 44.9 |
| Investment expenses | **0.5** | 0.5 |
| Foreign exchange losses | **1.7** | 1.7 |
| Expenses | **653.0** | 520.5 |
| | | |
| Profit before income tax | **39.8** | 72.5 |

### (C) Specific items

| | 2014 $M | 2013 $M |
|---|---|---|
| Payments on operating leases | **4.1** | 3.8 |
| Depreciation of property, plant and equipment | **1.3** | 1.0 |
| Loss on sale of plant and equipment | **0.1** | 0.1 |

## 6. CLAIMS INCURRED

### (A) Claims analysis

| | 2014 $M | 2013 $M |
|---|---|---|
| **Gross claims incurred and related expenses** | | |
| Direct and facultative | **290.4** | 197.7 |
| Inward reinsurance | **-** | (2.9) |
| | **290.4** | 194.8 |
| **Reinsurance and other recoveries** | | |
| Direct and facultative | **121.5** | 79.1 |
| Inward reinsurance | **0.1** | 0.1 |
| | **121.6** | 79.2 |
| **Net claims incurred** | **168.8** | 115.6 |

### (B) Claims development

Current year's claims relate to risks borne in the current reporting year. Prior year claims relate to a reassessment of the risks borne in all previous reporting years and include releases of risk margins as claims are paid. Refer to note 6(C).

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | CURRENT YEAR $M | PRIOR YEARS $M | TOTAL $M | CURRENT YEAR $M | PRIOR YEARS $M | TOTAL $M |
| **Gross claims incurred and related expenses** | | | | | | |
| Undiscounted | **232.6** | **42.2** | **274.8** | 190.4 | (27.0) | 163.4 |
| Discount | **(3.6)** | **19.2** | **15.6** | (3.1) | 34.5 | 31.4 |
| | **229.0** | **61.4** | **290.4** | 187.3 | 7.5 | 194.8 |
| **Reinsurance and other recoveries** | | | | | | |
| Undiscounted | **61.8** | **45.0** | **106.8** | 37.5 | 15.4 | 52.9 |
| Discount | **(1.2)** | **16.0** | **14.8** | (1.8) | 28.1 | 26.3 |
| | **60.6** | **61.0** | **121.6** | 35.7 | 43.5 | 79.2 |
| **Net claims incurred** | | | | | | |
| Undiscounted | **170.8** | **(2.8)** | **168.0** | 152.9 | (42.4) | 110.5 |
| Discount | **(2.4)** | **3.2** | **0.8** | (1.3) | 6.4 | 5.1 |
| Net claims incurred - discounted | **168.4** | **0.4** | **168.8** | 151.6 | (36.0) | 115.6 |

## 6. CLAIMS INCURRED (CONTINUED)

### (C) Reconciliations of net claims incurred to claims development table

The development of the net outstanding claims for the 10 most recent accident years is shown in note 19(E). This note is a reconciliation of the amounts included in the table in note 6(B) and the current financial year movements in the claims development table.

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | CURRENT ACCIDENT YEAR $M | PRIOR ACCIDENT YEARS $M | TOTAL $M | CURRENT ACCIDENT YEAR $M | PRIOR ACCIDENT YEARS $M | TOTAL $M |
| Net undiscounted claims development – central estimate (note 19 (E)) | **156.1** | **4.1** | **160.2** | 127.0 | (10.6) | 116.4 |
| Foreign exchange | **-** | **(0.3)** | **(0.3)** | - | (5.8) | (5.8) |
| Movement in claims settlement costs | **8.1** | **0.1** | **8.2** | 12.9 | (10.9) | 2.0 |
| Movement in discount | **(2.4)** | **3.2** | **0.8** | (1.3) | 6.4 | 5.1 |
| Movement in risk margin | **6.6** | **(6.7)** | **(0.1)** | 13.0 | (15.1) | (2.1) |
| **Net claims incurred – discounted** | **168.4** | **0.4** | **168.8** | 151.6 | (36.0) | 115.6 |

## 7. INCOME TAX EXPENSE

### (A) Reconciliation of prima facie tax to income tax expense

| | 2014 $M | 2013 $M |
|---|---|---|
| Profit before income tax | **39.8** | 72.5 |
| Prima facie tax payable at 30% | **12.0** | 21.7 |
| Tax effect of non-temporary differences: | | |
| Differences in tax rates | **0.6** | (0.7) |
| Other, including non-allowable expenses and non-taxable income | **0.1** | (4.4) |
| Prima facie tax adjusted for non-temporary differences | **12.7** | 16.6 |
| Underprovision/(overprovision) in prior years | **7.1** | (0.1) |
| Income tax expense | **19.8** | 16.5 |
| Analysed as follows: | | |
| Current tax | **10.5** | 13.9 |
| Deferred tax | **2.2** | 2.7 |
| Underprovision/(overprovision) in prior years | **7.1** | (0.1) |
| | **19.8** | 16.5 |
| Deferred tax expense comprises: | | |
| Deferred tax assets recognised in profit or loss | **0.1** | 0.7 |
| Deferred tax liabilities recognised in profit or loss | **2.1** | 2.0 |
| | **2.2** | 2.7 |

The company has potential exposures in relation to certain historic taxation matters regarding which the Commissioner of Inland Revenue (New Zealand) has issued a Notice of Proposed Adjustment. The quantum of tax proposed by the Commissioner is NZ $8.9 million ($8.5 million) before any available deductions. The company has estimated the use of money interest to be between NZ $2.0 million ($1.9 million) to NZ $3.0 million ($2.9 million) before any available deductions. The company continues to dispute this matter having obtained professional advice.

## 7. INCOME TAX EXPENSE (CONTINUED)

### (B) Tax consolidation legislation

The accounting policy in relation to this legislation is set out in note 1(J).

QBE Insurance Group Limited and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation.

On adoption of the tax consolidation legislation, the entities in the tax consolidated group entered into a tax sharing and tax funding agreement under which the wholly-owned entities are required to fully compensate QBE Insurance Group Limited for any current tax payable and are compensated by QBE Insurance Group Limited for any current tax receivable and deferred tax assets relating to unused tax losses or unused tax credits that are transferred to QBE Insurance Group Limited under the tax consolidation legislation.

The head entity, QBE Insurance Group Limited, and the controlled entities in the tax consolidated group allocate compensation based on a notional stand-alone tax calculation done as if each entity in the tax consolidated group was a stand-alone taxpayer in its own right. The assets and liabilities arising under the arrangement are recognised as inter-company assets and liabilities in the balance sheet of each Australian company.

## 8. CASH AND CASH EQUIVALENTS

| | 2014<br>$M | 2013<br>$M |
|---|---|---|
| Cash at bank and on hand | **77.8** | 41.7 |
| Overnight money | **-** | 0.2 |
| Cash management trust | **-** | 0.4 |
| Term deposits | **18.2** | 19.3 |
| | **96.0** | 61.6 |
| Analysed as follows: | | |
| Fixed interest rate | **18.2** | 19.3 |
| Floating interest rate | **77.8** | 42.3 |
| | **96.0** | 61.6 |

Amounts in cash and cash equivalents are the same as those included in the cash flow statement.

Cash and cash equivalents include balances readily convertible to cash. All balances are held to service normal operational requirements.

### (A) Reconciliation of cash flows from operating activities to profit after income tax

| | 2014<br>$M | 2013<br>$M |
|---|---|---|
| Net cash flows from operating activities | **34.9** | 40.2 |
| Depreciation of property, plant and equipment | **(1.3)** | (1.0) |
| Depreciation of intangible assets | **(0.5)** | - |
| Amortisation of premium/discount on fixed interest securities | **(0.8)** | (0.9) |
| Increase in net amounts receivable from controlled entities | **-** | 5.0 |
| Loss on sale of plant and equipment | **(0.1)** | (0.1) |
| Net foreign exchange loss | **(1.7)** | (1.7) |
| Other gains on financial assets | **6.9** | 8.2 |
| Increase in net outstanding claims | **(16.6)** | (3.0) |
| Increase in unearned premiums | **(13.1)** | (16.1) |
| Increase/(decrease) in deferred insurance costs | **1.6** | (8.7) |
| (Decrease)/increase in trade debtors | **(11.2)** | 59.6 |
| Increase/(decrease) in net operating assets | **3.1** | (0.5) |
| Decrease/(increase) in trade payables | **15.2** | (14.7) |
| Decrease/(increase) in tax liabilities | **3.6** | (10.3) |
| Profit after income tax | **20.0** | 56.0 |

## 9. INVESTMENTS

| | 2014 $M | 2013 $M |
|---|---|---|
| **Fixed interest rate** | | |
| Short term money | **379.4** | 493.0 |
| Government bonds | **79.4** | 47.2 |
| Corporate bonds | **115.8** | 45.4 |
| | **574.6** | 585.6 |
| **Floating interest rate** | | |
| Short term money | **1.7** | 1.2 |
| Corporate bonds | **100.1** | 128.8 |
| | **101.8** | 130.0 |
| Total investments | **676.4** | 715.6 |
| Amounts maturing within 12 months | **456.1** | 581.7 |
| Amounts maturing in greater than 12 months | **220.3** | 133.9 |
| Total investments | **676.4** | 715.6 |

### (A) Charges over investments and other assets

No encumbered asset at 31 December 2014 was held in the investment portfolio of QBE Insurance (Australia) Limited on behalf of QBE Insurance (International) Limited (2013: market value $2.6 million; face value $2.5 million).

### (B) Fair value hierarchy

The investments of the company are disclosed in the table below using a fair value hierarchy which reflects the significance of inputs into the determination of fair value as follows:

**Level 1**: Valuation is based on quoted prices in active markets for the same instruments.

**Level 2**: Valuation is based on quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data, for example, consensus price using broker quotes and valuation model with observable inputs.

**Level 3**: Valuation techniques are applied for which any significant input is not based on observable market data.

| | 2014 | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | LEVEL 1 $M | LEVEL 2 $M | LEVEL 3 $M | TOTAL $M | LEVEL 1 $M | LEVEL 2 $M | LEVEL 3 $M | TOTAL $M |
| **Assets** | | | | | | | | |
| Short-term money | **61.0** | **320.1** | - | **381.1** | 62.8 | 431.4 | - | 494.2 |
| Government bonds | **21.1** | **58.3** | - | **79.4** | 6.8 | 39.1 | 1.3 | 47.2 |
| Fixed interest trusts | - | - | - | - | - | - | - | - |
| Corporate bonds | - | **215.9** | - | **215.9** | - | 174.2 | - | 174.2 |
| Total investments | **82.1** | **594.3** | - | **676.4** | 69.6 | 644.7 | 1.3 | 715.6 |

**9. INVESTMENTS (CONTINUED)**

**(C) Valuation of investments**
The company's approach to measuring the fair value of investments is described below:

**Short-term money**
Term deposits are valued at par plus accrued interest and are classified as level 1. Other short-term money (bank bills, certificates of deposit, treasury bills and other short-term instruments) are priced using interest rates and yield curves observable at commonly quoted intervals.

**Fixed and floating rate bonds**
Bonds which are traded in active markets and have quoted prices from external data providers are classified as level 1. Bonds which are not traded in active markets are priced using broker quotes, using comparable prices for similar instruments or using pricing techniques set by local regulators or exchanges.

**(D) Movements in level 3 investments**
The following table provides an analysis of investments valued with reference to level 3 inputs.

| Level 3 | 2014 $M | 2013 $M |
|---|---|---|
| At 1 January | **1.3** | 1.1 |
| Reclassification to level 3 investments | - | - |
| Purchases | **2.0** | 1.1 |
| Disposals | **(3.2)** | (1.1) |
| Net fair value unrealised gains recognised in profit or loss | **(0.1)** | 0.2 |
| At 31 December | - | 1.3 |

**(E) Restrictions in use**

The France branch of the company has €45.7 million ($67.8 million) in investment (2013: $70.2 million) with the French insurance authority and controller to cover technical reserves.

## 10. DERIVATIVE FINANCIAL INSTRUMENTS

| | ASSETS | | LIABILITIES | |
|---|---|---|---|---|
| | 2014 $M | 2013 $M | 2014 $M | 2013 $M |
| **Maturing within 12 months** | | | | |
| Forward foreign exchange contracts | **0.6** | 0.8 | **5.2** | 1.7 |

All derivative positions entered into by the company are for economic hedging purposes but do not, in all cases, meet the criteria for hedge accounting.

### (A) Forward foreign exchange contracts

Forward foreign exchange contracts are entered into by the company for the purpose of managing residual foreign currency exposures. The company's policy for managing such exposures is explained in note 4(D). Undiscounted contractual amounts to sell $56.1 million (2013: $28.3 million) were outstanding at the balance sheet date. All these contracts mature within 12 months of the balance sheet date.

### (B) Credit risk

Credit risk may arise on forward foreign exchange contracts if the counterparty fails to meet its contractual settlement obligations. The unrealised gains of $0.6 million (2013: $0.8 million) represent the company's exposure to credit risk on forward foreign exchange contracts at the balance sheet date.

### (C) Fair value hierarchy

The company's accounting policy in relation to the valuation of derivatives is set out in note 1(N). Derivatives are analysed in the table below using a fair value hierarchy which reflects the significance of inputs into the determination of fair value. The hierarchy is explained in more detail in note 9(B).

| | 2014 | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | LEVEL 1 $M | LEVEL 2 $M | LEVEL 3 $M | TOTAL $M | LEVEL 1 $M | LEVEL 2 $M | LEVEL 3 $M | TOTAL $M |
| **Assets** | | | | | | | | |
| Forward foreign exchange contracts | **0.6** | - | - | **0.6** | 0.8 | - | - | 0.8 |
| **Liabilities** | | | | | | | | |
| Forward foreign exchange contracts | **5.2** | - | - | **5.2** | 1.7 | - | - | 1.7 |

## 11. TRADE AND OTHER RECEIVABLES

| | 2014 $M | 2013 $M |
|---|---|---|
| **Trade receivables** | | |
| Premium receivable[1] | **110.2** | 107.6 |
| Reinsurance and other recoveries[1] | **34.6** | 18.5 |
| Unclosed premium | **37.3** | 27.5 |
| | **182.1** | 153.6 |
| Other receivables | **16.6** | 7.5 |
| Prepayments | **0.7** | 0.8 |
| Amounts due from controlled entities | **20.6** | 15.9 |
| Amounts due from related entities | **121.8** | 116.8 |
| Trade and other receivables | **341.8** | 294.6 |
| Receivable within 12 months | **341.8** | 292.3 |
| Receivable in greater than 12 months | **-** | 2.3 |
| Trade and other receivables | **341.8** | 294.6 |

[1] Net of a provision for impairment

### (A) Provision for impairment

| | PREMIUM RECEIVABLE 2014 $M | PREMIUM RECEIVABLE 2013 $M | REINSURANCE AND OTHER RECOVERIES 2014 $M | REINSURANCE AND OTHER RECOVERIES 2013 $M |
|---|---|---|---|---|
| At 1 January | **0.5** | 0.3 | **2.1** | 1.7 |
| Decrease in provision from bad debts written off | **-** | - | **(0.6)** | (0.1) |
| Increase in provision | **0.6** | 0.2 | **-** | 0.5 |
| At 31 December | **1.1** | 0.5 | **1.5** | 2.1 |

### (B) Fair value

Due to the short term nature of these receivables, their carrying value is assumed to approximate their fair value.

### (C) Risk

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivables. No receivables are pledged by the company as collateral for liabilities or contingent liabilities. Information on the ageing and credit rating of balances in the table above, where relevant, is included in note 4(C). Note 4 also provides more information on the risk management policies of the company.

## 12. DEFERRED INSURANCE COSTS

| | 2014 $M | 2013 $M |
|---|---|---|
| Deferred reinsurance premium | **37.6** | 38.9 |
| Deferred net commission | **36.1** | 30.5 |
| Deferred acquisition costs | **13.1** | 12.5 |
| Deferred insurance costs | **86.8** | 81.9 |
| To be expensed within 12 months | **77.7** | 75.7 |
| To be expensed in greater than 12 months | **9.1** | 6.2 |
| Deferred insurance costs | **86.8** | 81.9 |

| | DEFERRED REINSURANCE PREMIUM | | DEFERRED NET COMMISSION | | DEFERRED ACQUISITION COSTS | |
|---|---|---|---|---|---|---|
| | 2014 $M | 2013 $M | 2014 $M | 2013 $M | 2014 $M | 2013 $M |
| At 1 January | **38.9** | 46.6 | **30.5** | 22.4 | **12.5** | 9.5 |
| Costs deferred in financial year | **35.0** | 35.3 | **33.8** | 27.4 | **4.2** | 3.8 |
| Amortisation of costs deferred in previous financial years | **(37.7)** | (48.4) | **(29.5)** | (23.0) | **(4.0)** | (2.4) |
| Foreign exchange | **1.4** | 5.4 | **1.3** | 3.7 | **0.4** | 1.6 |
| At 31 December | **37.6** | 38.9 | **36.1** | 30.5 | **13.1** | 12.5 |

## 13. PROPERTY, PLANT AND EQUIPMENT

| 2014 | LEASEHOLD IMPROVEMENTS $M | IT/OFFICE EQUIPMENT/ FIXTURES & FITTINGS $M | MOTOR VEHICLES $M | TOTAL $M |
|---|---|---|---|---|
| **Cost or valuation** | | | | |
| At 1 January | **1.4** | **8.9** | **0.7** | **11.0** |
| Additions | **-** | **0.6** | **0.3** | **0.9** |
| Disposals | **-** | **(0.9)** | **(0.3)** | **(1.2)** |
| Foreign exchange | **0.1** | **0.1** | **-** | **0.2** |
| At 31 December | **1.5** | **8.7** | **0.7** | **10.9** |
| **Accumulated depreciation and impairment losses** | | | | |
| At 1 January | **(0.8)** | **(6.0)** | **(0.4)** | **(7.2)** |
| Disposals | **-** | **0.9** | **0.2** | **1.1** |
| Depreciation charge for the year | **(0.3)** | **(0.9)** | **(0.1)** | **(1.3)** |
| Foreign exchange | **-** | **-** | **-** | **-** |
| At 31 December | **(1.1)** | **(6.0)** | **(0.3)** | **(7.4)** |
| **Carrying amount** | | | | |
| At 31 December | **0.4** | **2.7** | **0.4** | **3.5** |

| 2013 | LEASEHOLD IMPROVEMENTS $M | IT/OFFICE EQUIPMENT/ FIXTURES & FITTINGS $M | MOTOR VEHICLES $M | TOTAL $M |
|---|---|---|---|---|
| **Cost or valuation** | | | | |
| At 1 January | 1.2 | 7.0 | 0.7 | 8.9 |
| Additions | - | 0.9 | 0.1 | 1.0 |
| Disposals | - | (0.2) | (0.2) | (0.4) |
| Foreign exchange | 0.2 | 1.2 | 0.1 | 1.5 |
| At 31 December | 1.4 | 8.9 | 0.7 | 11.0 |
| **Accumulated depreciation and impairment losses** | | | | |
| At 1 January | (0.6) | (4.6) | (0.4) | (5.6) |
| Disposals | - | 0.2 | 0.2 | 0.4 |
| Depreciation charge for the year | (0.1) | (0.8) | (0.1) | (1.0) |
| Foreign exchange | (0.1) | (0.8) | (0.1) | (1.0) |
| At 31 December | (0.8) | (6.0) | (0.4) | (7.2) |
| **Carrying amount** | | | | |
| At 31 December | 0.6 | 2.9 | 0.3 | 3.8 |

## 14. DEFERRED INCOME TAX

| | 2014 $M | 2013 $M |
|---|---|---|
| Deferred tax assets | **4.2** | 4.6 |
| Deferred tax liabilities | **13.4** | 11.3 |

### (A) Deferred tax assets

### (i) The balance comprises temporary differences attributable to:

| | 2014 $M | 2013 $M |
|---|---|---|
| **Amounts recognised in profit or loss** | | |
| Provision for impairment | **0.2** | 0.1 |
| Employee benefits | **0.5** | 0.4 |
| Insurance provisions | **1.1** | 0.9 |
| Investment related | **2.2** | 2.3 |
| Other | **0.5** | 0.9 |
| Deferred tax assets before set-off | **4.5** | 4.6 |
| Set-off of deferred tax liabilities | **(0.3)** | - |
| | **4.2** | 4.6 |
| **Deferred tax assets before set-off analysed as follows:** | | |
| Recoverable within 12 months | **1.6** | 1.2 |
| Recoverable in greater than 12 months | **2.9** | 3.4 |
| | **4.5** | 4.6 |

### (ii) Movements

| | 2014 $M | 2013 $M |
|---|---|---|
| At 1 January | **4.6** | 5.3 |
| Amounts recognised in profit or loss | **(0.1)** | (0.7) |
| At 31 December | **4.5** | 4.6 |

### (B) Tax losses

The company has no tax losses brought to account in 2014 (2013: nil).

## 14. DEFERRED INCOME TAX (CONTINUED)

### (C) Deferred tax liabilities
### (i) The balance comprises temporary differences attributable to:

| | 2014 $M | 2013 $M |
|---|---|---|
| **Amounts recognised in profit or loss** | | |
| Insurance provisions | **10.5** | 8.7 |
| Investment related | **2.3** | 2.5 |
| Depreciation | **0.9** | 0.1 |
| Deferred tax liabilities before set-off | **13.7** | 11.3 |
| Set-off of deferred tax assets | **(0.3)** | - |
| | **13.4** | 11.3 |
| **Deferred tax liabilities before set-off analysed as follows:** | | |
| Payable within 12 months | **2.0** | 2.0 |
| Payable in greater than 12 months | **11.7** | 9.3 |
| | **13.7** | 11.3 |

### (ii) Movements:

| | 2014 $M | 2013 $M |
|---|---|---|
| At 1 January | **11.3** | 9.3 |
| Amounts recognised in profit or loss | **2.1** | 2.0 |
| At 31 December | **13.4** | 11.3 |

## 15. INVESTMENTS IN CONTROLLED ENTITIES

| | COUNTRY OF INCORPORATION | INVESTMENT | | EQUITY HOLDING | |
|---|---|---|---|---|---|
| | | 2014 $M | 2013 $M | 2014 % | 2013 % |
| QBE Insurance (Malaysia) Berhad | Malaysia | **44.0** | 44.0 | **100** | 100 |
| PT Asuransi QBE Pool Indonesia | Indonesia | **5.8** | 5.8 | **55** | 55 |
| QBE Insurance (Vietnam) Company Ltd | Vietnam | **18.3** | 18.3 | **100** | 100 |
| QBE Insurance (Singapore) Pte. Limited | Singapore | - | 0.2 | - | 100 |
| QBE Insurance (Thailand) Co Limited [1] | Thailand | **4.2** | 4.2 | **40.8** | 40.8 |
| | | **72.3** | 72.5 | | |

[1] For accounting purposes, the company has management control of QBE Insurance (Thailand) Co Limited. During the year, nil investments (2013: $0.6 million) and disposal of $0.2 million (2013: $0.8 million) were made in controlled entities.

## 16. INTANGIBLE ASSETS

| 2014 | SOFTWARE $M | GOODWILL $M | TOTAL $M |
|---|---|---|---|
| **Cost** | | | |
| At 1 January | **1.6** | **16.5** | **18.1** |
| Additions | **3.1** | - | **3.1** |
| Foreign exchange | **0.3** | - | **0.3** |
| At 31 December | **5.0** | **16.5** | **21.5** |
| **Accumulated amortisation** | | | |
| At 1 January | - | - | - |
| Impairment losses | - | - | - |
| Amortisation for the year | **(0.5)** | - | **(0.5)** |
| At 31 December | **(0.5)** | - | **(0.5)** |
| **Carrying amount** | | | |
| At 31 December | **4.5** | **16.5** | **21.0** |

| 2013 | SOFTWARE $M | GOODWILL $M | TOTAL $M |
|---|---|---|---|
| **Cost** | | | |
| At 1 January | - | 16.5 | 16.5 |
| Additions | 1.6 | - | 1.6 |
| Foreign exchange | - | - | - |
| At 31 December | 1.6 | 16.5 | 18.1 |
| **Accumulated amortisation** | | | |
| At 1 January | - | - | - |
| Impairment losses | - | - | - |
| Amortisation for the year | - | - | - |
| At 31 December | - | - | - |
| **Carrying amount** | | | |
| At 31 December | 1.6 | 16.5 | 18.1 |

### (A) Goodwill

Goodwill is allocated to cash generating units, or groups of units, expected to benefit from synergies arising from the acquisition giving rise to the goodwill. Cash generating units reflect the level at which goodwill is monitored by management. As the company continues to acquire operations and reorganise the way that operations are managed, reporting structures may change giving rise to a reassessment of cash generating units and/or the allocation of goodwill to those cash generating units.

## 16. INTANGIBLE ASSETS (CONTINUED)

### (B) Impairment testing of goodwill

The company's accounting policy in respect of impairment testing of goodwill is set out in note 1(Q). The recoverable amount of each cash generating unit has been determined by reference to a value in use calculation based on the following key assumptions and estimates:

- cash flow forecasts based on the latest three year business plan which has been approved by the Board. These forecasts are based on a combination of historical performance combined with management's expectations of future performance based on prevailing and anticipated market factors;
- terminal value is calculated using a perpetuity growth formula based on the cash flow forecast for year three. Growth rate reflects the long-term average of the country relevant to the cash generating unit and is sourced from observable market information. The terminal growth rate used in management's impairment testing is 2.5% (2013: 2.5%).
- discount rates reflect a beta and a market risk premium sourced from observable market information and a specific risk premium appropriate to reflect the nature of the business of each cash generating unit.

The pre-tax discount rates used to value significant cash generating units at 31 December 2014 were 9.0% for New Zealand branch and 10.2% for other branches (2013: 9.6% for New Zealand branch and 11.1% for other branches).

## 17. TRADE AND OTHER PAYABLES

| | 2014 $M | 2013 $M |
|---|---|---|
| Trade payables | **13.3** | 14.6 |
| Amounts due to related entities | **144.8** | 104.0 |
| Other payables | **16.8** | 83.4 |
| Accrued expenses | **8.1** | 11.5 |
| Trade and other payables | **183.0** | 213.5 |
| Payable within 12 months | **182.0** | 213.0 |
| Payable in greater than 12 months | **1.0** | 0.5 |
| Trade and other payables | **183.0** | 213.5 |

## 18. UNEARNED PREMIUM

### (A) Unearned premium

| | 2014 $M | 2013 $M |
|---|---|---|
| At 1 January | **280.7** | 228.9 |
| Deferral of premium on contracts written in the period | **285.2** | 253.0 |
| Earning of premium written in previous periods | **(272.0)** | (236.9) |
| Acquisition of entities | **-** | 0.4 |
| Foreign exchange | **10.7** | 35.3 |
| At 31 December | **304.6** | 280.7 |
| To be earned within 12 months | **283.2** | 265.5 |
| To be earned in greater than 12 months | **21.4** | 15.2 |
| Unearned premium | **304.6** | 280.7 |

### (B) Net premium liabilities

| | NOTE | 2014 $M | 2013 $M |
|---|---|---|---|
| Unearned premium | | **304.6** | 280.7 |
| Deferred insurance costs | 12 | **(86.8)** | (81.9) |
| Net premium liabilities | | **217.8** | 198.8 |

## 18. UNEARNED PREMIUM (CONTINUED)

### (C) Expected present value of future cash flows for future claims including risk margin

| | 2014 $M | 2013 $M |
|---|---|---|
| Undiscounted central estimate | **188.7** | 179.0 |
| Discount to present value | **(2.2)** | (1.9) |
| | **186.5** | 177.1 |
| Risk margin | **11.6** | 10.9 |
| Expected present value of future cash flows for future claims including risk margin | **198.1** | 188.0 |

### (D) Liability adequacy test

The probability of adequacy of the unearned premium liability differs from the probability of adequacy of the outstanding claims provision. The reason for the difference is that the former is a benchmark used only to test the sufficiency of net unearned premium liabilities whereas the latter is a measure of the adequacy of the outstanding claims provision actually carried by the company.

AASB 1023 requires the inclusion of a risk margin in insurance liabilities, but does not prescribe a minimum level of margin. Whilst there is established practice in the calculation of the probability of adequacy of the outstanding claims provisions, no such guidance exists in respect of the level of risk margin to be used in determining the adequacy of net premium liabilities. The company has adopted a risk margin of 6.2% (2013: 6.1%) for net unearned premium liabilities, for the purposes of the liability adequacy test to produce a 75% probability of adequacy in respect of total insurance liabilities. The 75% basis is a recognised industry benchmark in Australia, being the minimum probability of adequacy required for Australian licensed insurers by APRA. Without allowing for diversification benefits, the application of the 6.2% (2013: 6.1%) risk margin to the premium liabilities is estimated to achieve a probability of adequacy of 73.0% (2013: 73.0%) for net unearned premium liabilities on a standalone basis.

The application of the liability adequacy test in respect of net unearned premium liabilities identified a surplus at 31 December 2014 and 2013.

### (E) Risk margin

The process used to determine risk margin is explained in note 3(A)(iii). The risk margin in expected future cash flows for future claims as a percentage of the discounted central estimate is 6.2% (2013: 6.1%).

## 19. OUTSTANDING CLAIMS

### (A) Net outstanding claims

| | 2014 $M | 2013 $M |
|---|---|---|
| Gross outstanding claims provision | **523.0** | 714.1 |
| Risk margin | **38.3** | 37.2 |
| Outstanding claims | **561.3** | 751.3 |
| Reinsurance and other recoveries on outstanding claims | **(285.2)** | (498.6) |
| Net outstanding claims provision | **276.1** | 252.7 |
| **Analysed as follows:** | | |
| Net undiscounted central estimate | **243.9** | 222.2 |
| Discount to present value | **(6.1)** | (6.7) |
| Net discounted central estimate | **237.8** | 215.5 |
| Risk margin | **38.3** | 37.2 |
| Net outstanding claims provision | **276.1** | 252.7 |
| | | |
| Gross undiscounted central estimate | **526.8** | 732.6 |
| Claims settlement costs | **12.3** | 12.8 |
| | **539.1** | 745.4 |
| Discount to present value | **(16.1)** | (31.3) |
| Gross discounted central estimate | **523.0** | 714.1 |
| Less than 12 months | **277.0** | 299.4 |
| Greater than 12 months | **246.0** | 414.7 |
| Gross discounted central estimate | **523.0** | 714.1 |
| | | |
| Reinsurance and other recoveries on outstanding claims [1,2] | **295.2** | 523.2 |
| Discount to present value | **(10.0)** | (24.6) |
| Reinsurance and other recoveries on outstanding claims | **285.2** | 498.6 |
| Less than 12 months | **147.9** | 186.2 |
| Greater than 12 months | **137.3** | 312.4 |
| Reinsurance and other recoveries on outstanding claims | **285.2** | 498.6 |

1 Reinsurance and other recoveries on outstanding claims is shown net of a provision for impairment of nil (2013: nil).

2 To support reinsurance recoveries outstanding from a non-APRA authorised reinsurer, Letters of Credit (LOC's) have been issued to the company by Commonwealth Bank to the value of NZ$57.1 million ($38.8 million) (2013: $107.6 million) , Citibank to the value of $3.3 million, and NAB to the value of NZ$6.5 million ($5.1 million) (2013: $15.7 million). A Trust Deed has been set up between the company, related party and the Bank of New York Mellon, with the minimum account balance of $97.7 million for a related party recovery (2013: LOC's Citibank $134.6 million).

## 19. OUTSTANDING CLAIMS (CONTINUED)

### (B) Maturity profile of net outstanding claims provision

The expected maturity of the company's discounted net outstanding claims provision is analysed below.

| | | 1 YEAR OR LESS | 1 TO 2 YEARS | 2 TO 3 YEARS | 3 TO 4 YEARS | 4 TO 5 YEARS | OVER 5 YEARS | TOTAL |
|---|---|---|---|---|---|---|---|---|
| **At 31 December 2014** | **$M** | **150.3** | **60.9** | **28.3** | **19.7** | **7.5** | **9.4** | **276.1** |
| At 31 December 2013 | $M | 132.9 | 54.0 | 26.8 | 20.0 | 8.3 | 10.7 | 252.7 |

An analysis of the weighted average term to settlement of the claims provision is included in note 3(A)(iv).

### (C) Risk margin

The process used to determine the risk margin is explained in note 3(A)(iii) and details of the risk-free discount rates adopted are set out in note 3(A)(iv).

The risk margin included in net outstanding claims is 16.1% (2013: 17.3%) of the central estimate. The level of uncertainty in the net discounted central estimate at 31 December 2014 has reduced, mainly due to increased scale and lower volatility in New Zealand. As a consequence, the probability of adequacy at 31 December 2014 is 93.4% (2013: 93.8%) which is above APRA's 75% benchmark. Net profit after tax would have decreased by $0.7 million if the probability of adequacy was maintained at 93.8%.

### (D) Reconciliation of movement in discounted outstanding claims provision

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | OUTSTANDING CLAIMS $M | REINSURANCE $M | NET $M | OUTSTANDING CLAIMS $M | REINSURANCE $M | NET $M |
| At 1 January | **751.3** | **498.6** | **252.7** | 802.9 | 582.9 | 220.0 |
| Increase in net claims incurred in current accident year | **229.0** | **60.6** | **168.4** | 187.3 | 35.7 | 151.6 |
| Movement in prior year claims provision | **61.4** | **61.0** | **0.4** | 7.5 | 43.5 | (36.0) |
| Incurred claims recognised in profit or loss | **290.4** | **121.6** | **168.8** | 194.8 | 79.2 | 115.6 |
| Claim (payments) recoveries during the year | **(498.1)** | **(345.4)** | **(152.7)** | (340.4) | (224.6) | (115.8) |
| Foreign exchange (intercompany movement) | **17.7** | **10.4** | **7.3** | 94.0 | 61.1 | 32.9 |
| At 31 December | **561.3** | **285.2** | **276.1** | 751.3 | 498.6 | 252.7 |

## 19. OUTSTANDING CLAIMS (CONTINUED)

### (E) Claims development – undiscounted net central estimate

| | 2004 & prior $M | 2005 $M | 2006 $M | 2007 $M | 2008 $M | 2009 $M | 2010 $M | 2011 $M | 2012 $M | 2013 $M | 2014 $M | TOTAL $M |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Net central estimate** | | | | | | | | | | | | |
| Estimate of net ultimate claims cost at end of accident year | | 89.8 | 48.0 | 114.0 | 106.3 | 97.3 | 106.4 | 114.6 | 114.1 | 138.4 | 156.1 | 1,085.0 |
| One year later | | 92.2 | 89.8 | 97.9 | 103.4 | 94.9 | 109.0 | 115.2 | 106.6 | 145.9 | - | 954.9 |
| Two years later | | 85.6 | 85.8 | 89.5 | 105.3 | 91.3 | 104.9 | 109.6 | 107.2 | - | - | 779.2 |
| Three years later | | 87.9 | 94.3 | 90.7 | 106.9 | 89.1 | 104.5 | 108.1 | - | - | - | 681.5 |
| Four years later | | 84.6 | 94.0 | 90.1 | 164.1 | 90.1 | 105.5 | - | - | - | - | 628.4 |
| Five years later | | 85.1 | 91.9 | 88.5 | 105.1 | 88.6 | - | - | - | - | - | 459.2 |
| Six years later | | 85.3 | 90.8 | 88.4 | 105.9 | - | - | - | - | - | - | 370.4 |
| Seven years later | | 84.6 | 91.1 | 87.2 | - | - | - | - | - | - | - | 262.9 |
| Eight years later | | 84.1 | 90.5 | - | - | - | - | - | - | - | - | 174.6 |
| Nine years later | | 84.2 | - | - | - | - | - | - | - | - | - | 84.2 |
| Current estimate of net cumulative claims cost | | 84.2 | 90.5 | 87.2 | 105.9 | 88.6 | 105.5 | 108.1 | 107.2 | 145.9 | 156.1 | 1,079.2 |
| Cumulative net payments to date | | (83.6) | (89.7) | (85.2) | (102.0) | (80.9) | (97.8) | (94.9) | (84.7) | (98.0) | (53.4) | (870.2) |
| Net undiscounted central estimate | 13.1 | 0.7 | 0.8 | 2.0 | 3.9 | 7.7 | 7.7 | 13.2 | 22.5 | 47.9 | 102.7 | 222.2 |
| Foreign exchange | | | | | | | | | | | | 9.4 |
| Net undiscounted central estimate at 31 December 2014 | | | | | | | | | | | | 231.6 |
| Discount to present value | | | | | | | | | | | | (6.1) |
| Risk margin | | | | | | | | | | | | 38.3 |
| Claims settlement costs | | | | | | | | | | | | 12.3 |
| Other | | | | | | | | | | | | |
| **Net outstanding claims** | | | | | | | | | | | | 276.1 |
| **Movements in accident year claims estimate** | (1.1) | 0.1 | (0.8) | (1.2) | 0.8 | (1.5) | 1.0 | (1.5) | 0.6 | 7.5 | 156.1 | 160.2 |

A reconciliation of the net claims development to the net incurred claims in the income statement is included in note 6(C).

The company writes business in currencies other than the Australian dollar in its overseas operations. The translation of outstanding claims denominated in foreign currencies gives rise to foreign exchange movements which have no direct bearing on the development of the underlying claims. To eliminate this distortion, claims liabilities have been translated to the functional currencies of the company's overseas operations at constant rates of exchange. All estimates of net central estimate claims cost and cumulative claims payments for the ten most recent accident years reported in functional currencies other than Australian dollars have been translated to Australian dollars using the 2014 cumulative average rate of exchange.

The central estimate claims development table is presented net of reinsurance. With operations in 8 countries, hundreds of products, various reinsurance arrangements and with the company's risk tolerance managed on a consolidated net basis, it is considered neither meaningful nor practicable to provide this information other than on a net accident year basis.

## 20. PROVISIONS

| 2014 | PROVISION FOR LONG SERVICE LEAVE $M | OTHER PROVISIONS $M | TOTAL PROVISIONS $M |
|---|---|---|---|
| At 1 January | **0.2** | **2.1** | **2.3** |
| Other movement | **0.1** | **0.1** | **0.2** |
| At 31 December | **0.3** | **2.2** | **2.5** |
| Payable within 12 months | **0.1** | **2.2** | **2.3** |
| Payable in greater than 12 months | **0.2** | **-** | **0.2** |
| At 31 December | **0.3** | **2.2** | **2.5** |

| 2013 | PROVISION FOR LONG SERVICE LEAVE $M | OTHER PROVISIONS $M | TOTAL PROVISIONS $M |
|---|---|---|---|
| At 1 January | 0.2 | 0.1 | 0.3 |
| Other movement | - | 2.0 | 2.0 |
| At 31 December | 0.2 | 2.1 | 2.3 |
| Payable within 12 months | 0.1 | 1.9 | 2.0 |
| Payable in greater than 12 months | 0.1 | 0.2 | 0.3 |
| At 31 December | 0.2 | 2.1 | 2.3 |

## 21. EQUITY

### (A) Share capital

| 2014 | NUMBER OF SHARES MILLIONS | $M |
|---|---|---|
| Issued ordinary shares, fully paid at 1 January | **230.0** | **230.0** |
| Conversion of mandatory convertible notes | **26.6** | **91.2** |
| Issued ordinary shares, fully paid at 31 December | **256.6** | **321.2** |

| 2013 | NUMBER OF SHARES MILLIONS | $M |
|---|---|---|
| Issued ordinary shares, fully paid at 1 January | 230.0 | 230.0 |
| Issued ordinary shares, fully paid at 31 December | 230.0 | 230.0 |

### (B) Movements in share capital

Movement of $91.2 million (2013: nil) in share capital during the year was due to the conversion of mandatory convertible notes to ordinary shares.

### (C) Contributed equity

Ordinary shares in the company have no par value and entitle the holder to participate in dividends and the proceeds on winding up of the company in proportion to the number of and amounts paid on the shares held. Ordinary shareholders rank after all creditors and are entitled to any residual proceeds.

## 21. EQUITY (CONTINUED)

### (D) Reserves

| | 2014 $M | 2013 $M |
|---|---|---|
| **Realised capital profits** | | |
| At 1 January | **27.9** | 27.9 |
| At 31 December | **27.9** | 27.9 |
| **Foreign currency translation** | | |
| At 1 January | **17.5** | (25.3) |
| Other comprehensive income for the year | **12.8** | 42.8 |
| At 31 December | **30.3** | 17.5 |
| **Other** | | |
| At 1 January | **1.8** | 1.8 |
| At 31 December | **1.8** | 1.8 |
| **Total reserves at 31 December** | **60.0** | 47.2 |

### (E) Capital risk management

As a member of the wholly owned group, the company has adopted the risk management policies and framework of the QBE Group. QBE Group's objective when managing capital is to maintain an optimal balance of debt and equity in the capital structure to reduce the cost of capital whilst meeting capital adequacy requirements, providing security for policyholders and continuing to provide sufficient returns to shareholders.

Where appropriate, adjustments are made to capital levels in light of changes in economic conditions and risk characteristics of the company's activities. In order to maintain or adjust the capital structure, the company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or debt securities with capital characteristics, sell assets to reduce debt or adopt more conservative investment or reinsurance strategies.

The company is subject to, and complies with, various externally imposed regulatory capital requirements. These requirements are designed to ensure a sufficient solvency margin is maintained in order to provide adequate protection for policyholders. In addition, the company aims to maintain a strong credit rating and insurer financial strength rating, along with robust capital ratios in order to support its business objectives and maximise shareholder wealth.

The company uses an economic capital model (ECM) that is used across the QBE Group to assess the level of capital required for the underwriting, claims estimation, credit, market, liquidity and operational risks to which it is exposed. Economic capital is determined as the level of capital that the company needs to ensure that it can, with a pre-specified probability, satisfy its ultimate policyholder obligations in relation to all insurance contracts issued on or before the end of the business plan year. The ECM is used by management to help in the determination of the strategic capital allocation, business planning, underwriting performance, pricing, reinsurance and aggregate management. It also assists in determining regulatory capital. Capital across the QBE Group is allocated to business units, divisions and ultimately to underwriting portfolios according to the associated risk. The business plans include net asset projections, dividends, issued share projections and solvency projections as well as the impact of potential acquisitions. In the event of a significant change in the company's risk profile, the ECM will be recalculated and the results reported to the company's board.

## 21. EQUITY (CONTINUED)

### (E) Capital risk management (continued)

The company maintains an ongoing review of its structure to ensure flexibility in the allocation of capital whilst minimising the cost of capital. Active management of the business and its capital has enabled the company to maintain its insurer financial strength and credit rating, and has afforded it with good access to capital markets when needed.

Management monitors the company's capital levels on an ongoing basis, with particular focus on the following:

- The company actively manages the components of capital in order to maintain a level of eligible regulatory capital that exceeds APRA requirements. Having determined that the current risk appetite of the company remains appropriate, management has set the target level of regulatory capital for 2014 at around 1.8 - 2.2 times the Prescribed Capital Amount (PCA), including the full Insurance Concentration Risk Charge requirements which took effect 1 January 2014. Management monitors capital and solvency against capital target and annual rolling three years capital plans.
- The company is subject to regulatory requirements that a minimum level of capital is maintained to meet obligations to policyholders. It is the company's policy to maintain a capital base appropriate to its size, business mix, complexity and risk profile which fully complies with and meets or exceeds regulatory requirements.
- Insurer financial strength ratings provided by the major rating agencies which demonstrate our financial strength and claims paying ability.

In addition to the management reporting and planning processes, the company has dedicated staff responsible for understanding the regulatory capital requirements of its operations. The quality of assets (particularly investments and reinsurance recoveries) held by the company is continuously monitored to ensure any potential issues are identified and remedial action, where necessary, is taken to restore effective capital performance and levels.

## 22. MANDATORY CONVERTIBLE SECURITIES

| | 2014 $M | 2013 $M |
|---|---|---|
| **Mandatory convertible securities** | | |
| December 2046 NZ$102 million | - | 91.2 |

In December 2006, the company issued NZ$102 million of mandatory convertible notes to QBE Insurance Group Limited. The notes were transferred from QBE Insurance Group Limited to QBE Holdings (AAP) Pty Limited (the parent entity) in September 2007. The term of the notes is perpetual but they convert to ordinary shares of the company on the 40$^{th}$ anniversary of their issue.

The notes are subordinated and distributions are not cumulative. If a distribution is not paid, QBE Holdings (AAP) Pty Limited will have no claim in respect of non-payment. However, if a distribution is not paid within 20 business days of a distribution payment date, the mandatory convertible notes will convert into ordinary shares of the company.

In August 2014, mandatory convertible notes were converted to 26.6 million ordinary shares ($91.2million) as explained in note 21(B).

## 23. APRA CAPITAL ADEQUACY

Australian Prudential Regulation Authority (APRA) Prudential Standard GPS 110 Capital Adequacy for General Insurance requires that the company maintain a capital base in excess of its minimum capital requirement as defined under the Prudential Standards.

The following table shows the capital adequacy calculation in accordance with APRA prudential framework. The 2014 position reflects the 2014 quarter APRA return (unaudited).

| | 2014 $M | 2013 $M |
|---|---|---|
| **Eligible Tier 1 Capital as defined by APRA** | | |
| Contributed equity | **321.2** | 230.0 |
| Retained profit [1 2] | **189.8** | 160.3 |
| Insurance liability surplus | **31.5** | 20.3 |
| **Total equity** | **542.5** | 410.6 |
| Additional Tier 1 Capital | **-** | 82.1 |
| Less: APRA deductions | **(67.8)** | (61.8) |
| Total APRA capital base | **474.7** | 430.9 |
| APRA prudential capital requirement | **206.5** | 218.9 |
| APRA capital adequacy multiple | **2.29** | 1.97 |

1 Retained profits are in accordance with APRA Prudential Standards.
2 Dividends of $3.3 million were paid during the year (2013: $5.3 million).

## 24. KEY MANAGEMENT PERSONNEL

The names of persons who were directors of the company at any time during the financial year are as stated in the directors' report.

The key management personnel are all the directors of the company and the executives with the greatest authority for the strategic direction and management of the company.

Certain directors of the company are also directors of other subsidiaries of QBE Insurance Group Limited, the ultimate parent company. Their remuneration, which is paid by a related company, has been apportioned to the company on a basis consistent with the level of management effort.

Key management personnel compensation for the years ended 31 December 2014 and 2013 is set out below.

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| Short-term employee benefits | **6,190** | 5,834 |
| Post employment benefits | **409** | 247 |
| Other long-term employment benefits | **2** | 30 |
| Termination benefits | **672** | 195 |
| Share based payments | **178** | 232 |
| | **7,451** | 6,538 |

## 25. REMUNERATION OF AUDITORS

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| **PricewaterhouseCoopers (PwC) – Australian firm[1]** | | |
| Audit of financial reports | **214** | 215 |
| Audit of statutory returns | **108** | 119 |
| | **322** | 334 |
| **Related practices of PwC – Australian firm** | | |
| (including overseas PwC firms) | | |
| Audit of financial reports | **371** | 313 |
| Audit of statutory returns | **53** | 41 |
| Taxation services | **32** | 33 |
| Other consulting and advisory | **-** | 62 |
| | **456** | 449 |
| | **778** | 783 |
| Audit and assurance services | **746** | 688 |
| Other services | **32** | 95 |
| | **778** | 783 |

[1] The board believes some non-audit services are appropriate given the external auditor's knowledge of the Group. The company may engage the external auditor for non-audit services other than the excluded services subject to the general principle that fees for non-audit services should not exceed 50% of all fees paid to the external auditor in one financial year. External tax services are generally provided by an accounting firm other than the external auditor. Consistent with prior periods, PwC cannot provide the excluded services of preparing accounting records or financial reports, asset or liability valuations, acting in a management capacity, acting as a custodian of assets or acting as share registrar.

## 26. CONTINGENT LIABILITIES

| | 2014 $M | 2013 $M |
|---|---|---|
| The company had the following unsecured contingent liabilities: | | |
| Security deposit in overseas branch | **0.7** | 0.7 |
| Bankers guarantee to overseas branch | **1.0** | 1.6 |
| Guarantee to related entities | **14.6** | 13.4 |
| | **16.3** | 15.7 |

The bankers guarantee is in support of an overseas branch as required by local insurance regulators. The guarantee is in support of a related entity in the QBE Group to give the related entity a similar credit rating as the company.

No material losses are expected in relation to these guarantees.

## 27. CAPITAL EXPENDITURE COMMITMENTS

The company had no commitments for expenditure as at 31 December 2014 (2013: nil).

## 28. OPERATING LEASE COMMITMENTS

| | 2014 $M | 2013 $M |
|---|---|---|
| Payable: | | |
| Not later than one year | **4.1** | 4.2 |
| Later than one year but less than five years | **4.2** | 4.2 |
| Later than five years | **-** | 0.1 |
| Total future minimum lease payments under non-cancellable operating leases | **8.3** | 8.5 |

Lease commitments relate to property leases in the New Zealand and Singapore branch.

## 29. RELATED PARTIES

### (A) Parent entity

The parent entity is QBE Holdings (AAP) Pty Limited and the ultimate parent entity is QBE Insurance Group Limited.

### (B) Controlled entities

Interests in controlled entities are set out in note 15.

### (C) Transactions with related parties

The following material transactions occurred with related parties:

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| **Revenue** | | |
| Gross earned premium – inward reinsurance | **-** | 20 |
| Reinsurance and other recoveries - undiscounted | **26,077** | 17,704 |
| Reinsurance commission | **10,015** | 1,021 |
| Dividends received | **-** | 12,987 |
| Payments received for management services | **401** | 725 |
| **Expenses** | | |
| Outward reinsurance premium | **107,455** | 77,584 |
| Payments made for management services | **30,321** | 17,713 |
| **Other transactions** | | |
| Dividends paid | **3,377** | 5,253 |

### (D) Outstanding balances arising from transactions with related parties

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

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| **Current assets** | | |
| Reinsurance and other recoveries | **86,674** | 124,320 |
| Trade and other receivables | **32** | - |
| **Current liabilities** | | |
| Trade and other payables | **8,114** | 3,167 |

## 29. RELATED PARTIES (CONTINUED)

### (E) Terms and conditions

All transactions were made on normal commercial terms and conditions and at market rates. Outstanding balances are unsecured and repayable in cash, except for reinsurance recoveries that are secured by LOCs and Trust Deed as explained in note 19(A).

### (F) Other related party disclosures

All material information required to be disclosed under AASB 124: Related Party Disclosures has been included in the financial statements as follows:

| | Reference |
|---|---|
| Dividends from controlled entities | Note 5 |
| Interest received or receivable from controlled entities | Note 5 |
| Tax sharing agreement | Note 7(B) |
| Amounts due from controlled and related entities | Note 11 |
| Investments in controlled entities | Note 15 |
| Amounts due to controlled and related entities | Note 17 |
| Outstanding claims | Note 19 |
| Mandatory convertible securities | Note 22 |
| Remuneration of key management personnel | Note 24 |
| Guarantees in respect of related entities | Note 26 |

## 30. EVENTS OCCURRING AFTER REPORTING DATE

There is, at the date of this report, no matter or circumstance that has arisen since 31 December 2014 that has significantly affected, or may significantly affect:

(i) the company's operations in future financial years; or
(ii) the results of those operations in future financial years; or
(iii) the company's state of affairs in future financial years

**QBE INSURANCE (INTERNATIONAL) LIMITED**

**(A.C.N. 000 000 948)**

**DIRECTORS' DECLARATION**
For the year ended 31 December 2014

In the directors' opinion:

(a) the financial statements and notes set out on pages 5 to 61 are in accordance with the *Corporations Act 2001*, including:

(i) complying with accounting standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and

(ii) giving a true and fair view of the company's financial position as at 31 December 2014 and of its performance for the financial year ended on that date; and

(b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

Note1(A) confirms that the financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Signed in SYDNEY this 18 day of February 2015 in accordance with a resolution of the directors.

Director ..........................................     Director ..........................................

pwc

# Independent auditor's report to the members of QBE Insurance (International) Limited

## *Report on the financial report*

We have audited the accompanying financial report of QBE Insurance (International) Limited (the company), which comprises the balance sheet as at 31 December 2014, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes 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(A), the directors also state, in accordance with 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. Those 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 and fair presentation of the financial report 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 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*.

*PricewaterhouseCoopers, ABN 52 780 433 757*
*Darling Park Tower 2, 201 Sussex Street, GPO BOX 2650, SYDNEY NSW 1171*
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### *Auditor's opinion*

In our opinion:

(a) the financial report of QBE Insurance (International) 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 2014 and of its performance for the year ended on that date; and

  (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*.

(b) the company's financial report also complies with International Financial Reporting Standards as disclosed in Note 1(A).

PricewaterhouseCoopers
PricewaterhouseCoopers

R Balding
Partner

Sydney
18 February 2015

QBE

21 April 2015

QBE Insurance (International) Limited
ABN 11 000 000 948
Level 27, 8-12 Chifley Square
Sydney NSW 2000 Australia

Postal Address
GPO Box 82, Sydney NSW 2001
Telephone +612 9375 4444

Mr Terry Lawrence
Chief Financial Officer
QBE New Zealand
Level 9, AMP Centre
29 Customs Street West
Auckland

Dear Mr Lawrence

**Re: QBE Insurance (International) Limited Appointed Actuary's Report as at 31 December 2014**

Section 77 and 78 of the Reserve Bank of New Zealand's Insurance (Prudential Supervision) Act 2010, dated 1 December 2014, requires a licensed insurer to ensure that actuarial information contained in the financial statements or group financial statements has been reviewed by the insurer's Appointed Actuary.

QBE New Zealand (QBENZ) is a branch of QBE Insurance (International) Limited (QBEI), an entity regulated by Australian Prudential Regulation Authority (APRA). As the Appointed Actuary for QBEI, I, Jack Jiang, have conducted this review for QBEI's financial statements for the period ending 31 December 2014.

Since 2012, QBENZ is managed as part of the Australia New Zealand division, and accordingly the actuarial valuation is carried out by the actuarial team in Sydney. Actuarial reserve review for year ended 2014 was conducted by Mr Benoit Laganiere and I rely on the actuarial information provided in the following report:

- QBE New Zealand Insurance Liabilities as at 31 December 2014, prepared by Benoit Laganiere

This review involved ascertaining whether actuarial information used in the preparation of the financial statements has applied appropriately.

For the purposes of this review, actuarial information include

- Outstanding claims liabilities
- Premium liabilities
- Application of the Liability Adequacy Test
- Reinsurance and other recoveries
- Deferred acquisition costs

No limitations were placed on me in conducting this review, and all information requested has been made available to me.

I am an employee of QBE General Insurance (Hong Kong) Limited, which is a related company to QBENZ in that both companies are fully owned by QBE Insurance Group. My remuneration is partly dependent on the profitability of QBEI.

From my review, it is my opinion that

- the actuarial information included in QBEI's financial statements has been appropriately included;
- the actuarial information used in the preparation of QBEI's financial statements has been used appropriately; and
- from a solvency point of view, QBEI has held capital in excess of APRA's Minimum Capital requirements as at 31 December 2014.

Yours sincerely

Jack Jiang

Jack Jiang
Appointed Actuary for QBE Insurance (International) Limited
Fellow of the Institute of Actuaries of Australia

**QBE INSURANCE (INTERNATIONAL) LIMITED**

**NEW ZEALAND BRANCH**

**FINANCIAL REPORT – 31 DECEMBER 2014**

**INDEX**

**QBE INSURANCE (INTERNATIONAL) LIMITED**
**New Zealand Branch**

**STATEMENT BY DIRECTORS**
For the year ended 31 December 2014

We, being two directors of QBE Insurance (International) Limited, certify that the Statement of Comprehensive Income, Balance Sheet, Statement of Changes in Balances Due To Head Office, Statement of Cash Flows and notes set out on pages 4 to 38 are true copies of the Financial Statements of the New Zealand Branch of the Company for the year ended 31 December 2014.

The Board of Directors of QBE Insurance (International) Limited authorised these statements for issue on

the 18 day of FEBRUARY 2015.

DIRECTOR:

DIRECTOR:

# *Independent Auditors' Report*

to the Directors of QBE Insurance (International) Limited New Zealand Branch

### *Report on the Financial Statements*

We have audited the financial statements of QBE Insurance (International) Limited New Zealand Branch ("the Branch") on pages 4 to 38, which comprise the balance sheet as at 31 December 2014, the statement of comprehensive income and statement of changes in balances due to head office and cash flow statement for the year then ended, and the notes to the financial statements that include a summary of significant accounting policies and other explanatory information.

### *Directors' Responsibility for the Financial Statements*

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

### *Auditors' Responsibility*

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

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

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

Our firm carries out other services for the Branch in the area of tax compliance and advisory services. Appropriate safeguards were applied to reduce the threats to independence from the provision of other services to an acceptable level. The provision of these services has not impaired our independence as auditors of the Branch.

# *Independent Auditors' Report*

QBE Insurance (International) Limited New Zealand Branch

### *Opinion*

In our opinion, the financial statements on pages 4 to 38:

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

(ii) comply with International Financial Reporting Standards ; and

(iii) give a true and fair view of the financial position of the Branch as at 31 December 2014, and its financial performance and cash flows for the year then ended.

## *Report on Other Legal and Regulatory Requirements*

We also report in accordance with Sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993. In relation to our audit of the financial statements for the year ended 31 December 2014:

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

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

## *Restriction on Use of our Report*

This report is made solely to the Directors of the Branch, as a body. Our audit work has been undertaken so that we might state to the Directors of the Branch those matters which we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Directors of the Branch, as a body, for our audit work, for this report or for the opinions we have formed.

Chartered Accountants
18 February 2015

Auckland

**QBE INSURANCE (INTERNATIONAL) LIMITED**
**New Zealand Branch**

**STATEMENT OF COMPREHENSIVE INCOME**
For the year ended 31 December 2014

| | NOTE | 2014 $000's | 2013 $000's |
|---|---|---|---|
| Gross written premium | | **324,967** | 325,352 |
| Unearned premium movement | | **(5,139)** | (9,386) |
| Gross earned premium revenue | | **319,828** | 315,966 |
| Outward reinsurance premium | | **(146,780)** | (150,067) |
| Deferred reinsurance premium movement | | **(6,754)** | (5,033) |
| Outward reinsurance premium expense | | **(153,534)** | (155,100) |
| Net earned premium | | **166,294** | 160,866 |
| Gross claims incurred | 8 | **(184,152)** | (113,963) |
| Reinsurance and other recoveries revenue | 8 | **108,533** | 57,753 |
| Net claims incurred | 8 | **(75,619)** | (56,210) |
| Gross commission expense | | **(38,899)** | (44,297) |
| Reinsurance commission revenue | | **15,101** | 9,580 |
| Net commission | | **(23,798)** | (34,717) |
| Deferred acquisition cost movement | | **-** | 1,104 |
| Underwriting expenses | 6 | **(44,184)** | (39,552) |
| Underwriting profit | | **22,693** | 31,491 |
| Sundry income | | **1,122** | 1,448 |
| Investment income | 7 | **13,717** | 10,570 |
| Other expense | 7 | **(12,239)** | (6,727) |
| Profit before income tax | | **25,293** | 36,782 |
| Income tax expense | 9 | **(9,470)** | (10,389) |
| **Profit for the year attributable to Head Office Account** | | **15,823** | 26,393 |
| Other comprehensive income after income tax | | **-** | - |
| **Total comprehensive income for the year attributable to Head Office Account** | | **15,823** | 26,393 |

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



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**QBE INSURANCE (INTERNATIONAL) LIMITED**
**New Zealand Branch**

**BALANCE SHEET**
As at 31 December 2014

| | NOTE | 2014 $000's | 2013 $000's |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and cash equivalents | 10 | **16,515** | 6,443 |
| Investments | 11 | **343,623** | 351,390 |
| Trade and other receivables | 12 | **135,397** | 123,941 |
| Deferred insurance costs | 13 | **39,319** | 43,509 |
| Reinsurance and other recoveries on outstanding claims | 18 | **244,810** | 490,777 |
| Property, plant and equipment | 14 | **1,637** | 2,152 |
| Deferred tax assets | 15 | **650** | 320 |
| Total assets | | **781,951** | 1,018,532 |
| **LIABILITIES** | | | |
| Trade and other payables | 16 | **31,139** | 141,936 |
| Current tax liabilities | | **4,529** | 4,469 |
| Unearned premium | 17 | **182,929** | 177,790 |
| Outstanding claims | 18 | **364,576** | 608,370 |
| Deferred tax liabilities | 15 | **8,199** | 7,477 |
| Total liabilities | | **591,372** | 940,042 |
| Net assets | | **190,579** | 78,490 |
| **Due to Head Office – Australia** | 20 | **190,579** | 78,490 |

The balance sheet should be read in conjunction with the accompanying notes.

**QBE INSURANCE (INTERNATIONAL) LIMITED**
**New Zealand Branch**

**STATEMENT OF CHANGES IN BALANCES DUE TO HEAD OFFICE**
For the year ended 31 December 2014

| HEAD OFFICE – AUSTRALIA | NOTE | 2014 $000's | 2013 $000's |
|---|---|---|---|
| Balance as at 1 January | | **78,490** | 46,619 |
| Profit for the year | | **15,823** | 26,393 |
| Total comprehensive income | | **15,823** | 26,393 |
| Loan settlement | 26 | **102,000** | - |
| Current transactions with Head Office | | **(5,734)** | 5,478 |
| **Balance at 31 December** | 20 | **190,579** | 78,490 |

The statement of changes in balances due to Head Office should be read in conjunction with the accompanying notes.



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**QBE INSURANCE (INTERNATIONAL) LIMITED**
**New Zealand Branch**

**STATEMENT OF CASH FLOWS**
For the year ended 31 December 2014

| | NOTE | 2014 $000's | 2013 $000's |
|---|---|---|---|
| **OPERATING ACTIVITIES** | | | |
| Premium received | | **324,258** | 316,912 |
| Reinsurance and other recoveries received | | **340,765** | 266,583 |
| Outwards reinsurance paid | | **(135,681)** | (146,616) |
| Claims paid | | **(427,946)** | (326,055) |
| Insurance costs paid | | **(26,362)** | (35,681) |
| Interest received | | **10,014** | 7,734 |
| Other operating income | | **3,040** | 381 |
| Other operating payments | | **(57,117)** | (23,219) |
| Income taxes paid | | **(9,018)** | (7,864) |
| Net cash flows from operating activities | 10 | **21,953** | 52,175 |
| **INVESTING ACTIVITIES** | | | |
| Proceeds on sale of investments | | **931,799** | 717,024 |
| Payments for purchase of investments | | **(920,329)** | (793,811) |
| Payments for purchase of plant and equipment | | **(250)** | (800) |
| Net cash flows from investing activities | | **11,220** | (77,587) |
| **FINANCING ACTIVITIES** | | | |
| Interest paid | | **(3,636)** | (5,960) |
| Withholding tax and related expense | | **(8,144)** | - |
| Parent company settlements | | **(11,321)** | - |
| Net cash flows from financing activities | | **(23,101)** | (5,960) |
| Net movement in cash and cash equivalents | | **10,072** | (31,372) |
| Cash and cash equivalents at the beginning of the financial year | | **6,443** | 37,815 |
| Cash and cash equivalents at the end of the financial year | 10 | **16,515** | 6,443 |

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

## NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2014

## 1. GENERAL INFORMATION

QBE Insurance (International) Limited (sometimes referred to as the Parent or Head Office), is a company incorporated in Australia and operates in New Zealand as a branch (the Branch).

The Branch is an insurer providing general insurance services. It is based at 29 Customs Street West, Auckland.

The financial statements of the Branch are for the year ended 31 December 2014 and were authorised for issue by the directors on the 18th day of February 2015.

The Branch's owners do not have the power to amend these financial statements once issued.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

### (A) Basis of preparation

The financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable financial reporting standards, as appropriate for profit oriented entities. The Branch is a profit oriented entity registered under the Companies Act 1993. It is a reporting entity for the purposes of the Financial Reporting Act 1993. The financial statements are prepared in accordance with the requirements of the Financial Reporting Act 1993 and the Companies Act 1993.

The financial statements of the Branch comply with International Financial Reporting Standards (IFRS).

The Branch is an issuer under the Financial Reporting Act 1993 as it is a Licenced Insurer under the Insurance (Prudential Supervision) Act 2010.

**Historical cost convention**

These financial statements have been prepared under the historical cost convention, as modified by certain exceptions noted in the financial report, with the principal exceptions being the measurement of financial assets at fair value and the measurement of the outstanding claims liability and related reinsurance and other recoveries at present value.

The preparation of the financial statements requires the use of certain critical accounting estimates. It also requires management to exercise judgement in the process of applying the Branch's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions or estimates are significant, are disclosed in note 4.

### (B) Unearned premium

Unearned premium is calculated based on the term of the risk and in accordance with the expected pattern of the incidence of risks underwritten, using the daily pro-rata method or the 24ths method.

At each balance sheet date, the adequacy of the unearned premium liability is assessed on a net of reinsurance basis against the present value of the expected future cash flows relating to potential future claims in respect of the relevant insurance contracts, plus an additional risk margin to reflect the inherent uncertainty of the central estimate. If the present value of the expected future cash flows relating to future claims plus the additional risk margin exceeds the unearned premium liability less related intangible assets and related deferred acquisition costs, then the unearned premium liability is deemed to be deficient. The resulting deficiency is recognised immediately through the profit or loss.



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### (C) Premium revenue

Premium comprises amounts charged to policyholders, excluding taxes collected on behalf of third parties. The earned portion of premium received and receivable, including unclosed business, is recognised as revenue. Premium on unclosed business is brought to account based upon the pattern of booking of renewals and new business.

### (D) Outward reinsurance

Premium ceded to reinsurers is recognised as an expense from the attachment date over the period of indemnity of the reinsurance contract in accordance with the expected pattern of the incidence of risk. Accordingly, a portion of outward reinsurance premium is treated as deferred reinsurance premium at the balance sheet date.

### (E) Claims

The provision for outstanding claims is measured as the central estimate of the present value of expected future claims payments plus a risk margin. The expected future payments include those in relation to claims reported but not yet paid; claims incurred but not reported (IBNR); claims incurred but not enough reported (IBNER); and estimated claims handling costs. Claims expense represents claim payments adjusted for the movement in the outstanding claims liability.

The expected future payments are discounted to present value using a risk-free rate.

A risk margin is applied to the central estimate, net of reinsurance and other recoveries, to reflect the inherent uncertainty in the central estimate.

### (F) Reinsurance and other recoveries

Reinsurance and other recoveries on paid claims, reported claims not yet paid, IBNR and IBNER are recognised as revenue.

Amounts recoverable are assessed in a manner similar to the assessment of outstanding claims. Recoveries are measured as the present value of the expected future receipts, calculated on the same basis as the provision for outstanding claims.

### (G) Acquisition costs

Acquisition costs (which include commission costs) are the costs associated with obtaining and recording insurance contracts. Acquisition costs are capitalised when they relate to the acquisition of new business or the renewal of existing business and are referred to as deferred acquisition costs. These costs are amortised on the same basis as the earning pattern of the premium, over the period of the insurance contract to which they relate. At the reporting date, deferred acquisition costs represent the capitalised costs that relate to the unearned premium. Acquisition costs are deferred in recognition of their future benefit and are measured at the lower of cost and recoverable amount.

### (H) Investment income

Interest income is recognised on an accruals basis. Dividends are recognised when the right to receive payment is established. Investment income includes realised and unrealised gains or losses on financial assets which are reported on a combined basis as net fair value gains or losses on financial assets in the Statement of Comprehensive Income.

### (I) Taxation

The income tax expense for the year is the tax payable on the current year's taxable income, adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements.

Deferred tax is provided in full, using the liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements.

Deferred tax assets and liabilities are recognised for temporary differences at the tax rate expected to apply when the assets are recovered or liabilities are settled. The relevant tax rates are applied to the cumulative amounts of deductible and taxable temporary differences to measure the deferred tax asset or liability. An exception is made for certain temporary differences arising from the initial recognition of an asset or liability. No deferred tax asset or liability is recognised in relation to these temporary differences if they arose in a transaction that is not a business combination and at the time did not affect either accounting profit or taxable loss.

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

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities. Current tax assets and liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability on a net basis, or to realise the asset and settle the liability simultaneously.

**(J) Cash and cash equivalents**
Cash and cash equivalents includes cash at bank and on hand and deposits at call which are readily convertible to cash on hand and which are used for operational cash requirements.

**(K) Investments**
Investments comprise interest-bearing assets. Investments are designated as at fair value through profit or loss on initial recognition. They are initially recorded at fair value, being the cost of acquisition excluding transaction costs, and are subsequently remeasured to fair value at each reporting date. The policy of management is to designate a group of financial assets or financial liabilities as at fair value through profit or loss when that group is both managed and its performance evaluated on a fair value basis for both internal and external reporting in accordance with the Branch's documented investment strategy.

Fixed and floating rate securities are valued using independently sourced valuations.

All purchases and sales of investments that require delivery of the asset within the time frame established by regulation or market convention ("regular way" transactions) are recognised at trade date, being the date on which the Branch commits to buy or sell the asset. Investments are derecognised when the right to receive future cash flows from the asset has expired or has been transferred and the Branch has transferred substantially all the risks and rewards of ownership.

**(L) Trade and other receivables**
Trade and other receivables are recognised at amount receivable less a provision for impairment. A provision for impairment is established when there is objective evidence that the Branch will not be able to collect all amounts due according to the original term of the receivable. Any increase or decrease in the provision for impairment is recognised in profit or loss within underwriting expenses. When a receivable is uncollectible, it is written off against the provision for impairment account. Subsequent recoveries of amounts previously written off are credited against underwriting expenses in profit or loss.

**(M) Property, plant and equipment**
All property, plant and equipment is stated at historical cost less depreciation and impairment. Plant and equipment is depreciated using the diminishing value method over the estimated useful life of each class of asset. Estimated useful lives are between three and ten years.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Branch and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the Statement of Comprehensive Income during the financial period in which they are incurred.

The assets residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'underwriting expenses' in the Statement of Comprehensive Income.

**(N) Impairment of assets**
Assets that have an indefinite useful life are tested annually for impairment or more frequently when changes in circumstances indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised as the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped in cash generating units which are the lowest levels for which there are separately identifiable cash flows.

**(O) Trade and other payables**
Trade and other payables are measured at cost and are settled under standard terms and conditions. Related party payables are measured at cost and are repayable on demand.

**(P) Foreign currency**
**(i) Functional and presentation currency**
The Branch's financial statements are presented in New Zealand dollars, being the functional and presentation currency of the Branch.

**(ii) Translation of foreign currency transactions and balances**
Foreign currency transactions are translated into New Zealand dollars at the spot rates of exchange applicable at the dates of the transactions. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated at the rates of exchange prevailing at that date. Resulting exchange gains and losses are included in profit or loss.

**(iii) Hedging transactions**
Derivatives may be used to hedge the foreign exchange risk relating to certain transactions.

**(Q) Employee benefits**
**(i) Superannuation**

The Branch contributes to a privately administered pension plan on a mandatory, contractual or voluntary basis. The Branch has no obligation once the contributions have been paid. All contributions are recognised as an employee expense when they are due.

**(ii) Share based payment**

The employees of the branch participate in an equity settled share based compensation plan of QBE Insurance Group Limited. The fair value of the employee services received in exchange for the grant of those instruments is recognised as an expense.

**(iii) Other**

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

The liability for employee entitlements is carried at the present value of the estimated future cash flows.



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

**(S) Goods and services tax (GST)**
The Statement of Comprehensive Income has been prepared so that all components are stated exclusive of GST. All items in the Statement of Financial Position are stated net of GST, with the exception of receivables and payables, which include GST invoiced.

**(T) Rounding of amounts**
Amounts in the financial statements have been rounded off in the financial statements to the nearest one thousand dollars.

**(U) Comparatives**
Where necessary, prior period comparative information has been amended to achieve consistency in disclosure with the current year.

## 3. NEW ACCOUNTING STANDARDS AND AMENDMENTS

The following standards, amendments and interpretations to existing standards which have been published and are mandatory for the Branch's accounting periods beginning on or after 1 January 2014 have not been early adopted:

- NZ IFRS 9, Financial Instruments effective 1 January 2018. Introduces changes in the classification and measurement of financial assets and liabilities. Not expected to have a material impact on the financial statements.

The Branch has adopted the following new standards as of 1 January 2014:

- Amendment to IAS 32, Financial Instruments Presentation effective 1 January 2014. Clarifies some of the requirements for offsetting financial assets and liabilities in the balance sheet. Not expected to have a material impact on the financial statements.
- Amendment to IAS 36, Impairment of Assets effective 1 January 2014. Addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. Not expected to have a material impact on the financial statements.
- Amendment to IAS 39, Financial Instruments: Recognition and measurement effective 1 January 2014. Addresses the novation of derivatives and hedge accounting. Not expected to have a material impact on the financial statements.
- NZ IFRIC 21, Levies effective 1 January 2014. Not expected to have a material impact on the financial statements.

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Branch makes estimates and assumptions in respect of certain key assets and liabilities. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Estimates of the outstanding claims as at 31 December 2014 has been carried out by Kon Makris, Fellow of the Institute of Actuaries of Australia.

The actuarial assessments are in accordance with the standards of the New Zealand Society of Actuaries. The Actuary is satisfied as to the nature, sufficiency and accuracy of the data used to determine the outstanding claims liability.

The outstanding claims liability is set at a level that is appropriate and sustainable to cover the Group's obligations after having regard to the prevailing market environment and prudent industry practice.

The key areas in which critical estimates and judgments are applied are described as follows:

### (A) Outstanding claims provision

The Branch's net outstanding claims provision comprises:

- the gross central estimate of expected future claims payments;
- amounts recoverable from reinsurers based on the gross central estimate;
- a reduction to reflect the discount to present value using risk-free rates of return to reflect the time value of money; and
- a risk margin that reflects the inherent uncertainty in the net discounted central estimate.

A net discounted central estimate is intended to represent the mean of the distribution of the expected future cash flows. As the Branch requires a higher probability that estimates will be adequate over time, a risk margin is added to the net discounted central estimate to determine the outstanding claims provision.

### (i) Central estimates

The provision for expected future payments includes those in relation to claims reported but not yet paid; claims incurred but not reported (IBNR); claims incurred but not enough reported (IBNER); and estimated claims handling costs, being the indirect expenses incurred in the settlement of claims.

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 Branch, where more information about the claims is generally available. Liability and other long tail classes of business, where claims settlement may not happen for many years after the event giving rise to the claim, typically display greater variability between initial estimates and final settlement due to delays in reporting claims, uncertainty in respect of court awards and future claims inflation. Claims in respect of property and other short tail classes are typically reported and settled sooner after the claim event, giving rise to more certainty. The estimation techniques and assumptions used in determining the central estimate are described below.

The Branch's process for establishing the central estimate involves extensive consultation with internal and external actuaries, claims managers, underwriters and other senior management. This process includes half yearly internal claims provisioning committee meetings attended by the senior management and the Appointed Actuary and detailed review by external actuaries at least annually. The risk management procedures related to the actuarial function are explained further in note 5.

The determination of the amounts that the Branch will ultimately pay for claims arising under insurance and reinsurance contracts involves a number of critical assumptions. Some of the uncertainties impacting these assumptions are as follows:

- changes in patterns of claims incidence, reporting and payment;
- volatility in the estimation of future costs for long tail insurance classes due to the longer period of time that elapses before a definitive determination of the ultimate claims cost can be made;
- incidence of catastrophic events close to the balance sheet date;
- changes in the legal environment, including the interpretation of liability laws and the quantum of damages; and
- social and economic trends, for example price and wage inflation and interest rates.

The potential impact of changes in key assumptions used in the determination of the central estimate and the probability of adequacy of the central estimate on the Branch's profit or loss are summarised in note 4(A)(v).

Central estimates for each class of business are determined by reference to a variety of estimation techniques, generally based on a statistical analysis of historical experience which assumes an underlying pattern of claims development and payment. The final selected central estimates are based on a judgmental consideration of the results of each method and qualitative information, for example, the class of business, the maturity of the portfolio and the expected term to settlement of the class. Projections are based on both historical experience and external benchmarks where relevant.

Central estimates are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts recoverable from reinsurers based on the gross central estimate.

The net central estimate is discounted at risk-free rates of return to reflect the time value of money. Details of the key assumptions applied in the discounting process are summarised in note 4(A)(iv).

**(ii) Assets arising from contracts with reinsurers**
Assets arising from contracts with the Branch's reinsurers are determined using the same methods described above. In addition, the recoverability of these assets is assessed at each balance sheet date to ensure that the balances properly reflect the amounts that will ultimately be received, taking into account counterparty credit risk and the contractual terms of the reinsurance contract. Counterparty and credit risk in relation to reinsurance assets is considered in note 5(C)(ii).

**(iii) Risk margin**
Risk margins are determined by management and are held to mitigate the potential for uncertainty in the central estimate. The determination of the appropriate level of risk margin takes into account similar factors to those used to determine the central estimate, such as:

- change in the mix of business, in particular the mix of short tail and long tail business and the overall weighted average term to settlement;
- prior accident year claims development; and
- the level of uncertainty in the net discounted central estimate due to actuarial estimation, data quality issues, variability of key discount and inflation assumptions and legislative uncertainty.

The variability by class of business uses techniques similar to those used in determining the central estimate. These techniques determine a range of possible outcomes of ultimate payments and assign a likelihood to outcomes at different levels. These techniques use standard statistical distributions, and the measure of variability is referred to as the coefficient of variation.

The appropriate risk margin for two or more classes of business combined is likely to be less than the sum of the risk margins for the individual classes. This reflects the benefit of diversification in general insurance. The statistical measure used to determine diversification is called the correlation. The higher the correlation between two classes of business, the more likely it is that a negative outcome in one class will correspond to a negative outcome in the other class.

The risk margin for the Branch is determined by analysing the variability of each class of business and the correlation between classes of business and divisions. Correlations are determined for aggregations of classes of business. Whilst there are estimation techniques for determining correlations, they are difficult to apply. The correlations adopted by the Branch are normally derived from industry analysis and the judgement of experienced and qualified actuaries.

The probability of adequacy is a statistical measure of the relative adequacy of the outstanding claims provision and is derived from the comparison of the risk margin with the net discounted central estimate. Using a range of outcomes, it allows a determination of the probability of adequacy represented by a risk margin. For example, a 90% probability of adequacy indicates that the outstanding claims provision is expected to be adequate nine times in ten. The appropriate level of risk margin is not determined by reference to a fixed probability of adequacy.

**(iv) Financial assumptions used to determine the outstanding claims provision**
**Discount rates**
NZ IFRS 4 Insurance Contracts requires that the outstanding claims provision shall be discounted for the time value of money using risk-free rates that are based on current observable, objective rates that relate to the nature, structure and terms of the future obligations. The standard also states that government bond rates may be an appropriate starting point in determining a risk-free rate. The Branch generally uses currency specific risk-free rates to discount the outstanding claims provision.

The discount rates used in the measurement of outstanding claims and reinsurance recoveries for the succeeding year was 3.54% (2013: 2.90%) and subsequent years were 3.56% – 3.76% (2013: 3.29% – 4.70%).

**Weighted average term to settlement**
The relevant discount rate is applied to the anticipated cash flow profile of the central estimate, including related reinsurance recoveries, determined by reference to a combination of historical analysis and current expectations of when claims and recoveries will be settled. The weighted average term to settlement of the Branch's claims provision is 1.47 years (2013: 1.6 years).

**(v) Impact of changes in key variables on the outstanding claims provision**
The impact of changes in key variables used in the calculation of the outstanding claims provision is summarised in the table below. Each change has been calculated in isolation from the other changes and each change shows the after tax impact on profit assuming that there is no change to any of the other variables. In practice, this is considered unlikely as, for example, an increase in interest rates is normally accompanied by an increase in the rate of inflation.

The sensitivities below assume that all changes directly impact profit after tax. In practice, however, it is likely that if the central estimate was to increase by 5%, at least part of the increase would result in a decrease in the probability of adequacy. Likewise, if the coefficient of variation were to increase by 1%, it is likely that the probability of adequacy would reduce from its current level and that the change would therefore impact the amount of risk margins held rather than net profit after income tax or equity.

The impact of a change in interest rates on profit after tax due to market value movement on fixed interest securities is shown in note 5(D)(ii).

| | MOVEMENT IN VARIABLE % | FINANCIAL IMPACT PROFIT (LOSS)[1] 2014 $000's | 2013 $000's |
|---|---|---|---|
| Inflation rates | increase of 1% | (1,013) | (1,153) |
| | decrease of 1% | 995 | 1,130 |
| Discount rates | increase of 1% | 915 | 1,081 |
| | decrease of 1% | (949) | (1,124) |
| Claims expenses ratio | increase of 1% | (1,018) | (658) |
| | decrease of 1% | 1,018 | 658 |
| Weighted average term to settlement | +0.5 years | 1,172 | 1,169 |
| | -0.5 years | (1,192) | (1,189) |

Determined at the Branch level net of reinsurance and taxation

[1] Net of tax at the Branch's prima facie rate of 28%

**(B) Liability adequacy test**
At each balance sheet date, the adequacy of the unearned premium liability is assessed on a net of reinsurance basis against the present value of the expected future cash flows relating to potential future claims, plus a risk margin to reflect the inherent uncertainty of the central estimate. Future claims are those claims expected to arise from claims events occurring after the balance sheet date. The assessment is carried out using the same methods described in note 4(A) above and 17(B).

## 5. RISK MANAGEMENT

QBE Group's risk management policy, strategy and framework are embedded in the head office and in each of the divisional operations and business units within each of the divisions, ensuring a consistent approach to managing risk across the organisation. The board annually approves a comprehensive risk management strategy (RMS), including a risk appetite statement and a reinsurance management strategy (REMS).

As a member of the QBE Group, the Branch has adopted the risk management policy of QBE Group where applicable. The Branch's risk management objectives are to:

- achieve competitive advantage through better understanding the risk environment in which QBE operates;
- optimise risk and more effectively allocate resources by assessing the balance of risk and reward; and
- avoid unwelcome surprises by reducing uncertainty and volatility.

It is QBE Group's policy to adopt a rigorous approach to managing risk throughout each of the divisions and business units. Risk management is a continuous process and an integral part of quality business management. QBE Group's approach is to integrate risk management into the broader management processes of the organisation. It is QBE Group's philosophy to ensure that risk management remains embedded in the business and that the risk makers or risk takers are themselves the risk managers. Specifically, the management of risk must occur at each point in the business management cycle.

Risk management is a key part of our governance structure and our strategic and business planning. It underpins the setting of limits and authorities and it is embedded in the monitoring and evaluation of performance. This holistic approach to risk management allows all of the Branch's risks to be managed in an integrated manner.

QBE Group's global risk management framework defines the risks that QBE Group is exposed to and sets out the framework to manage those risks and meet strategic objectives whilst taking into account the creation of value of our shareholders. The framework is made up of complementary elements that are embedded throughout the business management cycle and culture. Key aspects include: governance, risk appetite and tolerance, delegated authorities, risk policies, measurement and modelling, risk and control self assessment, risk treatment, optimisation and ongoing improvement through management action plans, risk and performance monitoring.

A fundamental part of the Branch's overall risk management strategy is the effective governance and management of the risks that impact the amount, timing and uncertainty of cash flows from insurance contracts. The operating activities of the Branch expose it to risks such as market risk, credit risk and liquidity risk. The branch's risk management framework recognises the unpredictability of financial markets and seeks to minimise potential adverse effects on its financial performance. The Branch has established internal controls to manage risk in the key areas of exposure relevant to its business.

The Branch's risk profile is described under the following broad risk categories:

- Strategic risk
- Insurance risk
- Credit risk
- Market risk
- Liquidity risk
- Operational risk
- Group risk

Each of these is described more fully in sections (A) to (G) below.

### (A) Strategic risk

Strategic risk refers to the current and prospective impact on earnings and or capital arising from strategic business decisions, implementation of decisions and responsiveness to external change. This includes risks associated with business strategy and change, tax planning, investment strategy and corporate governance. Of particular relevance is capital management risk.

### Capital management risk

The Branch is subject to extensive prudential and other forms of regulation in the jurisdictions in which they conduct business. Prudential regulation is generally designed to protect policyholders. Regulation covers a number of areas including solvency, change in control and capital movement limitations. The regulatory environment in NZ, Australia and overseas continues to evolve in response to economic, political and industry developments. QBE Group works closely with regulators and monitors regulatory developments across its global operations to assess their potential impact on its ability to meet solvency and other requirements.

**(B) Insurance risk**

Insurance risk is the risk of fluctuations in the timing, frequency and severity of insured events and claims settlements, relative to the expectations at the time of underwriting. This includes underwriting, catastrophe, claims concentration and claims estimation risks. The risks inherent in any single insurance contract are the possibility of the insured event occurring and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, these risks are random and unpredictable. In relation to the pricing of individual insurance contracts and the determination of the level of the outstanding claims provision in relation to a portfolio of insurance contracts, the principal risk is that the ultimate claims payments will exceed the carrying amount of the provision established.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability around the expected outcome will be. In addition, a more diversified insurance Branch is less likely to be affected by a change in any one specific portfolio. The Branch has developed its underwriting strategy to diversify the type of insurance risks accepted, and where possible, within each of these categories, to achieve a sufficiently large population of risks to reduce the variability of the expected outcome.

QBE Group has established the following protocols to manage its insurance risk across the underwriting, claims and outwards reinsurance.

**(i) Underwriting risks**

**Selection and pricing of risks**

Underwriting authority is delegated to experienced underwriters for the forthcoming year following a detailed retrospective and prospective analysis of each class of business as part of the Branch's annual business planning process. Delegated authorities reflect the level of risk which the Branch allows. The authorities include reference to some combination of:

- return on risk adjusted equity;
- gross written premium;
- premium per contract;
- sum insured per contract;
- aggregate exposures per zone;
- probable maximum loss and realistic disaster scenarios (RDS);
- levels and quality of reinsurance protection;
- geographic exposures; and/or
- classes of business and types of product that may be written.

Limits in respect of each of the above are set at a portfolio and Branch level and are included within business plans for individual classes of business. They are adjusted to reflect a risk factor in respect of previous underwriting results, the economic environment and other potential drivers of volatility.

Insurance and reinsurance policies are written in accordance with the Branch's management practices and New Zealand regulations taking into account the Branch's risk appetite and tolerance and underwriting standards. Non-standard and long-term policies may only be written if expressly included in the delegated authorities. No individual long-term or non-standard policy is material to the Branch.

Pricing of risks is controlled by the use of in-house pricing models relevant to specific portfolios. Experienced underwriters and actuaries maintain historical pricing and claims analysis for each portfolio and this is combined with a detailed knowledge of the current developments in the respective markets and classes of business.

**Concentration risk**

The Branch's exposure to concentrations of insurance risk is mitigated by a portfolio diversified by multiple classes of business. Product diversification is achieved through a strategy of developing strong underwriting skills in a wide variety of classes of business.

The Branch has potential exposure to catastrophe losses. The Branch undertakes probable maximum loss modelling to ensure the Branch operates within its tolerance to concentration risk.

**(ii) Claims management and claims estimation risks**
The Branch's approach to determining the outstanding claims provision and the related sensitivities are set out in note 4. The Branch seeks to ensure the adequacy of its outstanding claims provision by reference to the following controls:

- experienced claims managers work with underwriters on coverage issues and operate within the levels of authority delegated to them in respect of the settlement of claims;
- processes exist to ensure that all claims advices are captured and updated on a timely basis with a realistic assessment of the ultimate claims cost;
- initial IBNR estimates are set by experienced internal actuaries in conjunction with the local product managers and underwriters for each class of business in each business unit. The valuation of the central estimate is primarily performed by actuaries who are not involved in the pricing function and who therefore provide an independent assessment;
- the determination of the risk margin is performed by senior management and the Board with input from the Appointed Actuary;
- the aggregate outstanding claims provision is assessed in a series of quarterly internal claims review meetings which are attended by senior management and the Appointed Actuary in order to ensure consistency of provisioning practices across all countries; and
- all of the Branch's central estimate is reviewed by external actuaries at least annually.

Despite the rigour involved in the establishment and review of the outstanding claims provision, the provision is subject to significant uncertainty for the reasons provided in note 4.

**(iii) Reinsurance**
Reinsurance is purchased to make the Branch's results more predictable by reducing the effect that individual large claims, and catastrophic events that lead to multiple claims, have on results. The majority of reinsurance will be arranged on a non proportional excess of loss treaty basis. Facultative cover will only be used where the inclusion of certain risks in the treaty would have an undue effect on the treaty or where there was a specific exposure that could not be covered under the treaty.

The Branch's strategy in respect of the selection, approval and monitoring or reinsurance arrangements is addressed by the following protocols:

- Placement of appropriate treaty or facultative reinsurance is governed by the Branch's reinsurance management strategy and Group committee guidelines.

- Reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historic losses and potential future losses based on realistic disaster scenarios.

The quality of the Branch's exposure to reinsurance counterparties is actively monitored at Branch level with reference to detailed counterparty analysis prepared using age of balance and rating agency analysis.

**(C) Credit risk**
Credit risk is the risk of default by transactional counterparties as well as the loss of value of assets due to deterioration in credit quality. Exposure to credit risk results from financial transactions with securities issuers, debtors, brokers, policyholders and reinsurers.

The Branch's credit risk arises mainly from investment and reinsurance protection activities. The following policies and procedures are in place to mitigate the Branch's exposure to credit risk:

- A QBE Group-wide investment credit risk policy is in place which defines what constitutes credit risk for QBE group and establishes tolerance levels. Compliance with the policy is monitored and exposures and breaches are reported to the QBE Group investment committee.
- Net exposure limits are set for each counterparty or group of counterparties in relation to investments, cash deposits and forward foreign exchange exposures. The policy also sets out minimum credit ratings for investments.
- QBE Group has strict guidelines covering the limits and terms of net open derivative positions and the counterparties with which the Branch may transact. The Branch does not expect any investment counterparties to fail to meet their obligations given their strong credit ratings and therefore does not require collateral or other security to support derivatives.
- Credit risk in respect of premium debtors and reinsurance receivables is actively monitored. Strict controls are maintained over counterparty exposures. Business is transacted with counterparties that have a strong credit rating and concentration of risk is managed by adherence to counterparty limits. The provision for impairment is formally assessed by management at least four times a year.

**(i) Credit quality of financial assets**

The following tables provide information regarding the Branch's aggregate credit risk exposure at the balance sheet date in respect of the major classes of financial assets. Trade and other receivables are excluded from this analysis on the basis that they comprise of smaller credit risk items which generally cannot be rated and are not individually or in aggregate, material. The analysis classifies the assets according to Moody's counterparty credit ratings. Aaa is the highest possible rating.

| | CREDIT RATING | | | |
|---|---|---|---|---|
| | Aaa $000's | Aa $000's | A $000's | TOTAL $000's |
| **At 31 December 2014** | | | | |
| Cash and cash equivalents | - | **16,132** | **383** | **16,515** |
| Interest bearing investments | **44,320** | **299,303** | - | **343,623** |
| **At 31 December 2013** | | | | |
| Cash and cash equivalents | - | 6,208 | 235 | 6,443 |
| Interest bearing investments | 24,821 | 326,569 | - | 351,390 |

The carrying amount of the relevant asset classes in the balance sheet represents the maximum amount of credit exposure.

The following table provides information regarding the ageing of the Branch's financial assets that are past due at the balance sheet date.

| | PAST DUE BUT NOT IMPAIRED $000's | PAST DUE BUT NOT IMPAIRED: 0 TO 3 MTHS $000's | 3 TO 6 MTHS $000's | 6 MTHS TO 1 YEAR $000's | GREATER THAN 1 YEAR $000's | TOTAL $000's |
|---|---|---|---|---|---|---|
| **At 31 December 2014** | | | | | | |
| Amounts due from related entities | **15** | - | - | - | - | **15** |
| Premium receivable [1] | **53,981** | **4,237** | **(685)** | **(12)** | - | **57,521** |
| Other debtors | **8,017** | - | - | - | - | **8,017** |
| **At 31 December 2013** | | | | | | |
| Amounts due from related entities | 980 | - | - | - | - | 980 |
| Premium receivable [1] | 61,469 | 5,035 | 81 | - | - | 66,585 |
| Other debtors | 9,935 | - | - | - | - | 9,935 |

[1] Net of a provision for impairment

**(ii) Reinsurance counterparty credit risk**

The Branch's objective is to maximise placement of reinsurance with highly rated counterparties. Concentration of risk with reinsurance counterparties is monitored strictly and regularly by the divisional security committee and is controlled by reference to the following protocols:

- Treaty or facultative reinsurance is placed in accordance with the requirements of the Branch's reinsurance management strategy and Group security committee guidelines.
- Reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historic losses and potential future losses and the Branch's maximum event retention.
- Exposure to reinsurance counterparties and the credit quality of those counterparties is actively monitored.

The following table provides information about the quality of the Branch's credit risk exposure in respect of undiscounted reinsurance and other recoveries on outstanding claims at the balance sheet date. The analysis classifies the assets according to Standard and Poors counterparty ratings. AAA is the highest possible rating.

| | | CREDIT RATING: AAA $000's | AA $000's | A $000's | BBB $000's | NOT RATED $000's | TOTAL $000's |
|---|---|---|---|---|---|---|---|
| Reinsurance recoveries on outstanding claims[1] | **2014** | - | **104,146** | **150,643** | **225** | **1** | **255,015** |
| | 2013 | - | 263,618 | 252,623 | 548 | 1 | 516,790 |
| Reinsurance recoveries on paid claims[1] | **2014** | - | **25,579** | **5,032** | **39** | | **30,650** |
| | 2013 | - | 12,580 | 4,336 | - | - | 16,916 |

[1] Net of a provision for impairment.

There are no amounts past due. (2013: nil)

**(D) Market risk**

Market risk is the risk of variability in the value of, and returns on, investments and the risk associated with variability of interest rates, foreign exchange rates and economy-wide inflation on both assets and liabilities, excluding insurance liabilities.



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Market risk comprises three types of risk: currency risk (due to fluctuations in foreign exchange rates); interest rate risk (due to fluctuations in market interest rates); and price risk (due to fluctuations in market prices). Within each of these categories, risks are evaluated before considering the effect of mitigating controls. The existence and effectiveness of such mitigating controls are then measured to ensure that residual risks are managed within the Branch's risk appetite and tolerance.

### (i) Currency risk

The Branch's exposure to currency risk generally arises as a result of the translation of foreign currency amounts back to the functional currency of the Branch. There is no material currency risk exposure to the Branch.

### (ii) Interest rate risk

Financial instruments with floating interest rate expose the Branch to cash flow interest rate risk, whereas fixed interest rate instruments expose the Branch to fair value interest rate risk.

QBE Group's risk management approach is to minimise interest rate risk by actively managing investment portfolios to achieve a balance between cash flow interest rate risk and fair value interest rate risk. The Branch invests in high quality, liquid interest-bearing securities and cash and actively manages the duration of the fixed interest portfolio.

The claims provision is discounted to present value by reference to risk-free interest rates. The Branch is therefore exposed to potential underwriting result volatility as a result of interest rate movements. In practice, however, an increase or decrease in interest rates is normally offset by a corresponding increase or decrease in inflation. Details are provided in note 4(A)(v). QBE Group has a policy of maintaining a relatively short duration for assets backing insurance liabilities in order to minimise any further potential volatility affecting insurance profit.

The contractual maturity profile of the Branch's interest-bearing financial assets and hence its exposure to interest rate risk, and the effective weighted average interest rate for interest-bearing financial assets is analysed in the table below. The table includes investments at the maturity date of the security; however, many of the longer dated securities have call dates of relatively short duration.

| | | INTEREST – BEARING FINANCIAL ASSETS MATURING IN | | | | | |
|---|---|---|---|---|---|---|---|
| | | 1 YEAR OR LESS | 1 TO 2 YEARS | 2 TO 3 YEARS | 3 TO 4 YEARS | 4 TO 5 YEARS | TOTAL |
| **At 31 December 2014** | | | | | | | |
| Fixed rate | $000's | **26,302** | **25,000** | **37,692** | **11,030** | **43,449** | **143,473** |
| Weighted average interest rate | % | **3.66%** | **4.83%** | **4.37%** | **4.52%** | **4.46%** | **4.04%** |
| Floating rate | $000's | **163,961** | **34,189** | **11,357** | **7,158** | **-** | **216,665** |
| Weighted average interest rate | % | **3.29%** | **4.07%** | **4.18%** | **4.38%** | **-** | **3.78%** |
| **At 31 December 2013** | | | | | | | |
| Fixed rate | $000's | 54,585 | 16,701 | - | - | - | 71,286 |
| Weighted average interest rate | % | 2.85% | 3.53% | 0% | 0% | 0% | 2.89% |
| Floating rate | $000's | 196,106 | 39,896 | 27,851 | 14,514 | 8,180 | 286,547 |
| Weighted average interest rate | % | 2.78% | 3.19% | 3.30% | 3.44% | 3.54% | 3.19% |

All financial assets are measured at fair value through profit or loss. Movements in interest rates impact the value of interest-bearing financial assets and therefore impact reported profit after tax. The impact of a 0.5% increase or decrease in interest rates on interest-bearing financial assets owned by the Branch at the balance sheet date is shown in the table below.

| | | PROFIT/(LOSS) & EQUITY[1] | |
|---|---|---|---|
| | SENSITIVITY | 2014 | 2013 |
| | % | $000's | $000's |
| Interest rate movement – interest-bearing financial assets | +0.50 | **(1,849)** | (354) |
| | -0.50 | **1,849** | 354 |

[1] Net of tax at the Branch's prima facie rate of 28%

**(iii) Price risk**

Price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded on the market.

At 31 December 2014, the Branch did not hold any investments in listed equities (2013: nil). The branch is exposed to price risk on its investment in corporate fixed interest and floating rate securities. All corporate securities are measured at fair value through profit or loss. Movements in credit spreads impact the value of corporate fixed interest and floating rate securities and therefore impact reported profit after tax. The profit/(loss) impact in $000's of a plus or minus 0.5% change in credit spreads is ($1,635) – $1,527. 2013 ($1,008) – $980.



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### (E) Liquidity risk

Liquidity risk is the risk of insufficient liquid assets to meet liabilities as they fall due to policyholders and creditors. This includes the risk associated with asset liability management. The key objective of the Branch's asset and liability management strategy is to ensure sufficient liquidity is maintained at all times to meet the Branch's obligations including its settlement of insurance liabilities and, within these parameters, to optimise investment returns for the Parent.

Liquidity must be sufficient to meet both planned and unplanned cash requirements. The Branch is exposed to liquidity risk mainly through its obligations to make payments in relation to its insurance activities.

In addition to treasury cash held for working capital requirements, and in accordance with the Branch's liquidity policy, a minimum percentage of investments and cash is held in liquid, short-term money market securities to ensure that there are sufficient liquid funds available to meet insurance obligations. The Branch has a strong liquidity position. The maturity of the Branch's interest-bearing financial assets is included in note 5(D)(ii).

The Branch may limit the risk of liquidity shortfalls resulting from mismatches in the timing of claims payments and receipts of claims recoveries by negotiating cash call clauses in reinsurance contracts and seeking accelerated settlements for large reinsurance recoveries.

The Branch has no significant concentration of liquidity risk.

The maturity profile of the Branch's net outstanding claims provision is analysed in note 18(B). All other financial liabilities have a contractual maturity profile of 1 year or less.

### (F) Operational risk

Operational risk is the risk of financial loss resulting from inadequate or failed internal processes, people and systems or from external events (including legal risk). The Branch manages operational risk within the same robust risk management framework as its other risks. The risk assessment and monitoring framework involves on-going:

- identification and review of the key risks to the Branch;
- definition of the acceptable level of risk appetite and tolerance;
- assessment of those risks throughout the Branch in terms of the acceptable level of risk (risk tolerance) and the residual risk remaining after having considered risk treatment;
- assessment of whether each risk is within the acceptable level of risk, or requires appropriate action be taken to mitigate any excess risk;
- transparent monitoring and reporting of risk management related matters on a timely basis; and
- alignment of internal audit programs with risks.

One of the cornerstones of the Branch's risk management framework is the recruitment and retention of high quality people who are entrusted with appropriate levels of autonomy within the parameters of disciplined risk management practices.

The Branch operates a system of delegated authorities based on expertise and proven performance, and compliance is closely monitored. Other controls include effective segregation of duties, access controls and authorisation and reconciliation procedures.

### (G) Group risk

Group risk is the risk to the Branch arising specifically from being part of the Group, including the financial impact and loss of support from the parent company.

## 6. UNDERWRITING EXPENSES

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Depreciation – leasehold improvements | **381** | 96 |
| Depreciation – property, plant & equipment | **383** | 323 |
| Employee benefit expenses | **28,127** | 26,997 |
| Lease and rental charges | **1,808** | 1,712 |
| Loss on sale of property, plant and equipment | **1** | 4 |
| Provision for doubtful debts | **412** | 15 |
| Head office charges | **7,539** | 5,969 |
| Retirement plan contributions | **1,365** | 1,131 |
| Other expenses | **4,168** | 3,305 |
| | **44,184** | 39,552 |

## 7. INVESTMENT INCOME AND OTHER EXPENSE

| | 2014 $000's | 2013 $000's |
|---|---|---|
| **Investment income** | | |
| Interest received or receivable | **10,014** | 7,911 |
| Net fair value gains on financial assets | **3,703** | 2,659 |
| | **13,717** | 10,570 |
| **Other expense** | | |
| Interest expense | **(3,636)** | (5,960) |
| Withholding tax and related expense | **(8,144)** | - |
| Foreign exchange (losses)/profit | **(139)** | (454) |
| Investment expenses | **(320)** | (313) |
| | **(12,239)** | (6,727) |

The Branch has potential exposures in relation to certain historic taxation matters regarding which the Commissioner of Inland Revenue has issued a Notice of Proposed Adjustment. The quantum of tax proposed by the Commissioner is $8,936,000 before any available deductions. The Branch has estimated the use of money interest to be between $2,000,000 - $3,000,000 before any available deductions. The Branch continues to dispute this matter having obtained professional advice.

## 8. CLAIMS INCURRED

### (A) Claims analysis

| | 2014 $000's | 2013 $000's |
|---|---|---|
| **Gross claims incurred and related expenses** | | |
| Direct | **184,152** | 113,963 |
| **Reinsurance and other recoveries** | | |
| Direct | **(108,533)** | (57,753) |
| Net claims incurred | **75,619** | 56,210 |

### (B) Claims development

Current year's claims relate to risks borne in the current reporting year. Prior year claims relate to a reassessment of the risks borne in all previous reporting years and include releases of risk margins as claims are paid.

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | CURRENT YEAR $000's | PRIOR YEARS $000's | TOTAL $000's | CURRENT YEAR $000's | PRIOR YEARS $000's | TOTAL $000's |
| **Gross claims incurred and related expenses** | | | | | | |
| Undiscounted | **104,497** | **63,138** | **167,635** | 94,866 | 15,613 | 110,479 |
| Discount | **(3,160)** | **19,677** | **16,517** | (2,986) | 6,470 | 3,484 |
| | **101,337** | **82,815** | **184,152** | 91,880 | 22,083 | 113,963 |
| **Reinsurance and other recoveries** | | | | | | |
| Undiscounted | **38,806** | **53,919** | **92,725** | 28,746 | 25,750 | 54,496 |
| Discount | **(1,329)** | **17,137** | **15,808** | (967) | 4,224 | 3,257 |
| | **37,477** | **71,056** | **108,533** | 27,779 | 29,974 | 57,753 |
| **Net claims incurred** | | | | | | |
| Undiscounted | **65,691** | **9,219** | **74,910** | 66,120 | (10,137) | 55,983 |
| Discount | **(1,831)** | **2,540** | **709** | (2,019) | 2,246 | 227 |
| | **63,860** | **11,759** | **75,619** | 64,101 | (7,891) | 56,210 |

### (C) Reconciliation of net claims incurred to claims development table

The development of the net outstanding claims for the 10 most recent accident years is shown in note 18(E). This note is a reconciliation of the amounts included in the table in note 8(B) and the current financial year movements in the claims development table.

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | CURRENT YEAR $000's | PRIOR YEARS $000's | TOTAL $000's | CURRENT YEAR $000's | PRIOR YEARS $000's | TOTAL $000's |
| Net undiscounted claims development – central estimate (note 18 (E)) | **55,905** | **14,839** | **70,744** | 53,734 | 2,055 | 55,789 |
| Movement in claims settlement costs | **1,965** | **2,201** | **4,166** | 4,553 | (3,924) | 629 |
| Movement in discount | **(1,831)** | **2,540** | **709** | (2,019) | 2,246 | 227 |
| Movement in risk margin | **7,821** | **(7,821)** | **-** | 7,833 | (8,268) | (435) |
| **Net claims incurred – discounted** | **63,860** | **11,759** | **75,619** | 64,101 | (7,891) | 56,210 |

## 9. INCOME TAX EXPENSE

### Reconciliation of prima facie tax to income tax expense

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Profit before income tax | **25,293** | 36,782 |
| Prima facie tax payable at 28% | **7,082** | 10,299 |
| Tax effect of non-temporary differences: | | |
| Non-allowable expenses and non-taxable income | **2,366** | 67 |
| Prima facie tax adjusted for non-temporary differences | **9,448** | 10,366 |
| Under provision in prior years | **22** | 23 |
| Income tax expense | **9,470** | 10,389 |
| Analysed as follows: | | |
| Current tax | **9,078** | 8,478 |
| Deferred tax | **392** | 1,911 |
| | **9,470** | 10,389 |
| Deferred tax expense comprises: | | |
| Deferred tax assets recognised in profit or loss | **(330)** | 958 |
| Deferred tax liabilities recognised in profit or loss | **722** | 953 |
| | **392** | 1,911 |

## 10. CASH AND CASH EQUIVALENTS

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Cash at bank and on hand | **16,515** | 6,443 |

Amounts in cash and cash equivalents are the same as those included in the cash flow statement.

Cash and cash equivalents include balances readily convertible to cash. All balances are held to service normal operational requirements.

### Reconciliation of profit after income tax to net cash flows from operating activities

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Profit after income tax | **15,823** | 26,393 |
| Depreciation of property, plant and equipment | **764** | 419 |
| Fair value movement of financial assets | **(3,703)** | (2,659) |
| Loss on sale of plant and equipment | **1** | 4 |
| Interest expense | **3,636** | 5,960 |
| Withholding tax and related expense | **8,144** | - |
| Movement in trade and other payables | **(8,944)** | 14,989 |
| Movement in trade and other receivables | **(11,456)** | (3,954) |
| Movement in net outstanding claims | **2,173** | (9,332) |
| Movement in unearned premiums | **5,139** | 9,287 |
| Movement in deferred insurance costs | **4,190** | 2,965 |
| Movement in tax balances | **452** | 2,525 |
| Movement in Head Office account | **5,734** | 5,478 |
| Net cash flows from operating activities | **21,953** | 52,175 |

## 11. INVESTMENTS

| | 2014 $000's | 2013 $000's |
|---|---|---|
| **Fixed interest rate** | | |
| Short term money | **25,000** | 25,000 |
| Government bonds | **17,245** | 7,374 |
| Corporate bonds | **101,228** | 38,912 |
| | **143,473** | 71,286 |
| **Floating interest rate** | | |
| Short term money | **124,383** | 174,630 |
| Floating rate notes | **75,767** | 105,474 |
| | **200,150** | 280,104 |
| Total investments | **343,623** | 351,390 |
| Amounts maturing within 12 months | **173,748** | 244,248 |
| Amounts maturing in greater than 12 months | **169,875** | 107,142 |
| Total investments | **343,623** | 351,390 |

**Valuation of investments**
All investments are initially recorded at fair value and are subsequently remeasured to fair value at each reporting date.

**Short-term money**
Term deposits are valued at par plus accrued interest and are classified as level 1. Other short-term money (bank bills, certificates of deposit, treasury bills and other short-term instruments) are priced using interest rates and yield curves observable at commonly quoted intervals.

**Fixed and floating rate bonds**
Bonds which are traded in active markets and have quoted prices from external data providers are classified as level 1. Bonds which are not traded in active markets are priced using broker quotes, using comparable prices for similar instruments or using pricing techniques set by local regulators or exchanges.

**Fair value hierarchy**
The investments of the Branch are disclosed in the table below using a fair value hierarchy which reflects the significance of inputs into the determination of fair value as follows:

**Level 1**: Valuation is based on quoted prices in active markets for similar instruments.

**Level 2**: Valuation is based on quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data, for example, consensus price using broker quotes and valuation model with observable inputs.

**Level 3:** Valuation techniques are applied for which any significant input is not based on observable market data. There were no level 3 investments.

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | LEVEL 1 $000's | LEVEL 2 $000's | TOTAL $000's | LEVEL 1 $000's | LEVEL 2 $000's | TOTAL $000's |
| Short-term money | **25,065** | **124,318** | **149,383** | 25,128 | 174,502 | 199,630 |
| Government bonds | **17,245** | **-** | **17,245** | 7,374 | - | 7,374 |
| Corporate bonds/other | **-** | **176,995** | **176,995** | - | 144,386 | 144,386 |
| Total investments | **42,310** | **301,313** | **343,623** | 32,502 | 318,888 | 351,390 |

## 12. TRADE AND OTHER RECEIVABLES

| | 2014 $000's | 2013 $000's |
|---|---|---|
| **Trade debtors** | | |
| Premium receivable[1] | **57,521** | 66,585 |
| Reinsurance and other recoveries[1] | **30,650** | 16,916 |
| Unclosed premium | **38,549** | 28,776 |
| | **126,720** | 112,277 |
| Amounts due from related entities (Note 26) | **15** | 980 |
| Other debtors | **8,017** | 9,935 |
| Prepayments | **645** | 749 |
| Trade and other receivables | **135,397** | 123,941 |
| Receivable within 12 months | **135,397** | 123,941 |
| Receivable in greater than 12 months | **-** | - |
| Trade and other receivables | **135,397** | 123,941 |

[1] Net of a provision for impairment

### (A) Provision for general impairment

| | PREMIUM RECEIVABLE | | REINSURANCE AND OTHER RECOVERIES | |
|---|---|---|---|---|
| | 2014 $000's | 2013 $000's | 2014 $000's | 2013 $000's |
| At 1 January | **145** | 106 | **-** | 24 |
| Amounts recognised in profit or loss | **390** | 39 | **22** | (24) |
| At 31 December | **535** | 145 | **22** | - |

### (B) Fair value

Due to the short term nature of these receivables, their carrying value is assumed to approximate their fair value.

### (C) Risk

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivables. No receivables are pledged by the Branch as collateral for liabilities or contingent liabilities. Information on the ageing and credit rating of balances in the table above, where relevant, is included in note 5(C). Note 5 also provides more information on the risk management policies of the Branch.

## 13. DEFERRED INSURANCE COSTS

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Deferred reinsurance premium | **9,985** | 16,739 |
| Deferred commission | **20,228** | 17,664 |
| Deferred acquisition costs | **9,106** | 9,106 |
| Deferred insurance costs | **39,319** | 43,509 |
| To be expensed within 12 months | **36,920** | 41,797 |
| To be expensed in greater than 12 months | **2,399** | 1,712 |
| Deferred insurance costs | **39,319** | 43,509 |



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| | DEFERRED REINSURANCE PREMIUM | | DEFERRED COMMISSION | | DEFERRED ACQUISITION COSTS | |
|---|---|---|---|---|---|---|
| | 2014 $000's | 2013 $000's | 2014 $000's | 2013 $000's | 2014 $000's | 2013 $000's |
| At 1 January | **16,739** | 21,772 | **17,664** | 16,700 | **9,106** | 8,002 |
| Costs deferred in financial year | **9,148** | 15,722 | **19,637** | 16,742 | **8,759** | 9,106 |
| Amortisation of costs deferred in previous financial years | **(15,903)** | (20,755) | **(17,073)** | (15,778) | **(8,759)** | (8,002) |
| At 31 December | **9,984** | 16,739 | **20,228** | 17,664 | **9,106** | 9,106 |

## 14. PROPERTY, PLANT AND EQUIPMENT

| 2014 | LEASEHOLD IMPROVEMENTS $000's | IT/OFFICE EQUIPMENT/ FIXTURES & FITTINGS $000's | TOTAL $000's |
|---|---|---|---|
| **Cost or valuation** | | | |
| At 1 January | **1,494** | **3,828** | **5,322** |
| Additions | **-** | **256** | **256** |
| Disposals | **-** | **(248)** | **(248)** |
| At 31 December | **1,494** | **3,836** | **5,330** |
| **Accumulated depreciation and impairment losses** | | | |
| At 1 January | **(756)** | **(2,414)** | **(3,170)** |
| Disposals | **-** | **241** | **241** |
| Depreciation charge for the year | **(381)** | **(383)** | **(764)** |
| At 31 December | **(1,137)** | **(2,556)** | **(3,693)** |
| **Carrying amount** | | | |
| At 31 December | **357** | **1,280** | **1,637** |

| 2013 | LEASEHOLD IMPROVEMENTS $000's | IT/OFFICE EQUIPMENT/ FIXTURES & FITTINGS $000's | TOTAL $000's |
|---|---|---|---|
| **Cost or valuation** | | | |
| At 1 January | 1,462 | 3,176 | 4,638 |
| Additions | 32 | 767 | 799 |
| Disposals | - | (115) | (115) |
| At 31 December | 1,494 | 3,828 | 5,322 |
| **Accumulated depreciation and impairment losses** | | | |
| At 1 January | (661) | (2,201) | (2,862) |
| Disposals | 1 | 110 | 111 |
| Depreciation charge for the year | (96) | (323) | (419) |
| At 31 December | (756) | (2,414) | (3,170) |
| **Carrying amount** | | | |
| At 31 December | 738 | 1,414 | 2,152 |

## 15. DEFERRED INCOME TAX

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Deferred tax assets | **650** | 320 |
| Deferred tax liabilities | **(8,199)** | (7,477) |
| | **(7,549)** | (7,157) |

### (A) Deferred tax assets
### (i) The balance comprises temporary differences attributable to:

| | 2014 $000's | 2013 $000's |
|---|---|---|
| **Amounts recognised in profit or loss** | | |
| Provision for impairment | **156** | 41 |
| Employee benefits | **342** | 272 |
| Other | **152** | 7 |
| Deferred tax assets | **650** | 320 |
| | | |
| **Deferred tax assets analysed as follows:** | | |
| Recoverable within 12 months | 650 | 320 |
| Recoverable in greater than 12 months | - | - |
| | 650 | 320 |

### (ii) Movements

| | 2014 $000's | 2013 $000's |
|---|---|---|
| At 1 January | **320** | 1,278 |
| Amounts recognised in profit or loss | **330** | (958) |
| At 31 December | **650** | 320 |

### (B) Deferred tax liabilities
### (i) The balance comprises temporary differences attributable to:

| | 2014 $000's | 2013 $000's |
|---|---|---|
| **Amounts recognised in profit or loss** | | |
| Insurance provisions | **(8,199)** | (7,477) |
| Deferred tax liabilities | **(8,199)** | (7,477) |
| | | |
| **Deferred tax liabilities analysed as follows:** | | |
| Payable within 12 months | **(8,199)** | (7,477) |
| Payable in greater than 12 months | - | - |
| | **(8,199)** | (7,477) |

### (ii) Movements:

| | 2014 $000's | 2013 $000's |
|---|---|---|
| At 1 January | **(7,477)** | (6,524) |
| Amounts recognised in profit or loss | **(722)** | (953) |
| At 31 December | **(8,199)** | (7,477) |

## 16. TRADE AND OTHER PAYABLES

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Trade payables | **8,790** | 5,718 |
| Amounts due to related entities (Note 26) | **180** | 102,033 |
| Other payables | **19,840** | 27,374 |
| Accrued expenses | **2,329** | 6,811 |
| Trade and other payables | **31,139** | 141,936 |
| Payable within 12 months | **31,139** | 39,936 |
| Payable in greater than 12 months | **-** | 102,000 |
| Trade and other payables | **31,139** | 141,936 |

## 17. UNEARNED PREMIUM

### (A) Unearned premium

| | 2014 $000's | 2013 $000's |
|---|---|---|
| At 1 January | **177,790** | 168,403 |
| Deferral of premium on contracts written in the period | **176,876** | 170,247 |
| Earning of premium written in previous periods | **(171,737)** | (160,860) |
| At 31 December | **182,929** | 177,790 |
| To be earned within 12 months | **175,714** | 172,003 |
| To be earned in greater than 12 months | **7,215** | 5,787 |
| Unearned premium | **182,929** | 177,790 |

### (B) Liability adequacy test

The probability of adequacy of the unearned premium liability differs from the probability of adequacy adopted in determining the outstanding claims provision. The reason for the difference is that the former is a benchmark used only to test the sufficiency of net unearned premium liabilities whereas the latter is a measure of the adequacy of the outstanding claims provision actually carried by the Branch.

NZ IFRS requires the inclusion of a risk margin in insurance liabilities, but does not prescribe a minimum level of margin. Whilst there is established practice in the calculation of the probability of adequacy of the outstanding claims provisions, no such guidance exists in respect of the level of risk margin to be used in determining the adequacy of net premium liabilities. The Branch has adopted a risk margin of 7.8% (2013: 7.8%) for premium liabilities, for the purposes of the liability adequacy test to produce a 75% probability of adequacy in respect of total insurance liabilities. The 75% basis is a recognised industry benchmark in New Zealand and Australia.

The application of the liability adequacy test in respect of net unearned premium liabilities identified a surplus at 31 December 2014 and 31 December 2013.

## 18. OUTSTANDING CLAIMS

### (A) Net outstanding claims

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Gross outstanding claims provision | **341,432** | 585,226 |
| Risk margin | **23,144** | 23,144 |
| Outstanding claims | **364,576** | 608,370 |
| Reinsurance and other recoveries on outstanding claims | **(244,810)** | (490,777) |
| Net outstanding claims provision | **119,766** | 117,593 |
| **Analysed as follows:** | | |
| Net undiscounted central estimate | **101,574** | 100,110 |
| Discount to present value | **(4,952)** | (5,661) |
| Net discounted central estimate | **96,622** | 94,449 |
| Risk margin | **23,144** | 23,144 |
| Net outstanding claims provision | **119,766** | 117,593 |
| | | |
| Gross undiscounted central estimate | **383,400** | 635,627 |
| Claim settlement accrual | **(3,667)** | 4,417 |
| | **379,733** | 640,044 |
| Discount to present value | **(15,157)** | (31,674) |
| Gross discounted central estimate | **364,576** | 608,370 |
| Less than 12 months | **179,092** | 227,065 |
| Greater than 12 months | **185,484** | 381,305 |
| Gross discounted central estimate | **364,576** | 608,370 |
| | | |
| Reinsurance and other recoveries on outstanding claims | **255,015** | 516,790 |
| Discount to present value | **(10,205)** | (26,013) |
| Reinsurance and other recoveries on outstanding claims | **244,810** | 490,777 |
| Less than 12 months | **121,265** | 173,797 |
| Greater than 12 months | **123,545** | 316,980 |
| Reinsurance and other recoveries on outstanding claims | **244,810** | 490,777 |

### (B) Maturity profile of net outstanding claims provision

The expected maturity of the Branch's discounted net outstanding claims provision is analysed below.

| | | 1 YEAR OR LESS | 1 TO 2 YEARS | 2 TO 3 YEARS | 3 TO 4 YEARS | 4 TO 5 YEARS | OVER 5 YEARS | TOTAL |
|---|---|---|---|---|---|---|---|---|
| **At 31 December 2014** | **$000's** | **61,620** | **30,163** | **13,979** | **6,974** | **3,799** | **3,231** | **119,766** |
| At 31 December 2013 | $000's | 53,268 | 28,999 | 18,576 | 7,895 | 4,396 | 4,459 | 117,593 |

The weighted average term to settlement of the claims provision is included in note 4(A)(iv).

### (C) Risk margin

The process used to determine the risk margin is explained in note 4(A)(iii) and details of the risk-free discount rates adopted are set out in note 4(A)(iv).

The risk margin included in net outstanding claims is 24% (2013: 24.5%) of the central estimate. The increase in the risk margin reflects increased uncertainty in the net discounted central estimate at 31 December 2014. Assumptions regarding uncertainty for each business class were applied to the central estimates, allowing for diversification in order to arrive at an overall position, which is intended to have a probability of adequacy greater than 80% (2013: greater than 80%).

### (D) Reconciliation of movement in discounted outstanding claims provision

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | OUTSTANDING CLAIMS $000's | REINSURANCE $000's | NET $000's | OUTSTANDING CLAIMS $000's | REINSURANCE $000's | NET $000's |
| At 1 January | **608,370** | **(490,777)** | **117,593** | 820,462 | (693,536) | 126,926 |
| Increase in net claims incurred in current accident year | **93,516** | **(37,477)** | **56,039** | 91,880 | (27,779) | 64,101 |
| Movement in prior year claims provision | **90,636** | **(71,056)** | **19,580** | 22,083 | (29,974) | (7,891) |
| Incurred claims recognised in profit or loss | **184,152** | **(108,533)** | **75,619** | 113,963 | (57,753) | 56,210 |
| Prior year adjustment – risk margin * | - | - | - | (21,065) | 21,065 | - |
| Claim (payments) recoveries during the year | **(427,946)** | **354,500** | **(73,446)** | (304,990) | 239,447 | (65,543) |
| At 31 December | **364,576** | **(244,810)** | **119,766** | 608,370 | (490,777) | 117,593 |

*In the prior year a portion of the risk margin was allocated to reinsurance.

## (E) Claims development – undiscounted net central estimate

| | Prior Years | 2005 $000's | 2006 $000's | 2007 $000's | 2008 $000's | 2009 $000's | 2010 $000's | 2011 $000's | 2012 $000's | 2013 $000's | 2014 $000's | TOTAL $000's |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Net claims cost - central estimate:** | | | | | | | | | | | | |
| At end of accident year | | 49,245 | 68,486 | 61,424 | 53,337 | 40,821 | 50,805 | 52,500 | 44,970 | 53,734 | 55,905 | 531,227 |
| One year later | | 53,482 | 52,535 | 48,484 | 53,476 | 41,159 | 56,241 | 54,416 | 40,954 | 58,346 | - | 459,093 |
| Two years later | | 46,072 | 59,755 | 47,503 | 58,081 | 40,575 | 53,503 | 53,258 | 47,757 | - | - | 406,504 |
| Three years later | | 47,465 | 60,672 | 50,128 | 60,665 | 40,479 | 55,667 | 56,515 | - | - | - | 371,591 |
| Four years later | | 46,483 | 60,318 | 49,951 | 59,792 | 42,712 | 58,683 | - | - | - | - | 317,939 |
| Five years later | | 47,503 | 58,802 | 49,588 | 60,974 | 42,257 | - | - | - | - | - | 259,124 |
| Six years later | | 48,601 | 58,252 | 50,202 | 62,351 | - | - | - | - | - | - | 219,406 |
| Seven years later | | 48,806 | 58,992 | 48,837 | - | - | - | - | - | - | - | 156,635 |
| Eight years later | | 48,235 | 58,464 | - | - | - | - | - | - | - | - | 106,699 |
| Nine years later | | 48,430 | - | - | - | - | - | - | - | - | - | 48,430 |
| Current estimate of net cumulative claims cost | | 48,430 | 58,464 | 48,837 | 62,351 | 42,257 | 58,683 | 56,515 | 47,757 | 58,346 | 55,905 | 537,545 |
| Cumulative net claims payments to date | | (48,077) | (58,159) | (47,628) | (59,782) | (36,716) | (52,888) | (45,990) | (34,889) | (37,268) | (21,411) | (442,808) |
| Net undiscounted central estimate | 3,170 | 353 | 305 | 1,209 | 2,569 | 5,541 | 5,795 | 10,525 | 12,868 | 21,078 | 34,494 | 97,907 |
| Net undiscounted central estimate as at 31 December 2014 | | | | | | | | | | | | 97,907 |
| Discount to present value | 174 | - | 4 | 24 | 77 | 170 | 273 | 560 | 741 | 1,101 | 1,828 | (4,952) |
| Risk margin | - | 845 | 75 | 298 | 626 | 1,351 | 1,389 | 2,508 | 3,264 | 4,966 | 7,822 | 23,144 |
| Claims settlement costs | 87 | - | 8 | 44 | 92 | 199 | 205 | 371 | 497 | 765 | 1,399 | 3,667 |
| **Net outstanding claims at 31 December 2014** | | | | | | | | | | | | 119,766 |
| **Net central estimate development** | | | | | | | | | | | | |
| Increase(decrease) in the year – current year minus prior year | (2,073) | 195 | (528) | (1,365) | 1,377 | (455) | 3,016 | 3,257 | 6,803 | 4,612 | 55,905 | 70,744 |

The central estimate claims development table is presented net of reinsurance.

## 19. SOLVENCY

On 4 March 2013 the Branch was granted a full licence under the Insurance (Prudential Supervision) Act 2010 ("the Act"). As the Branch is a branch of an overseas insurer it is exempt under the Act from complying with the Solvency Standard for Non-Life Insurance Business subject to the condition that the Company meets the equivalent Australian non-Life solvency standard.

The table below discloses the solvency coverage for QBE Insurance (International) Limited which includes the Branch as calculated under the Australian APRA requirements.

| | 2014 AUD$000's | 2013 AUD$000's |
|---|---|---|
| APRA prescribed capital amount | **206,451** | 218,745 |
| Capital surplus | **268,277** | 212,136 |
| Solvency coverage | **2.29** | 1.97 |

## 20. CAPITAL MANAGEMENT AND HEAD OFFICE ACCOUNT

The Branch's objective when managing capital is to meet the solvency requirements and financial strength rating of the parent company.

Local management monitor key financial parameters to safeguard the Branch's ability to continue as a going concern and provide financial returns for the shareholder. The capital of the Branch comprises the Head Office account which consists of retained earnings and current account transactions between the Branch and Head Office. Current transactions with the Head Office include reinsurance, head office charges and other expenses which are settled on a regular basis.

## 21. KEY MANAGEMENT PERSONNEL

Compensation of key management personnel employed by the New Zealand Branch for the years ended 31 December 2014 and 2013 is set out below.

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| Short term employee benefits | **3,377** | 3,235 |
| Post employment benefits | **152** | 147 |
| Other long term employment benefits | **-** | 11 |
| Share based payments | **368** | 204 |
| | **3,897** | 3,597 |

## 22. REMUNERATION OF AUDITOR

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| **PricewaterhouseCoopers** | | |
| Audit of financial reports | **291** | 232 |
| Taxation services | **66** | 37 |
| | **357** | 269 |



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## 23. CONTINGENT LIABILITIES

The Branch had no contingent liabilities as at 31 December 2014 (2013: nil).

## 24. CAPITAL EXPENDITURE COMMITMENTS

The Branch had no commitments for expenditure as at 31 December 2014 (2013: nil).

## 25. OPERATING LEASE COMMITMENTS

| | 2014 $000's | 2013 $000's |
|---|---|---|
| Payable: | | |
| Not later than one year | **2,205** | 2,126 |
| Later than one year but less than five years | **4,973** | 2,046 |
| Later than five years | **-** | 75 |
| Total future minimum lease payments under non-cancellable operating leases | **7,178** | 4,247 |

## 26. RELATED PARTY DISCLOSURES

(i) The Branch's ultimate parent and controlling party is QBE Insurance Group Limited, a company incorporated in Australia. All trading balances owed to/(from) related parties are settled on a regular basis. At the end of the reporting period the Branch had the following related party balances:

| | | 2014 $'000 | 2013 $'000 |
|---|---|---|---|
| **Related party** | **Description** | | |
| QBE Insurance Group Limited | Mandatory convertible notes | **-** | 102,000 |
| QBE Equator Reinsurances Limited | Reinsurance | **98** | (432) |
| QBE Insurance (Australia) Limited | Reinsurance | **82** | 33 |
| QBE Lenders Mortgage Insurance Ltd | Reinsurance | **(15)** | (13) |
| QBE Management (Ireland) Limited | Reinsurance | **-** | (535) |
| | | **165** | 101,053 |
| **The outstanding related party balances are reported as:** | | | |
| Trade and other payables | | **180** | 102,033 |
| Trade and other receivables | | **(15)** | (980) |



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(ii) The following were carried out with related parties:

| | 2014 $'000 | 2013 $'000 |
|---|---|---|
| **Transactions with QBE Insurance Group Limited** | | |
| Interest on related party loan | **3,636** | 5,960 |
| **Transactions with QBE Insurance (International) Limited** | | |
| Reinsurance expense less recoveries | **65,552** | 102,186 |
| Administration and management fees | **6,497** | 3,171 |
| Reimbursement of transactions with related parties | **729** | 1,260 |
| **Transactions with other related parties of ultimate parent** | | |
| Reinsurance expense less recoveries | **74,203** | 35,495 |

## 27. CREDIT RATING

Standard & Poors' Rating Services affirmed the financial strength of A+ with a negative outlook for QBE Insurance (International) Limited, New Zealand Branch, on 12 December 2014: A+ (2013: A+)

## 28. EVENTS OCCURRING AFTER REPORTING DATE

There is, at the date of this report, no matter or circumstance that has arisen since 31 December 2014 that has significantly affected, or may significantly affect:

(i) the Branch's operations in future financial years; or
(ii) the results of those operations in future financial years; or
(iii) the Branch's state of affairs in future financial year.

## 29. CORPORATE GOVERNANCE

Information regarding the corporate governance policies, practices and processes of QBE Insurance (International) Limited is available from www.group.qbe.com/investor-centre/corporate-governance.

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22 April 2014

Mr Terry Lawrence
Chief Financial Officer
QBE New Zealand
Level 9, AMP Centre
29 Customs Street West
Auckland

Dear Mr Lawrence

**Re: QBE New Zealand Operations Actuarial Report at 31 December 2013.**

Section 77 and 78 of the Insurance (Prudential Supervision) Act 2010 requires a licensed insurer to ensure that actuarial information included in the financial statements has been reviewed by the insurer's Appointed Actuary. As the Appointed Actuary for QBE New Zealand (QBENZ), I, Benoit Laganiere have conducted this review for QBENZ's financial statements for the period ending 31 December 2013.

This review involved ascertaining whether actuarial information used in the preparation of the financial statements has applied appropriately. No limitations were placed on me in conducting this review, and all information requested has been made available to me.

For the purposes of this review, actuarial information includes

- Outstanding claims liabilities
- Premium Liabilities
- Application of the Liability Adequacy Test
- Reinsurance and other recovery assets
- Deferred Acquisition Costs.

I am an employee of QBE Management Services (QMS), which is a related company to QBENZ in that both companies are fully owned by QBE Insurance Group. In addition to this, I held equity positions (current or deferred) in QBE Insurance Group securities at the date of this report. This holding is an immaterial proportion of the total shares issued by QBE.

From my review, it is my opinion that

- the actuarial information included in QBENZ's financial statements has been appropriately included;
- the actuarial information used to prepare the financial statements has been appropriately used; and
- it is understood that QBENZ was granted exemption from complying with the RBNZ solvency standards for non-life insurance business under Section 59 of the Insurance Act. QBENZ is currently a branch of QBE Insurance (International) Limited (QII) which is an APRA regulated entity. QBENZ is therefore dependent on QII's capital surplus to remain solvent under most adverse scenarios developed as part of QII's capital management plan.

Yours faithfully

Benoit Laganiere
New Zealand Appointed Actuary of QBE Insurance (International) Limited
Fellow of the Institute of Actuaries of Australia