QBE LENDERS' MORTGAGE INSURANCE LII

10060034994

(A.B.N 70 000 511 071)

FINANCIAL REPORT – 31 DECEMBER 2010

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This financial report includes separate financial statements for QBE Lenders' Mortgage Insurance Limited ("the company") as an individual entity. The financial report is presented in Australian dollars.

QBE Lenders' Mortgage Insurance Limited is a company limited by shares, incorporated and domiciled in Australia. Its registered office is:

82 Pitt Street

Sydney

NSW 2000

The principal place of business is Level 21, 50 Bridge St, Sydney, NSW

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 17 February 2011.

QBE LENDERS' MORTGAGE INSURANCE LIMITED

DIRECTORS' REPORT

For the year ended 31 December 2010

Your directors present their report on QBE Lenders' Mortgage Insurance Limited ("the company") for the year ended 31 December 2010.

Directors

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

Director		
The Hon. NF Greiner		Chairman
IT Graham		Chief Executive Officer
GJ Gilbert		
GP Hickey		
TW Ibbotson	Resigned 1 June 2010	
V McLenaghan	Appointed 1 November 2010	
FM O'Halloran	Resigned 1 November 2010	
GB Thwaites	Appointed 1 June 2010	
VJ Walter	Appointed 1 January 2010	

Principal activities

The principal activities of the company during the year were:

- To provide residential lenders' mortgage insurance, reinsurance to customer's captive lenders' mortgage insurance companies and insurance over residential mortgage backed securities programs in Australia and New Zealand.
- To manage, through a fund manager, the company's investments.
- To provide management services to lenders' mortgage insurance subsidiaries.

There were no significant changes to the principal activities during the year.

Results and review of operations

Net profit after income tax for the financial year was $253.5M, an increase of $117.1M on the prior year.

During the year, the company formed the view that the risk of an extended period of claims emergence as a result of the Global Financial Crisis had abated. Consequently, the earning patterns adopted in 2008 were revised across all underwriting years to reflect the latest actuarial view of long term average risk emergence. This resulted in one-off releases of unearned premiums and deferred insurance costs.

The table below illustrates the impact of these one off adjustments on the "underlying" result of the company.

	2010 $M
Net profit after income tax reported in the financial statements	**253.5**
Decrease in unearned premium	(132.8)
Decrease in deferred insurance costs	7.0
Tax impact of adjustments	37.7
Underlying net profit after income tax	**165.4**

The following analysis compares the 2010 underlying result, after allowing for these adjustments, with 2009 reported result:

	Underlying Result 2010 $M	2009 $M
Revenue		
Premium revenue	**229.7**	240.1
Other revenue	**97.6**	72.5
Net fair value gains (losses) on financial assets	**1.3**	(4.2)
	328.6	308.4
Expenses		
Net outward reinsurance premium expense	**24.3**	15.3
Gross claims incurred	**11.2**	43.2
Other expenses	**57.6**	55.9
	93.1	114.4
Profit before income tax	**235.5**	194.0
Income tax expense	**70.1**	57.6
Net profit after income tax	**165.4**	136.4

Gross written premium of $225.9M decreased compared to $231.3M in 2009 due primarily to a particularly strong first home buyers market in 2009 which did not carry forward into 2010.

The rise in underlying net profit after income tax to $165.4M was principally due to lower claims incurred and improved returns from the company's investments.

Claims incurred of $11.2M decreased compared to $43.2M in 2009 due to the favourable impact of improved macro-economic conditions on mortgage defaults, claim rates and average claim sizes.

Net investment income of $93.7M increased from $66.8M in 2009, principally due to the impact of higher interest rates on earnings from cash and securities.

Controlling entities

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

The controlling entity's registered office is at 82 Pitt Street, Sydney, NSW 2000.

Prior to 23 December 2009, the controlling entity was QBE Lenders' Mortgage Insurance (Holdings) Pty Limited, a company limited by shares, incorporated and domiciled in Australia.

Dividends

The directors recommend the payment of a dividend for the financial year ended 31 December 2010 of $75.0M (2009: $100.0M).

$125.0M dividends have been paid during the financial year ended 31 December 2010 (2009: Nil).

Options

There were no options granted by the company during the year (31 December 2009: 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 the information would be likely to result in unreasonable prejudice to the company.

Significant changes

There were no significant changes to the company's state of affairs during the year.

Events subsequent to balance date

There is, at the date of this report, no matter or circumstance that has arisen since 31 December 2010 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.

The company does not expect a material increase in claims incurred arising from the floods experienced in parts of Queensland, Victoria and New South Wales during January 2011. The company has established hardship procedures for borrowers experiencing temporary difficulties in meeting mortgage payments, and expects to work closely with lenders to help flood affected borrowers who need assistance in the months ahead.

Environmental regulation

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

Directors' benefit

Since the end of the previous financial year, no director of the company has received or become entitled to receive a benefit (other than a remuneration or retirement 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

Under its constitution, the company has agreed to indemnify all the officers of the company for any liability (to the maximum extent permitted by the law), whether civil or criminal, for which they may be held personally liable.

No indemnity is given to present or former officers of the company or its subsidiaries against any liability incurred in their capacity as an officer unless the giving of the indemnity has been approved by the Board.

The company paid premiums in respect of a contract insuring 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, KJ O'Loughlin and DAM Ramsay. In accordance with normal commercial practice, disclosure of the total amount of premium payable and the nature of liabilities covered by the insurance contracts are prohibited by a confidentiality clause in the contract.

No premiums have been paid to indemnify the auditors in any capacity.

Rounding of amounts

The company is of a kind referred to in the ASIC class order 98/0100 dated 10 July 1998 (as amended by class order 04/667 dated 15 July 2004) relating to the "rounding off" of amounts in the report of the directors. Amounts have been rounded off in the directors' report to the nearest one hundred thousand dollars in accordance with that class order.

<u>Auditors</u>

PricewaterhouseCoopers, Chartered Accountants, continues in office in accordance with Section 327B of the *Corporations Act 2001*.

Signed in accordance with a resolution of the directors made on 17 February 2011.

The Hon. NF Greiner
Chairman

IT Graham
Director

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Auditor's Independence Declaration

As lead auditor for the audit of QBE Lenders' Mortgage Insurance Limited (the company) for the year ended 31 December 2010, 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.

This declaration is in respect of QBE Lenders' Mortgage Insurance Limited (the company) during the period.

JW Bennett
Partner
PricewaterhouseCoopers

Sydney
17 February 2011

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Independent auditor's report to the members of QBE Lenders' Mortgage Insurance Limited

Report on the financial report

We have audited the accompanying financial report of QBE Lenders' Mortgage Insurance Limited (the company), which comprises the balance sheet as at 31 December 2010, 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, 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. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation 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.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report.

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

PRICEWATERHOUSECOOPERS

Independent auditor's report to the members of QBE Lenders' Mortgage Insurance Limited (continued)

Independence

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

Auditor's opinion

In our opinion:

(a) the financial report of QBE Lenders' Mortgage Insurance 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 2010 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;* and

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

PricewaterhouseCoopers

J W Bennett
Partner

Sydney
17 February 2011

QBE LENDERS' MORTGAGE INSURANCE LIMITED

DIRECTORS' DECLARATION

In the directors' opinion:

(a) the financial statements and notes set out on pages 9 to 52 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 2010 and of its performance, as represented by the results of its operations, changes in equity and its cash flows, 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. Note 1(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 17th day of February 2011 in accordance with a resolution of the directors.

The Hon. NF Greiner
Chairman

IT Graham
Director

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2010

	NOTES	2010 $M	2009 $M
REVENUE			
Premium revenue	6	**362.5**	240.1
Other revenue	6	**97.6**	72.5
Net fair value gains (losses) on financial assets	6	**1.3**	(4.2)
		461.4	308.4
EXPENSES			
Net outward reinsurance premium expense	7(A)	**24.3**	15.3
Gross claims incurred	8	**11.2**	43.2
Other expenses	7(C)	**64.6**	55.9
		100.1	114.4
Profit before income tax		**361.3**	194.0
Income tax expense	9	**107.8**	57.6
Profit after income tax		**253.5**	136.4
OTHER COMPREHENSIVE INCOME			
Net movement in foreign currency translation reserve	20(B)	**0.8**	0.1
Income tax relating to components of other comprehensive income		**-**	-
Other comprehensive income after income tax		**0.8**	0.1
Total comprehensive income after income tax attributable to ordinary equity holders of the company		**254.3**	136.5

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

QBE LENDERS' MORTGAGE INSURANCE LIMITED

BALANCE SHEET

As at 31 December 2010

	NOTES	2010 $M	2009 $M
ASSETS			
Financial assets at fair value through profit or loss:			
Cash and cash equivalents	10	**22.6**	12.5
Investments	11	**1,655.5**	1,625.7
Trade and other receivables	12	**77.7**	65.5
Non-reinsurance recoveries on outstanding claims	18(A)	**4.8**	3.9
Deferred insurance costs	13	**56.1**	38.9
Property, plant and equipment	14	**2.0**	2.9
Shares in controlled entities		**75.3**	75.3
Deferred tax assets	15	**-**	39.4
Total assets		**1,894.0**	1,864.1
LIABILITIES			
Trade and other payables	16	**120.5**	55.9
Deferred tax liabilities	15	**0.1**	-
Provisions	17	**0.6**	0.9
Outstanding claims	18(A)	**199.3**	225.5
Unearned premium	19	**508.0**	645.6
Total liabilities		**828.5**	927.9
Net assets		**1,065.5**	936.2
EQUITY			
Share capital	20(A)	**364.3**	364.3
Reserves	20(B)	**2.3**	6.4
Retained profits		**698.9**	565.5
Total equity		**1,065.5**	936.2

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

STATEMENT OF CHANGES IN EQUITY
For the year ended 31 December 2010

	Share Capital $M	Reserves $M	Retained Profits $M	Total Equity $M
2010				
As at 1 January	**364.3**	**6.4**	**565.5**	**936.2**
Profit after income tax	-	-	**253.5**	**253.5**
Other comprehensive income	-	**0.8**	-	**0.8**
Total comprehensive income	-	**0.8**	**253.5**	**254.3**
Transactions with owners in their capacity as owners				
Transfer of share based payments reserve	-	**(4.9)**	**4.9**	-
Dividends paid	-	-	**(125.0)**	**(125.0)**
As at 31 December	**364.3**	**2.3**	**698.9**	**1,065.5**
2009				
As at 1 January	364.3	6.3	429.1	799.7
Profit after income tax	-	-	136.4	136.4
Other comprehensive income	-	0.1	-	0.1
Total comprehensive income	-	0.1	136.4	136.5
Transactions with owners in their capacity as owners				
Dividends paid	-	-	-	-
As at 31 December	364.3	6.4	565.5	936.2

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

QBE LENDERS' MORTGAGE INSURANCE LIMITED

STATEMENT OF CASH FLOWS

For the year ended 31 December 2010

	NOTES	2010 $M	2009 $M
OPERATING ACTIVITIES			
Premium received		**259.3**	253.6
Non-reinsurance recoveries received		**1.8**	4.9
Outwards reinsurance premium paid		**(30.2)**	(28.1)
Claims paid		**(38.2)**	(73.8)
Insurance costs paid		**(30.3)**	(13.2)
Other underwriting costs paid		**(39.4)**	(27.4)
Interest and dividends received		**70.5**	41.1
Other operating receipts		**2.0**	1.4
Net GST collected and paid to the ATO		**(18.4)**	(17.7)
Income taxes (paid) received *		**(38.8)**	15.2
Net cash flows from operating activities	10(A)	**138.3**	156.0
INVESTING ACTIVITIES			
(Payments for purchase) proceeds from sale of financial assets**		**(4.2)**	(165.1)
Payments for purchase of property, plant and equipment		**(0.5)**	(0.7)
Payments for purchase of controlled entities and businesses acquired		**-**	(0.2)
Dividend received from controlled entity		**1.5**	1.3
Net cash flows from investing activities		**(3.2)**	**(164.7)**
FINANCING ACTIVITIES			
Dividends paid		**(125.0)**	-
Net cash flows from financing activities		**(125.0)**	-
Net movement in cash and cash equivalents		**10.1**	(8.7)
Cash and cash equivalents at the beginning of the financial year		**12.5**	21.2
Cash and cash equivalents at the end of the financial year	10	**22.6**	12.5

* Income taxes received / (paid) include amounts from / to related entities in Australia and New Zealand.

** Proceeds from sale (payments for purchase) of financial assets include net movements for investments.

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

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2010

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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. This financial report includes financial statements for QBE Lenders' Mortgage Insurance Limited ("the company") as an individual entity.

(A) Basis of preparation

This general purpose financial report has been prepared in accordance with Australian Accounting Standards, other authoritative pronouncements of the Australian Accounting Standards Board ("AASB"), Urgent Issues Group ("UIG") interpretations and the *Corporations Act 2001.*

The presentation currency of these financial statements is Australian dollars.

Compliance with IFRS

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

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 recoveries at present value.

Other

These financial statements are separate financial statements and the company is exempt from preparing consolidated financial statements. The ultimate parent company, QBE Insurance Group Limited ("QBE") (incorporated in Australia), produces consolidated financial statements in accordance with IFRS produced for public use, copies of which can be obtained at www.qbe.com or 82 Pitt Street, Sydney, NSW, 2000.

(B) Insurance contracts

All of the insurance products offered or utilised by the company meet the definition of insurance contracts under AASB 1023 "General Insurance Contracts", and are accounted for and reported in accordance with this standard. These products do not contain embedded derivatives or deposits that are required to be unbundled.

Insurance contracts that meet the definition of financial guarantee products are accounted for as insurance contracts under AASB 1023, rather than as financial instruments under AASB 139 "Financial Instruments: Recognition and Measurement".

(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 is recognised as revenue. Premium is treated as earned from the date of attachment of risk.

(D) Unearned premium

Unearned premium is calculated based on the term of the policies written and the likely pattern in which risk will emerge over that term.

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 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 business segment level, being a portfolio of contracts that are broadly similar and managed together as a single portfolio. If the unearned premium liability, less deferred acquisition costs, is deficient, then the resulting deficiency is recognised through the profit or loss of the company.

(E) Outward reinsurance

Premium ceded to reinsurers is recognised as an expense in accordance with the pattern of reinsurance service received. Where applicable, a portion of outward reinsurance premium is deferred at the balance 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"), and estimated claims handling costs. Claims expense represents claim payments adjusted for movements 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 non-reinsurance recoveries, to reflect the inherent uncertainty in the central estimate.

(G) Non-reinsurance recoveries

Non-reinsurance recoveries receivable on paid claims, reported claims not yet paid and IBNR 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.

(H) Acquisition costs

A portion of acquisition costs relating to unearned premium is deferred in recognition that it represents a future benefit. Deferred acquisition costs are measured at the lower of cost and recoverable amount. Deferred acquisition costs are amortised over the financial years expected to benefit from the expenditure in accordance with the premium income earning pattern adjusted for policy terminations.

(I) Commissions

Exchange commission is payable in accordance with the applicable reinsurance agreement on the basis of reinsurance premium written. Reinsurance exchange commission is recognised as an expense in accordance with the premium income earning pattern adjusted for policy terminations.

Profit commission is payable in accordance with the applicable agreements and based on the profitability of the underlying portfolio, including the recognition of revenue and claims experience. An expense is recognised as the risk emerges in the underlying portfolio.

(J) 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 fair value gains or losses on financial assets.

(K) Fee income

Fees are recognised on an accruals basis over the period during which the service is performed.

(L) Taxation

The income tax expense for the period is the tax payable on the current period's taxable income based on the notional income tax rate for each jurisdiction, 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 assets and liabilities are recognised for temporary differences at the tax rate expected to apply when the assets are recovered or liabilities are settled, based on those tax rates which are enacted or substantively enacted for each jurisdiction. 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 at the time of the transaction 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 liabilities and assets 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 near future.

Current and deferred tax balances attributable to amounts recognised directly in equity are also recognised directly in equity.

The company has implemented the tax consolidation legislation. All entities in the tax-consolidated group continue to account for 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. The head entity of the tax-consolidated group recognises any current tax or deferred tax arising from unused tax losses and unused tax credits assumed from controlled entities in the tax-consolidated group. Details of the tax funding agreement are included in Note 9(B).

(M) Financial instruments

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

(i) Financial assets

The company has identified the following classes of financial asset: cash and cash equivalents, investments, and trade and other receivables.

(ii) Financial liabilities

The company has identified the following class of financial liability: trade and other payables.

(iii) Financial instruments designated as fair value through profit or loss.

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.

(N) Cash and cash equivalents

Cash and cash equivalents includes balances readily convertible to cash, and which are used in cash management function on a day to day basis, net of bank overdrafts.

(O) Investments

All 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.

For securities traded in an active market, the fair value is determined by reference to published closing bid price quotations. For securities that are not traded and securities that are traded in a market that is not active, fair value is determined using valuation techniques generally be reference to the fair value of recent arm's length transactions involving the same or similar instruments. Fixed and floating rate securities are valued using independently sourced valuations that do not involve the exercise of judgement by management.

All purchases and sales of financial assets that require delivery of the asset within the timeframe 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 assets has expired, or has been transferred, and the company has transferred substantially all the risks and rewards of ownership.

(P) Receivables

Receivables are recognised and carried at original invoice amount less a provision for any impairment. 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 the 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 the profit or loss.

(Q) Property, plant and equipment

Property, plant and equipment is stated at historical cost less accumulated depreciation.

Leasehold improvements, office equipment, fixtures and fittings 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 to 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(S).

(R) Shares in controlled entities

Shares in controlled entities were acquired prior to 1 January 2010, were initially recognised at cost (fair value of consideration provided plus directly attributable acquisition related costs) and are subsequently carried in the company's financial statements at the lower of cost and recoverable amount.

A revised AASB 3 Business Combinations became applicable to the company for any acquisitions subsequent to 1 January 2010. Purchase consideration will be recorded at fair value at the acquisition date, and acquisition related expenses will be expensed as incurred.

Investments in subsidiaries are subject to impairment review – refer note 1(S).

(S) 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 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.

(T) Foreign currency translation

(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

Foreign currency transactions are translated into functional currencies at the rates of exchange 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 proft or loss.

(iii) Translation of overseas branch

The functional currency of the New Zealand branch operation of the company is New Zealand dollars (NZ$). The results and balance sheet of the New Zealand branch are translated into the presentation currency as follows:

- assets and liabilities are translated at the closing balance date rates of exchange;
- income and expenses are translated at average rates of exchange; and
- all resulting exchange differences are recognised as a separate component of equity.

(U) Employee Benefits

Effective 1 August 2009, employment contracts with all Australian employees of the company ceased and those employees commenced employment with a related party, QBE Management Services Pty Limited ("QMS"). Effective 17 August 2009, employment contracts with all New Zealand employees of the company ceased and those employees commenced employment with a related party, QBE Insurance (International) Limited ("QII") New Zealand branch.

As a result of the changes to employee contracts, the company ceased incurring employment related expenses and now incurs equivalent management fee expenses payable to the new employers. In addition, the company ceased providing for employee related expenses as the new employers make these provisions and recharge the company.

Prior to the cessation of the above employment contracts:

- Accrual was made for employee entitlement benefits accumulated as a result of employees rendering services up to that date. These benefits include salaries, bonuses, annual leave and long service leave.
- Liabilities arising in respect of salaries, bonuses, annual leave and any other employee entitlements expected to be settled within 12 months of the reporting date were measured at their nominal amounts.
- Provision for long service leave was 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 date were discounted to present value.
- Contributions made to defined contribution superannuation funds by the company were expensed as incurred.

(V) Provisions

Provisions are recognised when the company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

(W) 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.

(X) 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 date.

(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 the profit or loss on a straight line basis over the period of the lease.

(Z) Goods and services tax (GST)

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

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 flows.

Commitments are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(AA) Comparative figures

Comparative figures have been adjusted, where necessary, to conform to the basis of presentation and the classification used in the current year.

(BB) Rounding of amounts

The company is of a kind referred to in the ASIC class order 98/0100 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 have been rounded off in the financial statements to the nearest hundred thousand dollars in accordance with that class order.

2. NEW ACCOUNTING STANDARDS AND INTERPRETATIONS

The AASB has issued the following amendments to Australian Accounting Standards:

Title		Operative Date
AASB 9	Financial Instruments	1 January 2013
2009-11	Amendments to Australian Accounting Standards arising from AASB 9	1 January 2013
2009-12	Amendments to Australian Accounting Standards	1 January 2011
2009-13	Amendments to Australian Accounting Standards arising from Interpretation 19	1 January 2011
2009-14	Amendments to Australian Interpretation - Prepayments of a Minimum Funding Requirement	1 January 2011
2010-3	Amendments to Australian Accounting Standards arising from the Annual Improvements Project	1 January 2011
2010-4	Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project	1 January 2011
2010-5	Amendments to Australian Accounting Standards	1 January 2011
2010-6	Amendments to Australian Accounting Standards – Disclosures on Transfers of Financial Assets	1 July 2011
AASB 1053	Application of Tiers of Australian Accounting Standards	1 January 2014

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

The company will apply the amendments detailed above for the reporting periods beginning on the operative dates set out above. The application of these standards is not expected to have a material impact on the company's financial statements.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

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 actuaries and management 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) Ultimate liability arising from claims made under insurance contracts

Provision is made for the estimated cost of claims incurred but not settled at the balance date. This provision consists of estimates of both the expected ultimate cost of claims notified to the company as well as the expected ultimate cost of claims incurred but not reported to the company ("IBNR"). The estimated cost of claims includes direct expenses that are expected to be incurred in settling those 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. The longer the delay between the event giving rise to the claim and final claim settlement, the greater the variability between initial estimates of the loss to be incurred and the final settlement amount, as a result of additional financing and settlement costs incurred by the lender and changes in property valuations.

The estimation techniques and assumptions used in determining the outstanding claims provision and the associated non-reinsurance recoveries are described below.

(i) Insurance risk assumptions

The company's process for establishing the outstanding claims provision involves extensive consultation with actuaries, claims managers, and other senior management. This process includes regular internal claims review meetings attended by senior management and detailed review by an external actuary at least annually.

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 during the time that elapses before a definitive determination of the ultimate claims cost can be made;
- changes in the legal environment; and
- social and economic trends, for example house price inflation, unemployment and interest rates.

The potential impact of changes in key assumptions on the company's statement of comprehensive income and balance sheet are summarised in note 3(A)(vi).

(ii) Central estimates

The outstanding claims provision comprises the central estimate and a risk margin which is added to the central estimate to achieve a desired probability of adequacy. The outstanding claims provision is discounted at risk-free rates of return to reflect the time value of money.

A central estimate is an estimate of the level of claims provision that is intended to contain no intentional under or over estimation. As the company requires a higher probability that estimates will be adequate over time, a risk margin is added to the central estimate of outstanding claims.

Central estimates 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 estimate is based on a judgmental consideration of the results of each method and qualitative information, for example:

- Historical trends in the development and incidence of the numbers of defaults reported, numbers of defaults cured, numbers of properties taken into possession, numbers of such properties sold, numbers of claims arising from these sales, and the costs of those claims;
- Exposure details, including policy counts, sums insured and various other characteristics of the borrowers and loans; and
- Historical and likely future trends of expenses associated with managing claims to finalisation.

Central estimates are calculated gross of any non-reinsurance recoveries. Separate estimates are made of the amounts recoverable from reinsurers, borrowers and third parties based on the gross outstanding claims provision.

(iii) Risk margin

Risk margins are held to mitigate the potential for uncertainty in the outstanding claims estimation process. The determination of the appropriate level of risk margin takes into account the uncertainty or variability inherent in the company's business and the diversification benefits achieved by writing business in a number of geographic locations and with different lenders.

The measurement of variability 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. The use of a range of outcomes allows a determination of the risk margin required to provide an estimate at a given probability of adequacy, e.g. 9 times in 10 (a 90% probability of adequacy). These techniques use standard statistical distributions, and the measure of variability is referred to as the standard deviation or the coefficient of variation.

The directors and management have set an internal target for the probability of adequacy of the net outstanding claims provision to be 75% or above. The Australian Prudential Regulation Authority ("APRA") requires a probability of adequacy of 75% in the determination of minimum capital. For the actual probability of adequacy applied at the end of the financial year, refer to note 18(B).

(iv) Expected present value of future cash flows for future claims

The expected present value of future cash flows for future claims and risk margin used in the liability adequacy test (refer note 19(D)) are determined using the same methods described above.

(v) Assumptions used to determine the outstanding claims provision

	2010	2009
Severity	**29.1%**	30.4%
Claim rates	**32.1%**	34.5%
Recovery rates	**1.0%**	0.5%
Risk margin (as a proportion of the central estimate)	**125%**	119%

Severity is a measure of the anticipated claims cost relative to the corresponding risk exposures.

Claim rate is the percentage of current defaults that are expected to become claims

Recovery rate is a measure of anticipated non-reinsurance recoveries in claims.

The percentages adopted in the actuarial model are determined based on an analysis of historical experience combined with actuarial and management judgement of future trends.

The outstanding claims provision is discounted to net present value using a risk free rate of return. Details of the risk free rates of return are summarised below:

	2010		2009	
	Average of succeeding year	**Average of subsequent years**	Average of succeeding year	Average of subsequent years
Discount factor	**4.8%**	**5.4%**	4.1%	5.3%

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

The impact of changes in key outstanding claims variables is summarised in the following table. Each change has been calculated in isolation from the other changes and each change shows the after tax impact on profit and equity assuming that there is no change to:

- any of the other variables; and
- the probability of adequacy.

It is likely that if, for example, the central estimate was to increase by 5%, at least part of the increase would result in a decrease in the probability of adequacy.

Variable	Change in assumptions	2010 Revised Variable	2010 Impact on Profit (Loss) and Equity [1] $M	2009 Revised Variable	2009 Impact on Profit (Loss) and Equity [1] $M
Severity	+20%	**34.9%**	**(14.6)**	36.5%	(17.0)
	-20%	**23.3%**	**14.6**	24.3%	17.0
Claim rates	+20%	**38.5%**	**(14.6)**	41.4%	(17.0)
	-20%	**25.6%**	**14.6**	27.6%	17.0
Recovery rates	+20%	**1.2%**	**0.3**	0.6%	0.3
	-20%	**0.8%**	**(0.3)**	0.4%	(0.3)
Discount factors	+20%	**6.7%**	**0.9**	5.7%	0.9
	-20%	**4.5%**	**(0.9)**	3.8%	(0.9)
Risk margin	+20%	**149.6%**	**(15.1)**	142.8%	(16.9)
	-20%	**99.7%**	**15.1**	95.2%	16.9

[1] Assumes taxation at prima facie rate of 30%.

(B) Unearned premium liabilities and deferred insurance costs

As highlighted in note 1(C), premium is earned based on the term of the policies written and the likely pattern in which risk will emerge over that term. An actuarial analysis of the emergence of risk over the life of a policy is performed annually and is used to derive an earning pattern for each underwriting year. Premium is earned and acquisition costs recognised in accordance with this pattern.

During the year, the company formed the view that the risk of an extended period of claims emergence as a result of the Global Financial Crisis had abated. Consequently, the earning patterns adopted in 2008 were revised across all underwriting years to reflect the latest actuarial view of long term average risk emergence. This reduced the unearned premium liability by $132.8M and deferred insurance costs by $7.0M.

Given the unpredictable pattern of future policy terminations it is not practical to reliably estimate the impact of these changes in individual future periods.

4. RISK MANAGEMENT

(A) Governance

The Board of Directors must ultimately be satisfied that appropriate, adequate and effective risk management systems are in place, and that these systems are operating effectively in practice, having regard to the risks they aim to control. The Board reviews key risk management information to satisfy itself in this regard and reviews and approves the risk management and reinsurance management strategies annually.

Day to day management, including implementation of strategies, policies and processes that support the risk management framework approved by the Board, is undertaken by executive management. Additional assurance is received from the appointment of an Appointed Actuary and an Appointed Auditor, as well as an internal audit function.

The company is also subject to the governance and risk management practices of its ultimate parent company.

The company has a risk management strategy for identifying, managing, monitoring and reporting on risks that could have a material impact on its operations.

The company's risk management objectives are to:

- adequately price risk;
- avoid unwelcome surprises by reducing uncertainty and volatility;
- achieve competitive advantage through better understanding the risk environment in which the company operates;
- optimise risk and more efficiently allocate capital and resources by assessing the balance of risk and reward;
- comply with laws and internal procedures; and
- improve resilience to external events.

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 company has established internal controls to manage risk in the key areas of exposure relevant to its business. The broad risk categories discussed below are:

- insurance risk;
- reinsurance counterparty risk;
- operational risk; and
- capital and regulatory risk.

Within each of these categories, risks are evaluated before consideration of the impact of mitigating controls. The existence and effectiveness of such mitigating controls are then measured to ensure that residual risks are managed within risk tolerance.

(B) Insurance Risk

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 risks are that premiums charged do not adequately remunerate the company for the risks it assumes and that the ultimate claims payments will exceed the carrying amount of the provision established.

The company has established the following protocols to manage its insurance risk:

(i) Underwriting risks

<u>Selection and pricing of risks</u>

The company offers lenders' mortgage insurance (LMI) in Australia and New Zealand. LMI insures the lender should the borrower default on repayment of the loan, and covers the remaining loan balance, plus selling costs and expenses, following the application of the proceeds from the sale of the security property.

In Australia, LMI is characterised by coverage of 100% of the loan amount. In New Zealand, insurance coverage may also be "top cover", where the total loss (including expenses) is paid up to a prescribed percentage of the original loan amount. Typical top cover in New Zealand ranges from 20% to 30% of the original loan amount.

Key risk mitigation policies and procedures comprise:

- the pricing model measures return on capital and reflects risks on a long term cyclical performance basis for both standard and new products. Pricing tables are set according to appropriate risk characteristics, such as type of product, loan amounts and loan valuation ratio.
- standard insurance agreements and documented underwriting policies and procedures are in place with allocation of delegated authority levels to approve applications.

- quality assurance reviews of underwriting and claims managements are conducted on a regular basis.

Credit risk arising from insurance contracts

Credit risk arising from insurance contracts principally relates to the risk of default by borrowers and reinsurers. For reinsurance counterparty risk, refer note 4(C).

As insurer or re-insurer, the company does not require access to the current credit quality of performing insured loans but is provided with data on loans in default by insured lenders. The relevant LMI master policy defines "default" as the borrower's failure to pay when due an amount equal to the scheduled monthly mortgage payment under the terms of the mortgage. Generally, however, the master policies require an insured to notify the insurer of a default within 14 days of the end of the month when the total amount due is unpaid and in arrears by more than 60 days. For reporting and internal tracking purposes, the company does not consider a loan to be in default until it has been delinquent for two consecutive monthly payments.

Credit risk on LMI contracts is therefore principally managed up-front through the underwriting process, prior to the acceptance of risk. The company has a centralised credit risk function that incorporates pricing, claims liability modelling, credit policy, portfolio performance reporting and analysis, and underwriting quality assurance.

Acceptance of credit risk is managed primarily using two scorecards, built on credit bureau data and company portfolio history. Credit rules are used to support these two scorecards. The centralised credit risk unit manages and maintains the scorecards and a centralised underwriting policy and procedure.

Lenders usually collect the single premium from a prospective borrower and remit the amount to the company; generally, under a standard LMI policy, premium payment is required before policy cover is incepted, which eliminates credit risk on premiums receivable.

The company does not hold any collateral as security against its exposures; however, in the event of a claim by the lender, the lender's rights as mortgagee are assigned to the company.

Concentration risk

Concentration risk is the risk of exposure due to concentration of activity in certain geographical locations, industries or counterparties. The company operates throughout all regions in Australia and New Zealand and therefore has limited geographic concentration risk on insurance contracts; exposures are monitored but not limited by region. Limits, such as those placed on maximum aggregate exposures to individual borrowers and per property, are contained in underwriting policies and are embedded in systems and processes.

The company is exposed to the possibility of very large losses from economic events such as a significant increase in regional or nationwide unemployment levels, weakening in house prices, or a significant increase in interest rates over a short period of time. The company calculates its maximum event retention ("MER") which is the estimated maximum net loss from significant economic events with an approximate return period of 250 years. The MER must be less than the company's concentration risk tolerance; otherwise, steps such as the purchase of additional reinsurance are taken to limit the exposure. As at 31 December 2010, the MER was $732.2M (2009: $693.6M) before tax benefit.

(ii) Claims management and claims provisioning 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 operate within policy and within the levels of authority delegated to them in respect of the settlement of claims;
- processes exist to ensure that all defaults are captured and updated on a timely basis and with a realistic assessment of the ultimate claims cost;

- initial IBNR estimates are set by experienced internal actuaries in conjunction with management;
- the outstanding claims provision is assessed regularly by senior management and is reviewed by the external Appointed Actuary at least annually.

(C) Reinsurance counterparty risk

Reinsurance risk management is the process of transferring insurance risk to another insurer for a price. The company reinsures a portion of risks underwritten to control exposure to insurance losses, reduce volatility and protect capital. The company's strategy in respect of the selection, approval and monitoring of reinsurance arrangements is addressed by the following protocols:

- reinsurance is placed in accordance with a reinsurance management strategy approved by the Board, which in turn is consistent with the QBE Group reinsurance management strategy and QBE Group security committee guidelines;
- reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historical and potential future losses and the company's MER; and
- exposure to reinsurance counterparties and the credit quality of those counterparties is actively monitored.

The company's current reinsurance arrangements are disclosed within Note 27.

(D) Operational risk

Operational risk is the risk of loss arising from system failure or inadequacies, human error or external events that does not relate to insurance, acquisition, capital and regulatory or financial risks. The company manages operational risk within the same robust control framework as its other risks. One of the cornerstones of the company'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.

(E) Capital management risk

The company is subject to extensive prudential regulation covering the jurisdictions in which it conducts business. Prudential regulation is generally designed to protect the policyholders. Regulation covers a number of areas including solvency, change in control and capital movement limitations. The regulatory environments in Australia continue to evolve in response to economic, political and industry developments. The company works closely with regulators and monitors regulatory developments to assess their potential impact on its ability to meet solvency and other requirements. Refer note 20(C) for more details of the company's capital management procedures.

5. FINANCIAL RISK

(A) Risk management practices

As outlined in Note 4, an overall risk management strategy is approved annually by the Board of Directors. Specific risk strategies have been developed and responsibilities assigned in connection with risks arising from financial instruments, in particular credit risk and market risk. These risks principally occur in connection with the company's investment portfolio.

Key risk mitigation policies and procedures comprise:

- Investments are directly managed within the QBE Group in accordance with the QBE's Group's investment policy. The company has additionally outsourced its custodian activities to an approved provider.

- The company maintains high credit quality investments managed in accordance with an investment mandate approved by the company's board.
- An appropriate investment portfolio with the majority of investments in fixed interest, floating rate notes ("FRN's") and short term money market securities.
- The company's senior management, Board Audit & Risk Committee and Board of Directors review the performance of the investment portfolio against the approved investment policy on a regular basis.

The company's approach provides sufficient flexibility to adjust the weighting of each investment class, dependant upon the company's impression of current and future economic factors. The overall investment objective is to obtain a reasonable return on assets, while managing liquidity risk and without incurring material risk of loss of capital.

Except where otherwise noted, the risks and exposures at the end of the financial year are representative of those that occurred during the financial year.

(B) Credit risk

Credit risk is the risk that a loss will be incurred because customers or counterparties to financial instruments fail to discharge their contractual obligations.

The company's principal exposure to credit risk from financial instruments arises from the company's holdings of FRN's, fixed interest securities and short term money market securities. The company minimises credit risk on these assets by investing in high quality, liquid securities. Additional credit risk arises in respect of cash holdings and trade and other receivables.

The company monitors credit risk in respect of its investments in terms of geographic, and sectoral / industry concentrations, as well as exposures to individual non-government issuers.

Maximum exposures to credit risk at balance date in relation to each class of recognised financial asset is the carrying amount of those assets as indicated in the balance sheet.

There are no significant credit enhancements or collateral held as security that reduce the exposure to credit risk (2009: Nil). The company has not taken possession of collateral or called upon credit enhancements during the year (2009: Nil).

None of the company's financial assets are past due or impaired or have terms that have been renegotiated and would otherwise have been past due or impaired (2009: Nil).

The credit quality of the company's holdings of investments is as follows:

Moody's Investors Services rating	**2010**	2009
	$M	$M
Aaa	**212.5**	271.1
Aa1 to Aa3	**1,253.9**	1,258.4
A1 to A3	**171.8**	79.0
Baa1 to Baa3	**17.3**	14.0
Ba1 to Ba3	**-**	3.2
Total	**1,655.5**	1,625.7

All cash and cash equivalent balances are held with either Authorised Deposit-taking Institutions in Australia or registered banks in New Zealand.

(C) 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 market prices on assets and non-insurance liabilities.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Financial instruments with floating rate interest expose the company to cash flow interest rate risk, whereas fixed interest rate instruments expose the company to fair value interest rate risk.

The company's principal exposure to interest rate risk arises from investments in financial assets at fair value through profit or loss. The company minimises interest rate risk by investing in high quality, liquid assets and actively managing the duration of the portfolio.

The 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 below:

		FIXED INTEREST RATE MATURING IN						
	Floating interest rate	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 2010								
Interest bearing financial assets ($M)	**920.7**	**413.2**	**204.3**	**62.2**	**33.3**	**15.3**	**29.1**	**1,678.1**
Weighted average interest rate (%)	**6.38%**	**5.10%**	**5.84%**	**5.93%**	**5.63%**	**6.97%**	**7.26%**	**5.99%**
At 31 December 2009								
Interest bearing financial assets ($M)	324.5	942.5	77.3	221.6	28.2	-	44.1	1,638.2
Weighted average interest rate (%)	5.57%	4.16%	5.42%	5.81%	6.24%	-	6.89%	4.83%

The company's sensitivity to movements in interest rates in relation to the value of interest bearing financial assets is shown in the table below:

		Financial impact [1]			Financial impact [1]	
	Movement in variable	**Profit (loss) 2010**	**Equity 2010**	Movement in variable	Profit (loss) 2009	Equity 2009
	%	**$M**	**$M**	%	$M	$M
Interest rate movement: Interest-bearing financial assets	**+1.0**	**(6.0)**	**(6.0)**	+1.5	(9.8)	(9.8)
	–1.0	**6.0**	**6.0**	–1.5	9.8	9.8

[1] *Assumes taxation at prima facie rate of 30%.*

The effect of interest rate risk on the company's provision for outstanding claims is included in note 3(A)(vi).

(ii) Currency risk

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

There is minimal currency risk on financial instruments, as the company's investments are predominantly held in Australian dollars.

The company is exposed to currency risk in respect of the New Zealand branch operations and its investment in its subsidiary QBE Mortgage Insurance (Asia) Limited, which is based in Hong Kong. Management of this currency risk is performed at QBE Group level.

(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).

The company was exposed to price risk during the year in respect of investments in equities; this risk was managed within the investment management framework outlined in note 5(A) and by investing in high quality, liquid assets listed on the Australian Stock Exchange.

There was minimal/no price risk at the end of the financial year as these investments had been sold.

(D) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial and insurance liabilities as and when they fall due. Liquidity risk management forms an integral part of the company's overall risk management strategy, as the majority of the company's liabilities relate to insurance contracts.

The nature of the business is that cash is received by way of single premiums at the inception of insurance contracts and is invested to fund future claims on those contracts. The principal sources of funds are written premiums, investment maturities and sales, and net investment income. The principal uses of funds are the payment of operating expenses, claim payments, taxes and growth of investments.

The key elements of the liquidity risk management strategy are as follows:

- Cash requirements are monitored regularly by management.
- Sufficient cash and cash equivalents are set aside for operating requirements of the business.
- Surplus funds are invested in accordance with the investment mandate.

The company's investment strategies form a key part of liquidity risk management.

The following table summarises the maturity profile of financial liabilities, including contingent liabilities and commitments, based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately; however, it is not expected that all creditors will request payment on the earliest date the company could be required to pay.

	Note	1 Year or Less $M	1 to 3 Years $M	3 to 5 Years $M	Over 5 Years $M	Total $M
As at 31 December 2010						
Balance sheet financial liabilities:						
Trade and other payables	**16**	**111.9**	**7.1**	**1.5**		**120.5**
Total		**111.9**	**7.1**	**1.5**	**-**	**120.5**
Other:						
Commitments	**26**	**3.2**	**8.1**	**5.4**	**-**	**16.7**
Contingent liabilities	**24**	**49.0**	**-**	**-**	**-**	**49.0**
Total		**52.2**	**8.1**	**5.4**	**-**	**65.7**
As at 31 December 2009						
Balance sheet financial liabilities:						
Trade and other payables	16	54.9	1.0	-	-	55.9
Total		54.9	1.0	-	-	55.9
Other:						
Commitments	26	2.6	4.3	-	-	6.9
Contingent liabilities	24	55.8	-	-	-	55.8
Total		58.4	4.3	-	-	62.7

6. REVENUE

	2010 $M	2009 $M
Premium revenue		
Direct	**333.8**	215.7
Inward reinsurance	**28.7**	24.4
	362.5	240.1
Other revenue		
Non-reinsurance recoveries	**1.2**	(2.8)
Interest, discount and dividend income	**94.3**	72.8
Other income	**2.1**	2.5
	97.6	72.5
Net fair value gains (losses) on financial assets	**1.3**	(4.2)
Revenue	**461.4**	308.4

7. PROFIT BEFORE INCOME TAX

(A) Profit before income tax

	Note	2010 $M	2009 $M
Gross written premium		**225.9**	231.3
Unearned premium movement		**136.6**	8.8
Gross earned premium		**362.5**	240.1
Net outward reinsurance premium		**(44.4)**	(15.3)
Deferred reinsurance premium movement		**20.1**	-
Net outward reinsurance premium expense		**(24.3)**	(15.3)
Net earned premium		**338.2**	224.8
Gross claims incurred		**(11.2)**	(43.2)
Non-reinsurance recoveries		**1.2**	(2.8)
Net claims incurred	8	**(10.0)**	(46.0)
Commission expenses		**(8.5)**	(7.8)
Other acquisition costs		**(16.6)**	(11.8)
Underwriting and other expenses		**(37.6)**	(34.5)
		(62.7)	(54.1)
Underwriting profit		**265.5**	124.7
Net investment income	7(B)	**93.7**	66.8
Other income		**2.1**	2.5
Profit before income tax		**361.3**	194.0

(B) Net investment income

	2010 $M	2009 $M
Dividend income	**2.6**	1.3
Income from short term money market securities	**17.9**	27.4
Interest received or receivable from non-related entities	**73.8**	44.1
Interest, discount and dividend income	**94.3**	72.8
Net realised gains (losses) on interest rate securities	**3.9**	(2.4)
Net realised losses on equities	**(2.5)**	-
Net unrealised losses on interest rate securities	**(0.1)**	(1.8)
Net fair value gains (losses) on financial assets	**1.3**	(4.2)
Investment expenses	**(1.9)**	(1.8)
Net investment income	**93.7**	66.8

(C) Other expenses

	2010 $M	2009 $M
Commission expenses	**8.5**	7.8
Other acquisition costs	**16.6**	11.8
Underwriting and other expenses	**37.6**	34.5
	62.7	54.1
Investment expenses	**1.9**	1.8
Other expenses	**64.6**	55.9

(D) Specific items

	2010 $M	2009 $M
Claims settlement expenses	**4.1**	2.5
Operating lease payments	**3.1**	3.7
Depreciation of plant and equipment	**1.2**	1.2
Defined contribution superannuation plan expense	-	1.4
Related party transactions:		
(i) Revenue		
Inward reinsurance premium received or receivable from controlled entities	**1.4**	2.4
Dividends from controlled entities	**1.5**	1.3
Management fee received or receivable from controlled entities	**1.8**	1.4

		2010 $M	2009 $M
(ii)	Expenses		
	Management fees and cost allocations paid or payable to related entities	**33.4**	19.4
	Reinsurance premium paid or payable to related entities (net of no claims bonus)	**44.4**	13.3
	Commissions paid or payable to related entities	**0.7**	0.9
	Reinsurance claims paid to related parties	**-**	(0.1)

8. *CLAIMS INCURRED*

(A) Claims analysis

	2010 $M	2009 $M
Gross claims incurred and related expenses		
Direct	**12.2**	42.5
Inward reinsurance	**(1.0)**	0.7
	11.2	43.2
Non-reinsurance recoveries		
Direct	**(1.1)**	2.4
Inward reinsurance	**(0.1)**	0.4
	(1.2)	2.8
Net claims incurred	**10.0**	46.0

(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 the previous reporting periods.

	2010			2009		
	Current Year	**Prior Years**	**Total**	Current Year	Prior Years	Total
	$M	**$M**	**$M**	$M	$M	$M
Gross claims incurred and related expenses						
Undiscounted	**124.9**	**(113.6)**	**11.3**	153.2	(113.2)	40.0
Discount	**(3.1)**	**3.0**	**(0.1)**	(3.1)	6.3	3.2
	121.8	**(110.6)**	**11.2**	150.1	(106.9)	43.2
Non-reinsurance recoveries						
Undiscounted	**(3.1)**	**1.8**	**(1.3)**	(2.5)	5.5	(3.0)
Discount	**0.1**	**-**	**0.1**	0.1	(0.3)	0.2
	(3.0)	**1.8**	**(1.2)**	(2.4)	5.2	(2.8)
Net claims incurred						
Undiscounted	**121.8**	**(111.8)**	**10.0**	150.7	(107.7)	43.0
Discount	**(3.0)**	**3.0**	**-**	(3.0)	6.0	3.0
	118.8	**(108.8)**	**10.0**	147.7	(101.7)	46.0

The development of net undiscounted outstanding claims for the four most recent accident years is shown in note 18(D).

9. INCOME TAX

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

	2010 $M	2009 $M
Profit before income tax	**361.3**	194.0
Prima facie tax payable at 30%	**108.4**	58.2
Tax effect of permanent differences:		
Untaxed dividends	**(0.8)**	(0.4)
Other, including non allowable expenses and non taxable income	**0.1**	0.1
Prima facie tax adjusted for permanent differences	**107.7**	57.9
Under (over) provision in prior year	**0.1**	(0.3)
Income tax expense	**107.8**	57.6
Analysed as follows:		
Current tax	**69.1**	39.4
Deferred tax	**38.6**	18.5
Under (over) provision in prior year	**0.1**	(0.3)
	107.8	57.6
Deferred tax expense comprises:		
Deferred tax assets charged to profit or loss	**45.5**	12.8
Deferred tax liabilities (credited) charged to profit or loss	**(6.9)**	5.7
	38.6	18.5

(B) Tax consolidation legislation

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

The Company is a member of a tax consolidated group headed by QBE Insurance Group Limited.

The members of the tax consolidated group have entered into a tax funding agreement that determines the amounts payable from the subsidiaries to the head entity (and vice versa) in relation to income tax. These contributions are consistent with the accounting treatment referred to above 1(L).

The members of the tax consolidated group have also entered into a tax sharing agreement which determines the income tax payable by each subsidiary in the event that the head entity defaults on its tax obligations. No amounts have been recognised in the financial statements in respect of the tax sharing agreement, as the possibility of default is remote.

(C) New Zealand Branch

The company operates a branch in New Zealand. Profits or losses generated by the branch are ignored for Australian income tax purposes, so the branch is effectively excluded from the Australian tax consolidated group. The branch qualifies as a permanent establishment for international tax purposes, and consequently lodges income tax returns and pays income tax in New Zealand as though it were a separate entity. Tax losses generated by the branch may be transferred to other New Zealand entities provided that the receiving entity shares 100% common ownership with the branch.

Effective to the branch 1 January 2011, the rate of corporate tax in New Zealand will reduce from 30% to 28%. Deferred tax assets and liabilities of the branch at 31 December 2010 have been restated in line with the lower rate.

10. CASH AND CASH EQUIVALENTS

	2010 $M	2009 $M
Cash at bank and on hand	**3.0**	0.4
Overnight money	**10.9**	12.1
Cash management trusts	**8.7**	-
Cash and cash equivalents	**22.6**	12.5

Cash and cash equivalents earn interest at floating rates based on daily bank deposit rates.

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

	2010 $M	2009 $M
Cash flows from operating activities	**138.3**	156.0
Depreciation and amortisation	**(1.2)**	(1.2)
Net fair value gains (losses) on financial assets	**1.3**	(4.1)
Income from short term money market securities	**17.9**	27.4
Dividends received from controlled entity	**1.5**	1.3
Decrease in outstanding claims	**26.2**	28.9
Decrease in unearned premiums	**137.6**	9.2
Increase (decrease) in deferred insurance costs	**17.2**	(22.4)
Increase (decrease) in non-reinsurance recoveries	**0.9**	(3.6)
Increase (decrease) in trade and other receivables	**18.6**	(20.5)
(Increase) decrease in trade and other payables	**(36.2)**	21.1
Decrease in other provisions	**0.3**	1.4
(Increase) in deferred tax liabilities / (decrease) in deferred tax assets	**(39.5)**	(17.9)
(Increase) in amounts due to parent entity or tax authorities for current tax	**(29.4)**	(39.2)
Profit after income tax	**253.5**	136.4

11. INVESTMENTS

	2010 $M	2009 $M
Interest bearing		
Short term money	**206.5**	802.4
Government bonds	**173.1**	150.5
Corporate bonds	**377.8**	360.9
Floating rate notes	**898.1**	311.9
Total investments	**1,655.5**	1,625.7
Amounts maturing within 12 months	**1,311.3**	1,254.4
Amounts maturing in greater than 12 months	**344.2**	371.3
Total investments	**1,655.5**	1,625.7

(A) Valuation of investments

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

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

Fair value hierarchy

- 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 (consensus price using broker quotes and valuation models with observable inputs); and
- Level 3: valuation techniques are applied for which any significant input is not based on observable market data.

	Level 1 $M	Level 2 $M	Level 3 $M	2010 Total $M
Short term money	-	**206.5**	-	**206.5**
Government bonds	-	**173.1**	-	**161.5**
Corporate bonds	-	**377.8**	-	**389.4**
Floating rate notes	-	**898.1**	-	**898.1**
Total investments	-	**1,655.5**	-	**1,655.5**

	Level 1 $M	Level 2 $M	Level 3 $M	2009 Total $M
Short term money	-	802.4	-	802.4
Government bonds	-	150.5	-	150.5
Corporate bonds	-	360.9	-	360.9
Floating rate notes	-	311.9	-	311.9
Total investments	-	1,625.7	-	1,625.7

(B) Movements in level 3 investments

There are no investments valued with reference to level 3 inputs.

(C) Restrictions on use

The New Zealand branch of the company is required to have a security deposit with a face value of NZ$500,000 with the New Zealand Public Trust Office. There are no restrictions on use of the company's other investments.

12. TRADE AND OTHER RECEIVABLES

	2010 $M	2009 $M
Trade debtors		
Reinsurance premiums and related receivables		
Related entity	**2.1**	17.4
Non-related entity	**4.8**	0.3
Other recoveries receivable	**4.1**	5.6
	11.0	23.3
Amounts due from parent entity	**23.6**	24.4
Amounts due from controlled entity	**0.2**	1.3
Accrued investment income	**13.7**	15.7
Other debtors and prepayments	**29.2**	0.8
Total receivables	**77.7**	65.5
Amounts maturing within 12 months	**39.5**	41.9
Amounts maturing in greater than 12 months	**38.2**	23.6
Total receivables	**77.7**	65.5

The carrying values of receivables approximate their fair value.

13. DEFERRED INSURANCE COSTS

	2010 $M	2009 $M
Deferred reinsurance premium	**20.1**	-
Deferred commission	**4.6**	9.4
Deferred acquisition costs	**31.4**	29.5
Deferred insurance costs	**56.1**	38.9
To be expensed within 12 months	**30.4**	9.3
To be expensed in greater than 12 months	**25.7**	29.6
Deferred insurance costs	**56.1**	38.9

	Deferred reinsurance premium $M	Deferred commission $M	Deferred acquisition costs $M	Total $M
Deferred costs at 1 January 2009	-	13.5	47.8	61.3
Costs deferred in financial year	-	0.8	7.6	8.4
Amortisation of costs deferred in previous financial years	-	(4.9)	(25.9)	(30.8)
Deferred costs at 31 December 2009	**-**	**9.4**	**29.5**	**38.9**
Costs deferred in financial year	**20.1**	**0.7**	**16.7**	**37.5**
Amortisation of costs deferred in previous financial years	-	**(3.2)**	**(10.0)**	**(13.2)**
Additional release (Note 3(B))	**-**	**(2.3)**	**(4.7)**	**(7.0)**
Foreign exchange	**-**	**-**	**(0.1)**	**(0.1)**
Deferred costs at 31 December 2010	**20.1**	**4.6**	**31.4**	**56.1**

14. PROPERTY, PLANT AND EQUIPMENT

	Leasehold Improvements $M	Office Equipment, Fixtures and Fittings $M	Total $M
2010			
Cost or valuation			
At 1 January	**3.4**	**3.3**	**6.7**
Additions	**-**	**0.5**	**0.5**
Disposals	**(1.0)**	**(0.8)**	**(1.8)**
At 31 December	**2.4**	**3.0**	**5.4**
Accumulated depreciation			
At 1 January	**(2.0)**	**(1.8)**	**(3.8)**
Disposals	**0.9**	**0.7**	**1.6**
Depreciation charge for the year	**(0.5)**	**(0.7)**	**(1.2)**
At 31 December	**(1.6)**	**(1.8)**	**(3.4)**
Carrying amount			
At 31 December	0.8	1.2	2.0

	Leasehold Improvements	Office Equipment, Fixtures and Fittings	Total
	$M	$M	$M
2009			
Cost or valuation			
At 1 January	2.8	3.0	5.8
Additions	0.7	0.9	1.6
Disposals	(0.1)	(0.6)	(0.7)
At 31 December	3.4	3.3	6.7
Accumulated depreciation			
At 1 January	(1.4)	(1.9)	(3.3)
Disposals	0.1	0.6	0.7
Depreciation charge for the year	(0.7)	(0.5)	(1.2)
At 31 December	(2.0)	(1.8)	(3.8)
Carrying amount			
At 31 December	1.4	1.5	2.9

15. DEFERRED INCOME TAX

	2010 $M	2009 $M
Deferred tax assets	**5.6**	53.5
Deferred tax liabilities	**(5.7)**	(14.1)
	(0.1)	39.4

(A) Deferred tax assets – maturing in greater than 12 months

(i) The balance comprises temporary differences attributable to:

	2010 $M	2009 $M
Amounts recognised in profit or loss		
Insurance liabilities	**0.9**	44.7
Financial assets - fair value movements	**2.3**	6.1
Other items	**2.4**	2.7
	5.6	53.5
Set-off deferred tax liabilities	**(5.6)**	(14.1)
	-	39.4

(B) Tax losses

Included in deferred tax assets is nil (2009: $0.2M) relating to tax losses.

Included in receivables is an amount of $23.6M (2009: $23.6M) relating to tax losses transferred to the head entity of the tax consolidated group.

The New Zealand branch made a tax loss in 2009. This loss was transferred to QII New Zealand branch during the 2010 financial year. The branch received consideration of $0.3M, being the tax value of the losses transferred.

(C) Deferred tax liabilities – maturing in greater than 12 months

(i) The balance comprises temporary differences attributable to:

	2010 $M	2009 $M
Amounts recognised in profit or loss		
Financial assets - fair value movements	**0.6**	1.6
Accrued income	**4.1**	4.7
Insurance assets	**0.4**	2.6
Other items	**0.6**	5.2
	5.7	14.1
Set-off deferred tax assets	**(5.6)**	(14.1)
	0.1	-

16. TRADE AND OTHER PAYABLES

	2010 $M	2009 $M
Trade payables	**27.0**	4.9
Amounts due to parent entities	**-**	0.1
Amounts due to parent entity for current tax	**68.3**	39.4
Amounts due to related entities	**4.8**	5.2
Reinsurance and related payables		
Related entities	**14.2**	-
Controlled entities	**0.6**	-
Other payables	**5.6**	6.3
Trade and other payables	**120.5**	55.9
Amounts payable within 12 months	**111.9**	54.9
Amounts payable in greater than 12 months	**8.6**	1.0
Trade and other payables	**120.5**	55.9

Due to the short term nature of these payables, their carrying values approximate their fair value.

17. PROVISIONS

	2010 $M	2009 $M
Other Provisions		
At 1 January	**0.9**	-
Amounts charged to profit or loss	**-**	0.2
Amounts paid	**(0.3)**	-
Other movement	**-**	0.7
At 31 December	**0.6**	0.9
Payable within 12 months	**0.1**	0.3
Payable in greater than 12 months	**0.5**	0.6
At 31 December	**0.6**	0.9

18. OUTSTANDING CLAIMS

(A) Net outstanding claims

	2010 $M	2009 $M
Gross outstanding claims	**201.6**	227.9
Claims settlement costs	**2.9**	2.7
	204.5	230.6
Discount to present value	**(5.2)**	(5.1)
Gross outstanding claims provision	**199.3**	225.5
Less than 12 months	**107.2**	127.4
Greater than 12 months	**92.1**	98.1
Gross outstanding claims provision	**199.3**	225.5
Non-reinsurance recoveries on outstanding claims	**5.0**	4.2
Discount to present value	**(0.2)**	(0.3)
Non-reinsurance recoveries on outstanding claims	**4.8**	3.9
Less than 12 months	**2.6**	2.2
Greater than 12 months	**2.2**	1.7
Non-reinsurance recoveries on outstanding claims	**4.8**	3.9
Net outstanding claims	**194.5**	221.6
Central estimate	**86.6**	101.2
Risk margin	**107.9**	120.4
Net outstanding claims	**194.5**	221.6

(B) Risk margins

The process used to determine risk margins is explained in note 3(A)(iii).

The probability of adequacy at 31 December 2010 is 99% (2009: 99%).The risk margin included in net outstanding claims is 125% (2009: 119%) of the central estimate.

(C) Reconciliation of movement in discounted outstanding claims provision

	2010			2009		
	Gross	**Re-insurance & other recoveries**	**Net**	Gross	Re-insurance & other recoveries	Net
	$M	**$M**	**$M**	$M	$M	$M
At 1 January	**225.5**	**(3.9)**	**221.6**	254.4	(7.5)	246.9
Increase in net claims incurred in current accident year	**121.8**	**(3.0)**	**118.8**	150.1	(2.4)	147.7
Movement in prior year claims provision	**(110.6)**	**1.8**	**(108.8)**	(106.9)	5.2	(101.7)
Incurred claims recognised in profit or loss	**11.2**	**(1.2)**	**10.0**	43.2	2.8	46.0
Claims (payments) recoveries	**(37.3)**	**0.3**	**(37.0)**	(72.1)	0.8	(71.3)
Foreign exchange	**(0.1)**	**-**	**(0.1)**	-	-	-
At 31 December	**199.3**	**(4.8)**	**194.5**	225.5	(3.9)	221.6

(D) Claims development

(i) Net undiscounted central estimate of outstanding claims for the company for the four most recent accident years.

	2007 $M	2008 $M	2009 $M	2010 $M	Total $M
Estimate of net ultimate claims cost:					
At end of accident year	58.3	110.7	75.2	56.1	
One year later	62.2	88.5	47.4		
Two years later	58.1	81.2			
Three years later	56.2				
Current estimate of net cumulative claims cost	**56.2**	**81.2**	**47.4**	**56.1**	**240.9**
Cumulative net claims payments to date	54.3	70.6	24.8	3.9	153.6
Net undiscounted claims for the four most recent accident years	**1.9**	**10.6**	**22.6**	**52.2**	**87.3**

(ii) Reconciliation of net undiscounted outstanding claims for the four most recent accident years to outstanding claims

	2010 $M
Net undiscounted claims for the four most recent accident years	87.3
Outstanding claims – accident years 2005 & prior	1.4
Discount on outstanding claims	(5.0)
Claims settlement costs	2.9
Risk margin	107.9
Net outstanding claims at December 2010	**194.5**

(iii) Commentary

The company has experienced a favourable development of claims provisions across all years compared to the prior year. This reflects, in particular, reductions in loss severities as claims have been settled and ultimate claims costs became more certain. This has led to reduced central estimates and risk margins in respect of prior year outstanding and current year accidents.

Conditions and trends that have affected the development of the liabilities in the past may, or may not, occur in the future, and accordingly, conclusions about future results may not necessarily be derived from the information presented in the tables

(E) Expected maturity

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
	$M	$M	$M	$M	$M	$M	$M
At 31 December 2010	**104.6**	**59.7**	**21.6**	**6.2**	**2.4**	**-**	**194.5**
At 31 December 2009	125.2	66.8	21.9	5.7	2.0	-	221.6

The weighted average term to settlement of the company's net outstanding claims provision at the balance date is 1.2 years (2009: 1.1 years).

19. UNEARNED PREMIUM

(A) Unearned premium

	Note	2010 $M	2009 $M
At 1 January		**645.6**	654.8
Deferral of premium on contracts written in the period		**197.6**	213.0
Earning of premium on contracts written in previous periods and current period		**(201.4)**	(221.8)
Additional release	3(B)	**(132.8)**	-
Foreign exchange		**(1.0)**	(0.4)
At 31 December		**508.0**	645.6
Amount to be earned within 12 months		**150.7**	152.0
Amount to be earned in greater than 12 months		**357.3**	493.6
		508.0	645.6

(B) Net premium liabilities

	Note	2010 $M	2009 $M
Unearned premium		**508.0**	645.6
Deferred insurance costs	13	**(56.1)**	(38.9)
Net premium liabilities		**451.9**	606.7

(C) Expected present value of net future cash flows for future claims

	2010 $M	2009 $M
Undiscounted central estimate	**161.8**	164.6
Risk margin	**51.4**	61.3
	213.2	225.9
Discount to present value	**(35.3)**	(32.5)
Expected present value of net future cash flows for future claims including risk margin	**177.9**	193.4

(D) *Liability adequacy test*

The liability adequacy test required comparison of the unearned premium liability net of deferred insurance costs to the present value of net future cash flows relating to future claims under current general insurance contracts.

The probability of adequacy applied in the liability adequacy test 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 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 claims provision, 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 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.

The process used to determine the risk margin is explained in note 3(A)(iii).

The risk margin in expected net future cash flows for future claims as a percentage of the undiscounted central estimate is 32% (2009: 37%).

The application of the liability adequacy test in respect of the net premium liabilities identified a surplus at 31 December 2010 and 2009.

20. EQUITY

(A) Share capital

	2010 Shares '000	2009 Shares '000	**2010 $M**	2009 $M
Issued ordinary shares, fully paid	**327.8**	327.8	**364.3**	364.3

There were no movements in share capital during the year (2009: Nil).

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 shares held. Ordinary shareholders rank after all creditors and are entitled to any residual proceeds.

(B) Reserves

	Share Based Payments $M	Foreign Currency Translation $M	Total $M
At 1 January 2009	4.9	1.4	6.3
Currency translation differences	-	0.1	0.1
At 31 December 2009	**4.9**	**1.5**	**6.4**
Share based payments			
Transfer to retained earnings	**(4.9)**	-	**(4.9)**
Currency translation differences	-	**0.8**	**0.8**
At 31 December 2010	-	**2.3**	**2.3**

The share based payments reserve was used to record the value of share based payments provided to directors and senior executives under The TPG Equity Incentive Plan. The Plan is discussed in Note 28.

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of the New Zealand branch.

(C) Capital management

The company's objectives when managing capital are to maintain an optimal capital structure to reduce the cost of capital whilst meeting capital adequacy requirements, providing security for policyholders and continuing to provide 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.

The company is subject to and in compliance with externally imposed capital requirements set and monitored by APRA. These requirements are in place to ensure sufficient solvency margins for the protection of policyholders. In addition the company aims to maintain a strong credit rating to support its business objectives.

The company has a capital management plan which is reviewed and approved by the Board on an annual basis. The plan supports the risk management strategy (refer Note 4) and is intended to meet the capital requirements of APRA and its ultimate parent entity.

Dedicated staff are responsible for understanding regulatory capital requirements. The quality of assets (particularly investments) and insurance risk is monitored on an ongoing basis to ensure issues are identified early and remedial action, where necessary is taken to restore effective capital performance and levels.

The company aims to have a mix of "hard" and "soft" capital that provides sufficient capital to satisfy APRA and ratings agencies of the company's financial strength, while at the same time avoids over capitalisation, which would unduly depress returns. Additional hard (share) capital is available from the QBE Group, subject to relevant approvals; reinsurance may be sourced externally or from within the QBE Group.

The company has a policy of paying dividends to shareholders to the extent that capital exceeds target levels and allowing for amounts required to support business growth and meet APRA and rating agency requirements.

The company manages its capital requirements against the following levels:

- Minimum levels set by APRA and the ratings agencies, which must be met at all times.
- "Trigger" levels set by management in consultation (where applicable) with APRA, as a guide to capital levels which require close monitoring, to ensure minimum standards are not breached.
- "Target" levels set by management in consultation (where applicable) with APRA, as a guide to capital levels, which if exceeded, may indicate the existence of surplus capital.

Regulatory capital	2010 $M	2009 $M
Capital		
Paid up ordinary shares	**364.3**	364.3
General reserves	**2.3**	5.4
Retained earnings (under APRA methodology[1])	**445.4**	745.3
Current year earnings net of tax (under APRA methodology[1])	**253.4**	180.3
Surplus on technical provisions net of tax	**255.3**	-
Tier 1 Capital - Total Capital Base	**1,320.7**	1,295.3
Minimum Capital Requirement	**830.5**	783.1
Capital Adequacy Multiple	**1.6**	1.7

[1] In 2010 APRA changed the calculation of retained earnings and current year earnings to align with IFRS and to exclude the surplus or deficit on technical provisions.

21. DIVIDENDS

	2010 $M	2009 $M
Dividends paid	**125.0**	-

A dividend payment of $75.0M has been recommended by the directors for the year ended 31 December 2010 (2009: $100M).

22. KEY MANAGEMENT PERSONNEL

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

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. No compensation is disclosed in respect of key management personnel who are employees of other entities within the QBE Group and are not compensated separately or additionally for their management of the company.

Key management personnel compensation for the years ended 31 December 2010 and 2009 is set out below:

	2010 $'000	2009 $'000
Short-term benefits	**3,340**	2,551
Post-employment benefits	**257**	365
Other long-term benefits	**16**	(22)
Termination benefits	**-**	-
Share-based payments	**165**	-
Total	**3,778**	2,894

23. REMUNERATION OF THE AUDITOR

	2010 $'000	2009 $'000
PricewaterhouseCoopers – Australian firm		
Assurance services		
Audit or review of financial reports of the company	**406**	694
Other services		
Special audits required by regulators	**107**	141
	513	835
Related practices of PricewaterhouseCoopers – Australian firm		
Other services		
Taxation services	**8**	19

24. CONTINGENT LIABILITIES

The company has given undertakings in respect of its 100% controlled entity, QBE Mortgage Insurance (Asia) Limited ("QBEMIA"), that whilst QBEMIA is a wholly owned controlled entity of the company, QBEMIA's statutory capital will not be less than US$50 million and that QBEMIA will maintain sufficient liquid assets to meet maturing obligations at all times.

25. CAPITAL COMMITMENTS

The company had no capital commitments as at 31 December 2010 (31 December 2009: nil).

26. COMMITMENTS FOR EXPENDITURE

The company has entered into commercial leases on property, motor vehicles and IT equipment. These leases have remaining lives of up to 5 years, and do not have renewal options. There are no restrictions placed upon the lessee by entering into these leases.

	2010 $M	2009 $M
Operating lease commitments		
Within 1 year	**3.2**	2.6
After 1 year but not more than 5 years	**3.8**	4.3
Total future lease payments under non-cancellable operating leases	**7.0**	6.9
Commitments under other agreements		
After 1 year but not more than 5 years	**9.7**	-
	9.7	-

27. RELATED PARTIES

(A) Parent and ultimate parent

The company's immediate parent company is QBE Holdings (AAP) Pty Limited ("QBE AAP"). Prior to 23 December 2009 the company's immediate parent company was QBE Lenders' Mortgage Insurance (Holdings) Pty Limited.

The company's ultimate parent company is QBE Insurance Group Limited ("QBE"), incorporated in Australia.

(B) The subsidiaries of the company are listed below:

Name	Country of Incorporation	Equity Interest 2010	Equity Interest 2009
Permanent LMI Pty Limited	Australia	50.1%	50.1%
QBE Mortgage Insurance (Asia) Limited	Hong Kong	100.0%	100.0%

(C) Related party transactions

(i) Controlled Entities

The company charges its controlled entities Permanent LMI Pty Limited ("Permanent") and QBE Mortgage Insurance (Asia) Limited ("MI Asia") for management services under normal terms and conditions.

The company has a reinsurance agreement with Permanent under normal terms and conditions. Additionally, the company has guaranteed claim payments on certain loans insured by Permanent under normal terms and conditions; the possibility of outflows in respect of this guarantee has been assessed as remote.

(ii) Other related entities

The company has excess of loss outward reinsurance arrangements with Equator Reinsurances Limited and QII Singapore branch, members of the QBE Group.

Investment management services for the company are performed by Minster Court Asset Management Pty Limited, a member of the QBE Group.

Effective 1 August 2009, employment contracts with all Australian employees of the company ceased and those employees commenced employment with a related party, QBE Management Services Pty Limited ("QMS"). Effective 17 August 2009, employment contracts with all New Zealand employees of the company ceased and those employees commenced employment with a related party, QII New Zealand Branch.

QMS and QII New Zealand branch charge the company management fees in respect of these arrangements for individuals directly supporting the company's activities. QMS additionally charges the company in respect of time and cost incurred in indirectly supporting the company's activities.

All arrangements were under normal terms and conditions.

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

Reference	
Revenue and expenses	Note 7(D)
Trade and other receivables	Note 12
Trade and other payables	Note 16

28. SHARE BASED PAYMENTS

Prior to 23 October 2008, certain directors and senior executives were eligible to be participants in an equity incentive plan ("the plan") for the granting of non-transferable options and restricted stock units ("RSU's") in the then ultimate parent company, The PMI Group ("TPG"). Only RSU's were granted in 2008. Future participation in the plan ceased following the acquisition of the company's parent by QBE AAP on 23 October 2008.

The key terms and conditions applicable to the options and RSU's granted under the plan included:

- Options and RSU's issued under the plan vested in three equal portions, progressively 1, 2 and 3 years after the grant date.
- Options and RSU's expired no later than the first to occur of the following events:
  - 10 years after the grant date;
  - 1 year after cessation of employment with the TPG Group for a reason other than retirement death or disability; or
  - 3 years after cessation of employment with the TPG Group due to disability or retirement.
- The exercise price of the options was set at the grant date and was based on the share price on the date of the grant. Upon exercise, options would be settled in ordinary shares of TPG.
- RSU's had a value equal to the TPG share price both at grant date and in the future. Upon vesting, RSU's would convert into actual TPG shares.

On 23 October 2008, all unvested options and RSU's were forfeited and the expiry date of vested options was reset to 22 October 2009 (unless scheduled to expire earlier). All options expired on or before 22 October 2009.

The following table illustrates the number (No.) and weighted average exercise price ("WAEP") in United States dollars of stock options issued under the plan.

	2010 No.	**WAEP USD**	2009 No.	WAEP USD
Outstanding at the beginning of the year	-	-	203,445	40.00
Forfeited during the year	-	-	-	-
Expired during the year	-	-	(203,445)	40.00
Outstanding at the end of the year	-	-	-	-
Exercisable at the end of the year	-	-	-	-

Stock options issued under the plan and outstanding at 1 January 2009 had the following exercise prices:

Expiry date	Price USD	2009 Number
28 February 2009	43.15	5,933
28 February 2009	48.30	3,100
7 March 2009	48.30	700
3 June 2009	35.21	2,000
30 June 2009	43.15	3,133
30 June 2009	48.30	1,766
22 October 2009	28.03	23,533
22 October 2009	38.80	35,000
22 October 2009	42.87	2,220
22 October 2009	38.17	44,800
22 October 2009	35.21	6,334
22 October 2009	35.09	3,000
22 October 2009	43.15	42,331
22 October 2009	48.30	29,595
		203,445

The above tables exclude 21,066 shares that were not recognised in accordance with AASB 2, as the options were granted on or before 7 November 2002.

29. EVENTS OCCURRING AFTER REPORTING DATE

There is, at the date of this report, no matter or circumstance that has arisen since 31 December 2010 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.

The company does not expect a material increase in claims incurred arising from the floods experienced in parts of Queensland, Victoria and New South Wales during January 2011. The company has established hardship procedures for borrowers experiencing temporary difficulties in meeting mortgage payments, and expects to work closely with lenders to help flood affected borrowers who need assistance in the months ahead.

QBE LENDERS' MORTGAGE INSURANCE LIMITED

New Zealand Branch

FINANCIAL STATEMENTS – 31 December 2010

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This financial report includes separate financial statements for QBE Lenders' Mortgage Insurance Limited New Zealand Branch (the "branch") as an individual entity. The financial report is presented in New Zealand Dollars.

The branch is a branch of QBE Lenders' Mortgage Insurance Limited (the "company") and is a reporting entity for the purposes of the Financial Reporting Act 1993. Its principal place of business is:

Level 6, AMP Centre, 29 Customs Street West,

Auckland

New Zealand

QBE LENDERS' MORTGAGE INSURANCE LIMITED

New Zealand Branch

The Board of Directors present the financial statements of QBE Lenders' Mortgage Insurance Limited New Zealand Branch for the year ended 31 December 2010 and the auditor's statement thereon.

Signed in accordance with a resolution of the directors made on 17 February 2011.

For and on behalf of the board.

The Hon. NF Greiner	I T Graham
Chairman	Director

QBE LENDERS' MORTGAGE INSURANCE LIMITED

New Zealand Branch

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2010

	NOTES	**2010**	2009
		$	$
REVENUE			
Premium revenue	5	**12,743,435**	7,561,290
Other revenue	5	**268,819**	254,676
Net fair value losses on financial assets	5	**(3,968)**	(10,387)
		13,008,286	7,805,579
EXPENSES			
Net outward reinsurance premium expense	6(A)	**996,725**	662,257
Gross claims incurred	7	**1,667,591**	4,224,205
Other expenses	6(C)	**3,116,307**	4,095,152
		5,780,623	8,981,614
Profit (loss) before income tax		**7,227,663**	(1,176,035)
Income tax expense (benefit)	8	**2,135,297**	(337,273)
Net profit (loss) after income tax attributable to equity holders of the company		**5,092,366**	(838,762)
OTHER COMPREHENSIVE INCOME		-	-
Income tax relating to components of other comprehensive income		-	-
Other comprehensive income after income tax		-	-
Total comprehensive income (expense) after income tax attributable to equity holders of the company		**5,092,366**	(838,762)

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

QBE LENDERS' MORTGAGE INSURANCE LIMITED

New Zealand Branch

BALANCE SHEET

As at 31 December 2010

	NOTES	**2010**	2009
		$	$
ASSETS			
Financial assets at fair value through profit or loss			
Cash and cash equivalents	9	4,717,469	3,729,830
Investments	10	515,059	519,026
Trade and other receivables	11	529,523	736,229
Current tax receivable		-	119,442
Non-reinsurance recoveries on outstanding claims	16(A)	60,516	29,569
Deferred insurance costs	12	2,583,661	2,462,237
Deferred tax assets	13	-	992,002
Total assets		8,406,228	8,588,335
LIABILITIES			
Trade and other payables	14	538,601	2,166,224
Current tax liabilities		527,117	-
Provisions	15	160,440	339,028
Deferred tax liabilities	13	471,457	-
Outstanding claims	16(A)	2,805,833	3,544,508
Unearned premium	17(A)	20,098,213	23,826,374
Total liabilities		24,601,661	29,876,134
Net liabilities		(16,195,433)	(21,287,799)
RESIDUAL EQUITY			
Head office account		(16,195,433)	(21,287,799)
Total equity		(16,195,433)	(21,287,799)

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

QBE LENDERS' MORTGAGE INSURANCE LIMITED

New Zealand Branch

STATEMENT OF CHANGES IN HEAD OFFICE ACCOUNT

For the year ended 31 December 2010

	Amount due from Head Office	Retained Earnings	Total
	$	$	$
At 1 January 2010	**(67,651,055)**	**46,363,256**	**(21,287,799)**
Profit after income tax	**-**	**5,092,366**	**5,092,366**
Other comprehensive income	**-**	**-**	**-**
Total comprehensive income	**-**	**5,092,366**	**5,092,366**
Net funding movements	**-**	**-**	**-**
At 31 December 2010	**(67,651,055)**	**51,455,622**	**(16,195,433)**
At 1 January 2009	(60,587,376)	47,202,018	(13,385,358)
Loss after income tax	-	(838,762)	(838,762)
Other comprehensive income	-	-	-
Total comprehensive expense	-	(838,762)	(838,762)
Net funding movements	(7,063,679)	-	(7,063,679)
At 31 December 2009	(67,651,055)	46,363,256	(21,287,799)

The above statement of changes in Head Office Account should be read in conjunction with the accompanying notes.

QBE LENDERS' MORTGAGE INSURANCE LIMITED

New Zealand Branch

NOTES TO FINANCIAL STATEMENTS

For the year ended 31 December 2010

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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

The financial report includes financial statements for QBE Lenders' Mortgage Insurance Limited New Zealand Branch (the "branch") as an individual entity. The branch is a branch of QBE Lenders' Mortgage Insurance Limited ("QBE LMI" or the "company") and is a reporting entity for the purposes of the Financial Reporting Act 1993.

For a complete understanding of the financial position of the company refer to the company's full financial statements as lodged with the Australian Securities and Investment Commission.

(A) Basis of preparation

The financial statements have been prepared in accordance with New Zealand equivalents to International Financial Reporting Standards ("NZIFRS"), other applicable Financial Reporting Standards, as appropriate for profit-oriented entities that qualify for and apply differential reporting concessions, and the requirements of the Financial Reporting Act 1993.

The presentation currency of these financial statements is New Zealand dollars.

The shareholders of the company have exercised their right under section 211(3) of the Companies Act 1993 and unanimously agreed that these financial statements need not comply with paragraphs (a), and (e) to (j) of section 211(1) of the Act.

Compliance with IFRS

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

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 recoveries at present value.

Differential reporting

The branch qualifies for differential reporting as it is not publicly accountable and there is no separation between the owners and the governing body. The branch has taken advantage of all differential reporting exemptions.

Going concern

The directors of the company believe that the branch has access to sufficient resources to meet its future liabilities and commitments. For this reason the directors continue to adopt the going concern assumption in the preparation of the branch financial statements.

(B) Insurance contracts

All of the insurance products offered or utilised by the branch meet the definition of insurance contracts under NZIFRS, and are accounted for and reported in accordance with these standards. These products do not contain embedded derivatives or deposits that are required to be unbundled.

(C) Premium revenue

Premium comprises amounts charged to policyholders. The earned portion of premium received and receivable is recognised as revenue. Premium is treated as earned from the date of attachment of risk.

(D) Unearned premium

Unearned premium is calculated based on the term of the policies written and the likely pattern in which risk will emerge over that term.

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 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 business segment level, being a portfolio of contracts that are broadly similar and managed together as a single portfolio. If the unearned premium liability, less deferred acquisition costs, is deficient, then the resulting deficiency is recognised in the through the profit or loss of the branch.

(E) Outward reinsurance

Premium ceded to reinsurers is recognised as an expense in accordance with the pattern of reinsurance service received. Where applicable, a portion of outward reinsurance premium is deferred at the balance 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"), and estimated claims handling costs. Claims expense represents claim payments adjusted for movements 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 non-reinsurance recoveries, to reflect the inherent uncertainty in the central estimate.

(G) Non-reinsurance recoveries

Non-reinsurance recoveries receivable on paid claims, reported claims not yet paid and IBNR 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.

(H) Acquisition costs

A portion of acquisition costs relating to unearned premium is deferred in recognition that it represents a future benefit. Deferred acquisition costs are measured at the lower of cost and recoverable amount. Deferred acquisition costs are amortised over the financial years expected to benefit from the expenditure in accordance with the premium income earning pattern adjusted for policy terminations.

(I) Commissions

Exchange commission is paid in accordance with the applicable insurance agreement on the basis of insurance premium assumed. Insurance exchange commission is recognised as an expense in accordance with the premium income earning pattern adjusted for policy terminations.

Profit commission is payable in accordance with the applicable agreements and based on the profitability of the underlying portfolio including the recognition of revenue and claims experience. It is recognised as the risk emerges in the underlying portfolio on a basis consistent with premium income.

(J) Investment income

Interest income is recognised on an accruals basis. 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.

(K) Taxation

The income tax expense for the period is the tax payable on the current period's taxable income based on the notional income tax rate, 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.

The current income tax asset or liability recognised on the Balance Sheet represents the current income tax balance due from or obligation to the Inland Revenue Department at balance date.

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, based on those tax rates which are enacted or substantively enacted for each jurisdiction. 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, other than a business combination, that at the time of the transaction 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.

Current and deferred tax balances attributable to amounts recognised directly in equity are also recognised directly in equity.

(L) Financial instruments

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

(i) Financial assets

The company has identified the following classes of financial asset: cash and cash equivalents, investments, and trade and other receivables.

(ii) Financial liabilities

The company has identified the following class of financial liability: trade and other payables.

(iii) Financial instruments designated as fair value through profit or loss

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.

(M) 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 in the cash management function on a day to day basis.

(N) Investments

All 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. Fair value for each type of investment is determined as follows:

For securities traded in an active market, the fair value is determined by reference to published closing bid price quotations. For securities that are not traded and securities that are traded in a market that is not active, fair value is determined using valuation techniques generally be reference to the fair value of recent arm's length transactions involving the same or similar instruments. Fixed and floating rate securities are valued using independently sourced valuations that do not involve the exercise of judgement by management.

All purchases and sales of financial assets that require delivery of the asset within the timeframe 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 assets has expired, or has been transferred, and the branch has transferred substantially all the risks and rewards of ownership.

(O) Receivables

Receivables are recognised and carried at original invoice amount less a provision for any 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 the 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 the profit or loss.

(P) Property, plant and equipment

Property, plant and equipment is stated at historical cost less accumulated depreciation.

Leasehold improvements, office equipment and fixtures and fittings are depreciated using the straight line method over the estimated useful life to the branch 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 to note 1(Q).

(Q) Impairment of assets

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 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.

(R) Employee Benefits

Effective 17 August 2009, employment contracts with all employees of the branch ceased and those employees commenced employment with a related party, QBE Insurance (International) Limited ("QII") New Zealand branch. As a result of the changes to employee contracts, the branch ceased incurring employment related expenses and now incurs equivalent management fee expenses payable to the new employers. In addition the branch ceased providing for employee related expenses such as annual and long service leave, as the new employers make these provisions and recharge the branch.

Prior to the cessation of the above employment contracts:

- Accrual was made for employee entitlement benefits accumulated as a result of employees rendering services up to that date. These benefits include salaries, bonuses, annual leave and long service leave.
- Liabilities arising in respect of salaries, bonuses, annual leave and any other employee entitlements expected to be settled within 12 months of the reporting date were measured at their nominal amounts.

- Provision for long service leave was 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 date were discounted to present value.
- Contributions made to defined contribution superannuation funds by the branch were expensed as incurred.

(S) Provisions

Provisions are recognised when the branch has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

(T) Leases

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

(U) Goods and services tax (GST)

GST incurred is not recoverable from the Inland Revenue Department. GST is recognised as part of the cost of acquisition of an asset or as part of an item of expense. Receivables and payables in the balance sheet are shown inclusive of GST.

Commitments are disclosed inclusive of GST.

(V) Comparative figures

Comparative figures have been adjusted, where necessary, to conform to the basis of presentation and the classification used in the current year.

2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The branch 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 actuaries and management 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 below.

(A) Ultimate liability arising from claims made under insurance contracts

Provision is made for the estimated cost of claims incurred but not settled at the balance date. This provision consists of estimates of both the expected ultimate cost of claims notified to the branch as well as the expected ultimate cost of claims incurred but not reported to the branch ("IBNR"). The estimated cost of claims includes direct expenses that are expected to be incurred in settling those 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. The longer the delay between the event giving rise to the claim and final claim settlement, the greater the variability between initial estimates of the loss to be incurred and the final settlement amount, as a result of additional financing and settlement costs incurred by the lender and changes in property valuations.

The estimation techniques and assumptions used in determining the outstanding claims provision and the associated non-reinsurance recoveries are described below.

(i) Insurance risk assumptions

The branch's process for establishing the outstanding claims provision involves extensive consultation with actuaries, claims managers, and other senior management. This process includes regular internal claims review meetings attended by senior management and detailed review by an external actuaries at least annually.

The determination of the amounts that the branch will ultimately pay for claims arising under insurance 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 during the time that elapses before a definitive determination of the ultimate claims cost can be made;
- changes in the legal environment; and
- social and economic trends, for example house price inflation, unemployment and interest rates.

The potential impact of changes in key assumptions on the branch's statement of comprehensive income and balance sheet are summarised in note 2(A)(vi).

(ii) Central estimates

The outstanding claims provision comprises the central estimate and a risk margin which is added to the central estimate to achieve a desired probability of adequacy. The outstanding claims provision is discounted at risk-free rates of return to reflect the time value of money.

A central estimate is an estimate of the level of claims provision that is intended to contain no intentional under or over estimation. As the branch requires a higher probability that estimates will be adequate over time, a risk margin is added to the central estimate of outstanding claims.

Central estimates 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 estimate is based on a judgmental consideration of the results of each method and qualitative information, for example:

- Historical trends in the development and incidence of the numbers of defaults reported, numbers of defaults cured, numbers of properties taken into possession, numbers of such properties sold, numbers of claims arising from these sales, and the costs of those claims;
- Exposure details, including policy counts, sums insured and various other characteristics of the borrowers and loans;
- Historical and likely future trends of expenses associated with managing claims to finalisation.

Central estimates are calculated gross of any non-reinsurance recoveries. A separate estimate is made of the amounts recoverable from reinsurers, borrowers and third parties based on the gross outstanding claims provision.

(iii) Risk margin

Risk margins are held to mitigate the potential for uncertainty in the outstanding claims estimation process. The determination of the appropriate level of risk margin takes into account the uncertainty or variability inherent in the branch's business and the diversification benefits achieved by writing business in a number of geographic locations and with different lenders.

The measurement of variability 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. The use of a range of outcomes allows a determination of the risk margin required to provide an estimate at a given probability of adequacy, e.g. nine times in ten (a 90% probability of adequacy). These techniques use standard statistical distributions, and the measure of variability is referred to as the standard deviation or the coefficient of variation.

The directors and management have set an internal target of 75% or above for the probability of adequacy of the net outstanding claims provision. The Australian Prudential Regulation Authority ("APRA") requires a probability of adequacy of 75% for the determination of the minimum capital requirement. For the actual probability of adequacy applied at the end of the financial year, refer to note 16(B).

(iv) Expected present value of future cash flows for future claims

The expected present value of future cash flows for future claims and risk margin used in the liability adequacy test (refer note 17(C)) are determined using the same methods described above.

(v) Assumptions used to determine the outstanding claims provision

	2010	2009
Severity	30.0%	27.6%
Claim rates	18.6%	29.2%
Recovery rates	1.0%	0.5%
Risk margin (as a proportion of central estimate)	26.0%	26.0%

Severity is a measure of the anticipated claims cost relative to the corresponding risk exposures.

Claim rate is the percentage of current defaults that are expected to become claims.

Recovery rate is a measure of anticipated non-reinsurance recoveries in claims.

The percentages adopted in the actuarial model are determined based on an analysis of historical experience combined with actuarial and management judgement of future trends.

The outstanding claims provision is discounted to net present value using a risk free rate of return. Details of the risk free rates of return are summarised below:

	2010		2009	
	Average of succeeding year	**Average of subsequent years**	Average of succeeding year	Average of subsequent years
Discount factor	**4.8%**	**5.4%**	4.1%	5.3%

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

The impact of changes in key outstanding claims variables 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 and equity assuming that there is no change to:

- any of the other variables; and
- the probability of adequacy

It is likely that if, for example, the central estimate was to increase by 5%, at least part of the increase would result in a decrease in the probability of adequacy.

		2010		2009	
Variable	Change in assumptions	**Revised Variable**	**Impact on Profit (Loss) and Equity** [1]	Revised Variable	Impact on Profit (Loss) and Equity [1]
			$		$
Severity	+20%	36.0%	(395,324)	33.1%	(492,107)
	-20%	24.0%	395,324	22.1%	492,107
Claim rates	+20%	22.3%	(395,324)	35.1%	(492,107)
	-20%	14.9%	395,324	23.4%	492,107
Recovery rates	+20%	1.2%	8,834	0.6%	8,232
	-20%	0.8%	(8,834)	0.4%	(8,232)
Discount factors	+20%	6.7%	23,440	5.7%	24,446
	-20%	4.5%	(23,440)	3.8%	(24,446)
Risk Margin	+20%	31.2%	(107,083)	31.2%	(125,653)
	-20%	20.8%	107,083	20.8%	125,653

[1] Assumes taxation at prima facie rate of 30%.

(B) Unearned premium liabilities and deferred acquisition costs

As highlighted in note 1(C), premium is earned based on the term of the policies written and the likely pattern in which risk will emerge over that term. An actuarial analysis of the emergence of risk over the life of a policy is performed annually and is used to derive an earning pattern for each underwriting year. Premium is earned and acquisition costs recognised in accordance with this pattern.

During the year, the risk of an extended period of claims emergence as a result of the Global Financial Crisis was considered to have abated. Consequently, the earning patterns adopted in 2008 were revised across all underwriting years to reflect the latest actuarial view of long term average risk emergence. This reduced the branch's unearned premium liability by $4,555,119, and deferred insurance costs by $530,455.

Given the unpredictable pattern of future policy terminations it is not practical to reliably estimate the impact of these changes in individual future periods.

3. RISK MANAGEMENT

(A) Governance

The Board of Directors must ultimately be satisfied that appropriate, adequate and effective risk management systems are in place, and that these systems are operating effectively in practice, having regard to the risks they aim to control. The Board reviews key risk management information to satisfy itself in this regard and reviews and approves the risk management and reinsurance management strategies annually.

Day to day management, including implementation of strategies, policies and processes that support the risk management framework approved by the Board, is undertaken by executive management. Additional assurance is received from the appointment of an Appointed Actuary and an Appointed Auditor, as well as an internal audit function.

The company is also subject to the governance and risk management practices of its ultimate parent company.

The company has a risk management strategy for identifying, managing, monitoring and reporting on risks that could have a material impact on its operations.

The company's risk management objectives are to:

- adequately price risk;
- avoid unwelcome surprises by reducing uncertainty and volatility;
- achieve competitive advantage through better understanding the risk environment in which the company operates;
- optimise risk and more efficiently allocate capital and resources by assessing the balance of risk and reward;
- comply with laws and internal procedures; and
- improve resilience to external events.

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 company has established internal controls to manage risk in the key areas of exposure relevant to its business. The broad risk categories discussed below are:

- insurance risk;
- reinsurance counterparty risk;
- operational risk; and
- capital and regulatory risk.

Within each of these categories, risks are evaluated before consideration of the impact of mitigating controls. The existence and effectiveness of such mitigating controls are then measured to ensure that residual risks are managed within risk tolerance.

(B) Insurance Risk

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 risks are that the premiums charged do not adequately remunerate the company for the risk it assumes, and that the ultimate claims payments will exceed the carrying amount of the provision established.

The following protocols have been established to manage insurance risk:

(i) Underwriting risks

Selection and pricing of risks

The branch offers lenders' mortgage insurance (LMI) in New Zealand. LMI insures the lender should the borrower default on repayment of the loan, and covers the remaining loan balance, plus selling costs and expenses, following the application of the proceeds from the sale of the security property.

LMI is characterised by coverage of 100% of the loan amount, however insurance coverage may also be "top cover", where the total loss (including expenses) is paid up to a prescribed percentage of the original loan amount. Typical top cover in New Zealand ranges from 20% to 30% of the original loan amount.

Key risk mitigation policies and procedures comprise:

- the pricing model and policies measure return on capital and reflects risks on a long term cyclical performance basis for both standard and new products. Pricing tables are set according to appropriate risk characteristics, such as type of product, loan amounts and loan valuation ratio.
- standard insurance agreements and documented underwriting policies and procedures are in place with allocation of delegated authority levels to approve applications.

- quality assurance reviews of underwriting and claims managements are conducted on a regular basis.

Credit risk arising from insurance contracts

Credit risk arising from insurance contracts principally relates to the risk of default by borrowers and reinsurers.

As insurer, the branch does not require access to the current credit quality of performing insured loans but is provided with data on loans in default by insured lenders. The relevant LMI master policy defines "default" as the borrower's failure to pay when due an amount equal to the scheduled monthly mortgage payment under the terms of the mortgage. Generally, however, the master policies require an insured to notify the insurer of a default within 14 days of the end of the month when the total amount due is unpaid and in arrears by more than 60 days. For reporting and internal tracking purposes, the branch does not consider a loan to be in default until it has been delinquent for two consecutive monthly payments.

Credit risk on LMI contracts is therefore principally managed up-front through the underwriting process, prior to the acceptance of risk. The company has a centralised credit risk function that incorporates pricing, claims liability modelling, credit policy, portfolio performance reporting and analysis, and underwriting quality assurance.

Acceptance of credit risk is managed primarily using two scorecards, built on credit bureau data and company portfolio history. Credit rules are used to support these two scorecards. The centralised credit risk unit manages and maintains the scorecards and a centralised underwriting policy and procedure.

Lenders usually collect the single premium from a prospective borrower and remit the amount to the branch; generally, under a standard LMI policy, premium payment is required before policy cover is incepted, which eliminates credit risk on premiums receivable.

The branch does not hold any collateral as security against its exposures; however, in the event of a claim by the lender, the lender's rights as mortgagee are assigned to the branch.

Concentration risk

Concentration risk is the risk of exposure due to concentration of activity in certain geographical locations, industries or counterparties.

The branch operates throughout New Zealand and therefore has limited geographic concentration risk on insurance contracts; exposures are monitored but not limited by region. Limits, such as those placed on maximum aggregate exposures to individual borrowers and per property, are contained in underwriting policies and are embedded in systems and processes.

(i) Claims management and claims provisioning risks

The approach to determining the outstanding claims provision and the related sensitivities are set out in note 2. The adequacy of outstanding claims provision is determined with reference to the following controls:

- experienced claims managers operate within policy and within the levels of authority delegated to them in respect of the settlement of claims;
- processes exist to ensure that all defaults are captured and updated on a timely basis and with a realistic assessment of the ultimate claims cost;
- initial IBNR estimates are set by experienced internal actuaries in conjunction with management;
- the outstanding claims provision is assessed regularly by senior management and is reviewed by the external Appointed Actuary at least annually.

(C) Reinsurance counterparty risk

Reinsurance risk management is the process of transferring insurance risk to another insurer for a price. The branch reinsures a portion of risks underwritten to control exposure to insurance losses, reduce volatility and protect capital. The strategy in respect of the selection, approval and monitoring of reinsurance arrangements is addressed by the following protocols at corporate level:

- reinsurance is placed in accordance with a reinsurance management strategy approved by the Board, which in turn is consistent with the QBE Group reinsurance management strategy and QBE Group security committee guidelines;
- reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historical and potential future losses; and
- exposure to reinsurance counterparties and the credit quality of those counterparties is actively monitored.

The branch's current reinsurance arrangements are disclosed within note 22(B).

(D) Operational Risk

Operational risk is the risk of loss arising from system failure or inadequacies, human error or external events that does not relate to insurance, acquisition, capital and regulatory or financial risks. Operational risk is managed at corporate level within the same robust control framework as its other risks. One of the cornerstones of the 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.

(E) Capital management risk

The company is subject to extensive prudential regulation covering the jurisdictions in which it conducts business. Prudential regulation is generally designed to protect the policyholders. Regulation covers a number of areas including solvency, change in control and capital movement limitations. The regulatory environment in Australia continues to evolve in response to economic, political and industry developments. The company works closely with regulators and monitors regulatory developments to assess their potential impact on its ability to meet solvency and other requirements.

4. FINANCIAL RISK

(A) Risk management practices

As outlined in Note 3, an overall risk management strategy is approved annually by the Board of Directors. While specific risk strategies have been developed and responsibilities assigned in connection with risks arising from financial instruments by the company, the branch has very restricted exposure to financial instruments.

Except where otherwise noted, the risks and exposures at the end of the financial year are representative of those that occurred during the financial year.

(B) Credit risk

Credit risk is the risk that a loss will be incurred because customers or counterparties to financial instruments fail to discharge their contractual obligations.

The branch's principal exposure to credit risk from financial instruments arises from the branch's holdings of cash and cash equivalents and amounts due from reinsurers.

Maximum exposures to credit risk at balance date in relation to each class of recognised financial asset is the carrying amount of those assets as indicated in the balance sheet.

There are no significant credit enhancements or collateral held as security that reduce the exposure to credit risk (2009: Nil). The branch has not taken possession of collateral or called upon credit enhancements during the year (2009: Nil).

None of the branch's financial assets are past due or impaired or have terms that have been renegotiated and would otherwise have been past due or impaired (2009: Nil).

All cash and cash equivalent balances are held with registered banks in New Zealand.

(C) 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 market prices on assets and non-insurance liabilities. The branch is exposed to interest rate risk and currency risk.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The branch's principal exposure to interest rate risk arises from investments in financial assets at fair value through profit or loss. The branch minimises interest rate risk by investing in high quality, liquid fixed interest securities and cash.

The 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 below:

		FIXED INTEREST RATE MATURING IN						
	Floating interest rate	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 2010								
Interest bearing financial assets ($M)	**4,717,469**	**515,059**	-	-	-	-	-	**5,232,528**
Weighted average interest rate (%)	**2.68%**	**6.00%**	-	-	-	-	-	**3.01%**
At 31 December 2009								
Interest bearing financial assets ($M)	3,729,830	-	519,026	-	-	-	-	4,248,856
Weighted average interest rate (%)	2.50%	-	6.00%	-	-	-	-	2.92%

The branch's sensitivity to movements in interest rates in terms of changes in net interest income, for one year for interest bearing financial assets based upon year end balances is shown in the table below:

		Financial impact [1]			Financial impact [1]	
	Movement in variable	**Profit (loss) 2010**	**Equity 2010**	Movement in variable	Profit (loss) 2009	Equity 2009
	%	**$**	**$**	%	$	$
Interest rate movement – interest-bearing financial assets	**+1.0**	33,022	33,022	+1.5	39,163	39,163
	–1.0	(33,022)	(33,022)	–1.5	(39,163)	(39,163)

[1] Assumes taxation at prima facie rate of 30%.

The effect of interest rate risk on the branch's provision for outstanding claims is included in note 2(A)(vi).

(ii) Currency risk

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

The branch is exposed to currency risk in respect of amounts due from or payable to related parties denominated in Australian dollars.

Foreign currency balances are actively monitored and exposures kept to acceptable levels.

(D) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial and insurance liabilities as and when they fall due. Liquidity risk management forms an integral part of the overall risk management strategy, as the majority of the branch's liabilities relate to insurance contracts.

The nature of the business is that cash is received by way of single premiums at the inception of insurance contracts and is invested to fund future claims on those contracts. The principal sources of funds are written premiums, and net investment income. The principal uses of funds are the payment of operating expenses, claim payments, taxes and transfer of surplus funds to Head Office.

The key elements of the liquidity risk management for the branch are as follows:

- Cash requirements are monitored regularly by management.
- Sufficient cash and cash equivalents are set aside for operating requirements of the business.

The branch aims to be self-sufficient in terms of cash flow. Surplus cash flows are transferred to the company in Australia, and conversely cash flow deficits, if any, are supported by the company.

The following table summarises the maturity profile of financial liabilities, based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately; however, it is not expected that all creditors will request payment on the earliest date the branch could be required to pay.

	Note	1 Year or Less	1 to 3 Years	3 to 5 Years	Over 5 Years	Total
		$	$	$	$	$
As at 31 December 2010						
Balance sheet financial liabilities:						
Trade and other payables	**14**	**438,601**	**100,000**	**-**	**-**	**538,601**
Total		**438,601**	**100,000**	**-**	**-**	**538,601**
As at 31 December 2009						
Balance sheet financial *liabilities:*						
Trade and other payables	**14**	2,166,224	-	-	-	2,166,224
Total		2,166,224	-	-	-	2,166,224

5. REVENUE

	2010	2009
	$	$
Premium revenue		
Direct	**12,743,435**	7,561,290
Other revenue		
Non-reinsurance recoveries	**134,584**	49,807
Interest income	**128,421**	204,869
Other income	**5,814**	-
	268,819	254,676
Net fair value (losses) on financial assets	**(3,968)**	(10,387)
Revenue	**13,008,286**	7,805,579

6. PROFIT BEFORE INCOME TAX

(A) Profit before income tax

	NOTES	2010	2009
		$	$
Gross written premium		**9,015,274**	10,536,843
Unearned premium movement		**3,728,161**	(2,975,553)
Gross earned premium		**12,743,435**	7,561,290
Net outward reinsurance premium		**(1,761,889)**	(662,257)
Deferred reinsurance premium movement		**765,164**	-
Net outward reinsurance premium expense		**(996,725)**	(662,257)
Net earned premium		**11,746,710**	6,899,033
Gross claims incurred		**(1,667,591)**	(4,224,205)
Non-reinsurance recoveries		**134,584**	49,807
Net claims incurred	7	**(1,533,007)**	(4,174,398)
Commission expenses		**(195,877)**	(585,691)
Other acquisition costs		**(1,208,542)**	(837,349)
Underwriting and other expenses		**(1,710,285)**	(2,672,112)
		(3,114,704)	(4,095,152)
Underwriting profit (loss)		**7,098,999**	(1,370,517)
Net investment income	6(B)	**122,850**	194,482
Other income		**5,814**	-
Profit (loss) before income tax		**7,227,663**	(1,176,035)

(B) Net investment income

	2010	2009
	$	$
Interest received or receivable from non-related entities	**128,421**	204,869
Net unrealised losses on fixed interest	**(3,968)**	(10,387)
Investment expenses	**(1,603)**	-
Net investment income	122,850	194,482

(C) Other Expenses

	2010	2009
	$	$
Commission expenses	**195,877**	585,691
Other acquisition costs	**1,208,542**	837,349
Underwriting and other expenses	**1,710,285**	2,672,112
	3,114,704	4,095,152
Investment expenses	**1,603**	-
Other expenses	**3,116,307**	4,095,152

(D) Specific Items

	2010	2009
	$	$
Claims settlement expenses	**307,541**	18,745
Employee benefit expense	**-**	14,966
Operating lease payments	**37,138**	372,386
Depreciation of plant and equipment	**-**	11,219
Related party transactions:		
Management fees paid or payable to Head Office	**2,050,378**	2,009,052
Management fees paid or payable to related entity	**372,415**	187,640
Reinsurance premiums paid or payable to related entities, net of no claims bonus	**1,761,889**	574,938

7. CLAIMS INCURRED

(A) Claims analysis

	2010	2009
	$	$
Gross claims incurred		
Direct	**1,667,591**	4,224,205
Non-reinsurance recoveries		
Direct	**(134,584)**	(49,807)
Net claims incurred	**1,533,007**	4,174,398

(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 the previous reporting periods.

	2010			2009		
	Current Year	Prior Years	Total	Current Period	Prior Years	Total
	$	$	$	$	$	$
Gross claims incurred and related expenses						
Undiscounted	**3,178,617**	**(1,519,458)**	**1,659,159**	5,100,013	(825,257)	4,274,756
Discount	**(121,324)**	**129,756**	**8,432**	(128,921)	78,370	(50,551)
	3,057,293	**(1,389,702)**	**1,667,591**	4,971,092	(746,887)	4,224,205
Non-reinsurance recoveries						
Undiscounted	**(60,213)**	**(76,054)**	**(136,267)**	43,983	(90,742)	(46,759)
Discount	**2,706**	**(1,023)**	**1,683**	1,104	(4,152)	(3,048)
	(57,507)	**(77,077)**	**(134,584)**	45,087	(94,894)	(49,807)
Net claims incurred						
Undiscounted	**3,118,404**	**(1,595,512)**	**1,522,892**	5,143,996	(915,999)	4,227,997
Discount	**(118,618)**	**128,733**	**10,115**	(127,817)	74,218	(53,599)
	2,999,786	**(1,466,779)**	**1,533,007**	5,016,179	(841,781)	4,174,398

The development of net undiscounted outstanding claims for the four most recent accident years is shown in note 16(D).

8. INCOME TAX

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

	2010	2009
	$	$
Profit (loss) before income tax	**7,227,663**	(1,176,035)
Prima facie tax payable (receivable) at 30%.	**2,168,299**	(352,810)
Tax effect of permanent differences:		
Non allowable expenses and non taxable income	**674**	1,256
Prima facie tax adjusted for permanent differences	**2,168,973**	(351,554)
Under-provision in prior year	**-**	14,281
Change in tax rate	**(33,676)**	-
Income tax expense (benefit)	**2,135,297**	(337,273)
Analysed as follows:		
Current tax	**982,910**	(256,067)
Deferred tax	**1,186,063**	(95,487)
Under-provision in prior year	**-**	14,281
Change in tax rate	**(33,676)**	-
	2,135,297	(337,273)
Deferred tax (credit) expense comprises:		
Deferred tax assets charged to profit or loss	**1,573,333**	47,595
Deferred tax liabilities credited to profit or loss	**(387,270)**	(143,082)
	1,186,063	(95,487)

Effective to the branch 1 January 2011, the rate of corporate tax will reduce from 30% to 28%. Deferred tax assets and liabilities at 31 December 2010 have been restated in line with the lower rate.

9. CASH AND CASH EQUIVALENTS

	2010	2009
	$	$
Cash at bank and on hand	**940,333**	4,304
Overnight money	**3,777,136**	3,725,526
Cash and cash equivalents	**4,717,469**	3,729,830

Cash and cash equivalents earn interest at floating rates based on daily bank deposit rates.

10. INVESTMENTS

	2010	2009
	$	$
Interest bearing securities		
New Zealand Government bond	**515,059**	519,026
Interest bearing securities	**515,059**	519,026
Amounts maturing within 12 months	**515,059**	-
Amounts maturing in greater than 12 months	**-**	519,026
Interest bearing securities	**515,059**	519,026

Interest bearing securities mature in less than 1 year (2009: 1-2 years).

The branch is required to have a security deposit with a face value of $500,000 with the New Zealand Public Trust Office. There are no restrictions on use of the branch's other assets.

11. TRADE AND OTHER RECEIVABLES

	2010	2009
	$	$
Amounts due from reinsurers - related entity	**81,298**	732,435
Prepayments	**444,444**	-
Accrued investment income	**3,781**	3,794
Trade and other receivables	**529,523**	736,229
Amounts maturing within 12 months	**251,745**	736,229
Amounts maturing in greater than 12 months	**277,778**	-
Trade and other receivables	**529,523**	736,229

12. DEFERRED INSURANCE COSTS

	2010	2009
	$	$
Deferred reinsurance premium	**765,164**	-
Deferred commission	**-**	183,351
Deferred acquisition costs	**1,818,497**	2,278,886
Deferred insurance costs	**2,583,661**	2,462,237
To be expensed within 12 months	**1,321,885**	592,344
To be expensed in greater than 12 months	**1,261,776**	1,869,893
Deferred insurance costs	**2,583,661**	2,462,237

	Deferred reinsurance premium $	Deferred commission $	Deferred acquisition costs $	Total $
Deferred costs at 1 January 2009	-	652,659	2,618,989	2,462,237
Costs deferred in financial year	-	-	457,459	457,459
Amortisation of costs deferred in previous financial years	-	(469,308)	(797,562)	(1,266,870)
Deferred costs at 31 December 2009	**-**	**183,351**	**2,278,886**	**2,462,237**
Costs deferred in financial year	**765,164**	-	**655,382**	**1,420,546**
Amortisation of costs deferred in previous financial years	-	**(105,886)**	**(662,781)**	**(768,667)**
Additional release (note 2 (B))	-	**(77,465)**	**(452,990)**	**(530,455)**
Deferred costs at 31 December 2010	**765,164**	**-**	**1,818,497**	**2,583,661**

13. DEFERRED INCOME TAX

	2010	2009
	$	$
Deferred tax assets	**61,599**	1,895,399
Deferred tax liabilities	**(533,056)**	(903,397)
	(471,457)	992,002

(A) Deferred tax assets – maturing in greater than 12 months

The balance comprises temporary differences attributable to:

	2010	2009
	$	$
Amounts recognised in profit or loss		
Insurance liabilities	**-**	1,509,175
Tax losses	**-**	256,067
Other items	**61,599**	130,157
	61,599	1,895,399
Set-off deferred tax liabilities	**(61,599)**	(903,397)
	-	992,002

(B) Tax losses

The branch qualifies as a permanent establishment for New Zealand tax purposes, and consequently lodges income tax returns and pays income tax in New Zealand as though it were a separate entity. Tax losses generated by the branch may be transferred to other New Zealand entities provided that the receiving entity shares 100% common ownership with the branch. 2009 tax losses were transferred to QBE Insurance (International) Limited New Zealand branch during the 2010 financial year. The branch received full consideration for the tax value of the losses transferred

(C) Deferred tax liabilities – maturing in greater than 12 months

The balance comprises temporary differences attributable to:

	2010	2009
	$	$
Amounts recognised in profit or loss		
Insurance assets	**509,179**	683,666
Other receivables	**23,877**	219,731
	533,056	903,397
Set-off of deferred tax assets	**(61,599)**	(903,397)
	471,457	-

14. TRADE AND OTHER PAYABLES

	2010	2009
	$	$
Amount due to Head Office	**170,414**	1,662,907
Amount due to related entities	**39,597**	66,499
Bank overdraft	**-**	251,985
Trade payables	**261,504**	97,560
Other payables	**67,086**	87,273
Trades and other payables	**538,601**	2,166,224
Amounts payable within 12 months	**438,601**	2,166,224
Amounts payable in greater than 12 months	**100,000**	-
Trades and other payables	**538,601**	2,166,224

15. PROVISIONS

	Other provisions $	Total $
2010		
At 1 January	**339,028**	**339,028**
Amounts paid	**(178,588)**	**(178,588)**
At 31 December	**160,440**	**160,440**
Amounts payable within 12 months	**160,440**	**160,440**
At 31 December	**160,440**	**160,440**

	Long service leave $	Other provisions $	Total $
2009			
At 1 January	10,809	-	10,809
Amounts (credited) charged to profit or loss	(10,809)	339,028	328,219
At 31 December	-	339,028	339,028
Amounts payable within 12 months	-	178,588	178,588
Amounts payable in greater than 12 months	-	160,440	160,440
At 31 December	-	339,028	339,028

16. OUTSTANDING CLAIMS

(A) Net outstanding claims

	2010 $	2009 $
Gross outstanding claims	**2,859,823**	3,607,269
Claims settlement costs	**73,680**	73,341
	2,933,503	3,680,610
Discount to present value	**(127,670)**	(136,102)
Gross outstanding claims provision	**2,805,833**	3,544,508
Less than 12 months	**1,508,699**	2,003,970
Greater than 12 months	**1,297,134**	1,540,538
Gross outstanding claims provision	**2,805,833**	3,544,508
Non-reinsurance recoveries on outstanding claims	**63,364**	30,734
Discount to present value	**(2,848)**	(1,165)
Non-reinsurance recoveries on outstanding claims	**60,516**	29,569
Less than 12 months	**32,540**	16,718
Greater than 12 months	**27,976**	12,851
Non-reinsurance recoveries on outstanding claims	**60,516**	29,569
Net outstanding claims	**2,745,317**	3,514,939
Central estimate	**2,178,824**	2,789,633
Risk margin	**566,493**	725,306
Net outstanding claims	**2,745,317**	3,514,939

(B) Risk margins

The probability of adequacy at 31 December 2010 is 75% (2009: 75%) - 75% is a recognised industry benchmark in Australia, being the minimum probability of adequacy required for Australian licensed insurers by APRA. The risk margin included in net outstanding claims is 26% (2009: 26%) of the central estimate.

The process used to determine risk margins is explained in note 2(A)(iii).

(C) Reconciliation of movement in discounted outstanding claims provision

	2010			2009		
	Gross	Non-reinsurance Recoveries	Net	Gross	Non-reinsurance Recoveries	Net
	$	$	$	$	$	$
At 1 January	**3,544,508**	**(29,569)**	**3,514,939**	2,665,932	(130,625)	2,535,307
Increase in net claims incurred in current accident year	**3,057,293**	**(57,507)**	**2,999,786**	4,971,092	45,088	5,016,180
Movement in prior year claims provision	**(1,389,702)**	**(77,077)**	**(1,466,779)**	(746,887)	(94,895)	(841,782)
Incurred claims recognised in profit or loss	**1,667,591**	**(134,584)**	**1,533,007**	4,224,205	(49,807)	4,174,398
Claims (payments) recoveries	**(2,406,266)**	**103,637**	**(2,302,629)**	(3,345,629)	150,863	(3,194,766)
At 31 December	**2,805,833**	**(60,516)**	**2,745,317**	3,544,508	(29,569)	3,514,939

(D) Claims development

(i) Net undiscounted outstanding claims for the branch for the four most recent accident years.

	2007	2008	2009	2010	Total
	$	$	$	$	$
Estimate of net ultimate claims cost:					
At end of accident year	313,554	2,937,785	4,241,295	2,460,142	
One year later	953,606	2,628,628	3,054,397		
Two years later	1,131,152	2,720,403			
Three years later	1,117,932				
Current estimate of net cumulative claims cost	1,117,932	2,720,403	3,054,397	2,460,142	9,352,874
Cumulative net payments	1,117,932	2,715,941	2,948,013	341,022	7,122,908
Net undiscounted claims for the four most recent accident years	**-**	**4,462**	**106,384**	**2,119,120**	**2,229,966**

(ii) Reconciliation of net undiscounted outstanding claims for the four most recent accident years to outstanding claims

	2010
	$
Net undiscounted claims for the four most recent accident years	**2,229,966**
Outstanding claims – accident years 2005 & prior	**-**
Discount on outstanding claims	**(124,822)**
Claims settlement costs	**73,680**
Risk margin	**566,493**
Net outstanding claims at 31 December 2010	**2,745,317**

(iii) Commentary

Favourable arrears and claims experience in the past year have given rise to the release of risk margins and central estimates for prior years, as ultimate claim costs were settled or became more certain at a lower level than previously expected. Despite this trend, there was a small increase in net ultimate claims cost for the 2008 accident year, due to a small number of larger than expected claims that were paid in 2010.

Conditions and trends that have affected the development of the liabilities in the past may, or may not, occur in the future, and accordingly, conclusions about future results may not necessarily be derived from the information presented in the tables.

(E) Expected maturity

The expected maturity of the branch's 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 2010	**1,476,159**	**842,654**	**305,068**	**87,448**	**33,988**	**-**	**2,745,317**
At 31 December 2009	1,987,252	1,058,993	346,983	90,101	31,610	-	3,514,939

The weighted average term to settlement of the branch's net outstanding claims provision at the balance date 1.2 years (2009: 1.1 years).

17. UNEARNED PREMIUM

(A) Unearned premium

	Note	2010 $	2009 $
At 1 January		**23,826,374**	20,850,821
Deferral of premium on contracts written in the period		**7,863,197**	9,652,313
Earning of premium written in previous periods		**(7,036,239)**	(6,676,760)
Additional release	2(B)	**(4,555,119)**	-
At 31 December		**20,098,213**	23,826,374
Amounts to be earned within 12 months		**6,195,007**	5,838,454
Amounts to be earned in greater than 12 months		**13,903,206**	17,987,920
At 31 December		**20,098,213**	23,826,374

(B) Net premium liabilities

	Note	2010 $	2009 $
Unearned premium		**20,098,213**	23,826,374
Deferred insurance costs	12	**(2,583,661)**	(2,462,237)
Net premium liabilities		**17,514,552**	21,364,137

(C) Expected present value of net future cash flows for future claims

	2010 $	2009 $
Undiscounted central estimate	**3,851,968**	2,130,721
Risk margin	**1,733,385**	1,065,371
	5,585,353	3,196,092
Discount to present value	**(946,519)**	(597,211)
Expected present value of net future cash flows for future claims including risk margin	**4,638,834**	2,598,881

(D) Liability Adequacy Test

The liability adequacy test requires comparison of the unearned premium liability net of deferred insurance costs to the present value of net future cash flows relating to future claims arising under current general insurance contracts.

The risk margin in expected net future cash flows for future claims as a percentage of the undiscounted central estimate is 45% (2009: 50%). This is the risk margin required to give a probability of adequacy of 75% for total insurance liabilities.

The branch's net unearned premium liability exceeded the present value of net future claims as at 31 December 2010 and 2009.

18. CAPITAL MANAGEMENT

(A) Objectives and composition of capital

The branch is not subject to any minimum capital requirements, and accordingly does not have its own capital management plan.

Capital is managed by the Australian head office at a corporate level in accordance with requirements of its prudential regulator, shareholders and rating agencies, without any specific regard to New Zealand capital levels.

19. REMUNERATION OF THE AUDITOR

Audit fees for the company incorporate the New Zealand branch and are paid at Head Office level. Amounts received by the company's auditors are as follows:

	2010	2009
	$	$
PricewaterhouseCoopers – Australian firm		
Assurance services		
Audit or review of financial reports of the entity	**516,376**	867,549
Other services		
Special audits required by regulators	**136,003**	175,774
Total remuneration for audit services	**652,379**	1,043,323
Related practices of PricewaterhouseCoopers – Australian firm		
Other services		
Taxation services	**9,731**	23,507

20. CONTINGENT LIABILITIES

The branch had no contingent liabilities as at 31 December 2010 (31 December 2009: nil)

21. CAPITAL COMMITMENTS

The branch had no capital commitments as at 31 December 2010 (31 December 2009: nil).

22. RELATED PARTY DISCLOSURES

(A) Parent and ultimate parent

The branch forms part of QBE LMI, a company incorporated and domiciled in Australia.

The company's ultimate parent company is QBE Insurance Group Limited ("QBE"), incorporated in Australia.

(B) Related party transactions

(i) Australia Head Office

The Australia Head Office charges management fees in respect of time and costs incurred supporting the branch's activities.

(ii) Other related entities

The company has excess of loss outward reinsurance arrangements with Equator Reinsurances Ltd and QII Singapore branch, members of the QBE Group. The branch pays part of the company's premiums, proportionate to the level of its insurance risks.

Effective 17 August 2009 employment contracts with all employees of the branch ceased and those employees commenced employment with a related party, QII New Zealand branch. QII New Zealand branch charges the branch management fees in respect of this arrangement, for individuals directly supporting the branch's activities.

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

Reference

Revenue and expenses	Note 6(D)
Amounts due from related entities	Note 11
Amounts due to related entities	Note 14

23. EVENTS OCCURRING AFTER REPORTING DATE

There is, at the date of these statements, no matter or circumstance that has arisen since 31 December 2010 that has significantly affected, or may significantly affect:

(i) the branch's operations in future financial years;

(ii) the results of those operations in future financial years; or

(iii) the branch's state of affairs in future financial years.

PRICEWATERHOUSECOOPERS

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Independent Auditors' Report to the Directors of QBE Lenders' Mortgage Insurance Limited New Zealand Branch

Report on the Financial Statements

We have audited the financial statements of QBE Lenders' Mortgage Insurance (New Zealand Branch) on pages 2 to 34, which comprise the Balance Sheet as at 31 December 2010, Statement of Comprehensive Income and Statement of Changes in Head Office account for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Financial Statements

The Company's Directors are responsible for the preparation of these financial statements in accordance with generally accepted accounting practice in New Zealand and that present fairly 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 auditor considers the internal controls relevant to the entity's preparation of financial statements that present fairly 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 entity'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.

Other than in our capacity as auditors we have no relationship with, or interests in, the New Zealand Branch.

PRICEWATERHOUSECOOPERS

Independent Auditors' Report to the Directors of QBE Lenders' Mortgage Insurance Limited New Zealand Branch (continued)

Opinion

In our opinion, the financial statements on pages 2 to 34

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

(ii) present fairly, in all material effects, the financial position of the New Zealand Branch as at 31 December 2010, and its financial performance for the year ended on that date.

Restriction on Distribution or Use

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

PricewaterhouseCoopers

Chartered Accountants — Sydney

I, John W Bennett, am currently a member of Institute of Chartered Accountants in Australia and my membership number is 27653.

PricewaterhouseCoopers was the audit firm appointed to undertake the audit of QBE Lenders' Mortgage Insurance Limited – New Zealand Branch for the year ended 31 December 2010. I was responsible for the execution of the audit and delivery of our firm's auditors' report. The audit work was completed on 17 February 2011 and an unqualified opinion was issued

J W Bennett — Sydney

Partner — 17 February 2011