QBE LENDERS' MORTGAGE INSURANCE LIMITED
New Zealand Branch

ANNUAL REPORT – 31 DECEMBER 2019

CONTENTS

This financial report includes separate 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 (the Company) and is a reporting entity for the purposes of the Financial Reporting Act 2013 and the Financial Markets Conduct Act 2013. Its principal place of business is:

Level 21 QBE Centre
125 Queen Street
Auckland Central 1010
New Zealand

The financial report was authorised for issue by the directors on 14 February 2020. The directors have the power to amend and reissue the financial report.

STATEMENT BY DIRECTORS

For the year ended 31 December 2019

We, being two directors of QBE Lenders' Mortgage Insurance Limited, certify that the Statement of Comprehensive Income, Balance Sheet, Statement of Changes in Balances Due To Head Office, Statement of Cash Flows and notes set out on pages 9 to 38 fairly present the Financial Statements of the New Zealand Branch of the Company for the year ended 31 December 2019.

The Board of Directors of QBE Lenders' Mortgage Insurance Limited authorised these statements for issue on 14 February 2020.

Director

Director

Independent auditor's report

To the Shareholder of QBE Lenders' Mortgage Insurance Limited

The financial statements comprise:

- the balance sheet as at 31 December 2019;
- the statement of comprehensive income for the year then ended;
- the statement of changes in balances due to Head Office for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the financial statements of QBE Lenders' Mortgage Insurance Limited – New Zealand Branch (the Company), present fairly, in all material respects, the financial position of the Company as at 31 December 2019, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs NZ) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

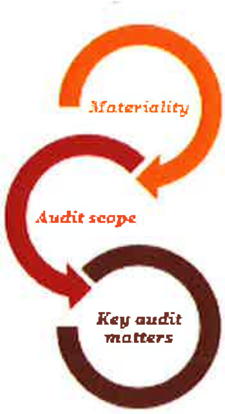
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Company in accordance with Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

Our audit approach

Overview



An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement.

Overall materiality: $15,033, which represents approximately 5% of the Company's profit before tax from continuing operations, averaged over the current and previous two years.

We chose profit before tax averaged over the current and previous two years as the benchmark because, in our view, it is the benchmark against which the performance of the Company is most commonly measured by users, and is a generally accepted benchmark. We used a 5% threshold based on our professional judgement, noting it is within the range of commonly acceptable thresholds.

We have determined that there are two key audit matters:

- Net Earned Premiums (NEP) and valuation of the unearned premium liability
- Valuation of the outstanding claims liability

Materiality

The scope of our audit was influenced by our application of materiality.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the financial statements as a whole as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Audit scope

We designed our audit by assessing the risks of material misstatement in the financial statements and our application of materiality. As in all of our audits, we also addressed the risk of management override of internal controls including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the Company, the accounting processes and controls, and the industry in which the Company operates.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the key audit matter
Net Earned Premiums (NEP) and valuation of the unearned premium liability *Net earned premium: $71,334* *Unearned premium liability: $42,216* The Company sold Lenders Mortgage Insurance products and received payments for all insurance policies upfront, however this premium revenue has been recognised over time. The timing pattern for recognition of premiums and the resulting valuation of the unearned premium liability (the proportion of the premium revenue not yet recognised), has been determined by applying actuarial modelling techniques to develop an earnings curve. In this way, the timing of revenue recognition is dependent on the way in which claims are expected to emerge. Net earned premiums (NEP) and the unearned premium liability were a key audit matter due to the complexity of the actuarial methodology used to model the earnings curve and the significant level of judgment applied in assessing the assumptions adopted, including risk profile of the portfolio and expected housing market growth. The earnings curve and the timing of revenue recognition is dependent on an assessment of future claim emergence. As a result, the complexities discussed in the key audit matter 'Outstanding claims liabilities' were also relevant to our work over net earned premiums and the valuation of the unearned premium liability. Management have concluded that no significant change was required to the earning pattern having completed a detailed review of the earning pattern in the previous year. Other Financial Statement Line Items impacted by this change are: • Deferred insurance costs ($18,997) • Unearned reinsurance commission ($4,294) • Deferred reinsurance premium movement ($58,365) and • Reinsurance commission revenue ($13,190).	Working with the assistance of PwC actuarial experts, we have assessed the appropriateness of the assumptions and methodologies used by comparing them with our expectations based on experience, current trends and benchmarks. This included an assessment of the sensitivity of the adopted earnings curve to key model assumptions and an analysis of key changes from previous periods. To assess the calculation of the NEP along with other impacted balances we have: • Tested the underlying policy in-force reports and data used in the calculation by agreeing a sample of the information back to source systems • Obtained a listing of acquisition costs taken into consideration in the model. Agreed a sample to source records and assessed if sampled costs had been recognised in-line with applicable accounting standards • Recalculated the unearned premium liability using the underlying policy in-force reports and updated earning patterns, including recalculation of the movement recognised in the statement of comprehensive income • Recalculated the deferred insurance costs recognised as at 31 December 2019, primarily the deferred reinsurance premiums • Assessed the overall earning pattern accounting estimate and its application in deriving the unearned premium liability, in light of the requirements of the applicable accounting standard.

Key audit matter	How our audit addressed the key audit matter
Valuation of the outstanding claims liability *Outstanding claims: $111,694* The estimation of outstanding claims involves significant judgement given the size of the liability and the inherent uncertainty in estimating the expected future payments for claims incurred. The two key elements to this are the gross discounted central estimate and risk margin, both considered below. The valuation of the outstanding claims liability was a key audit matter due to the higher level of estimation and judgement required in determining the appropriateness of the assumptions used in valuing the liability. *Gross discounted central estimate* Valuation of the liability involves complex and subjective judgements on a number of areas, including: • Future events, internal and external to the business, for which small changes in assumptions can result in material impacts on the estimate • Estimation of payments for claims incurred but not reported at the reporting date given there is generally less clarity on this information • Estimation of the period over which claims are expected to settle, impacting the estimation of expected future payments. *Risk margins* A risk margin, relating to the inherent uncertainty in the estimation of the present value of expected future payments, is determined by making judgements on the variability of the book of business. Management will consider the Probability of Adequacy in determining the appropriate risk margin. Probability of Adequacy (PoA) is a measure of the estimated overall sufficiency of reserves including a risk margin in light of that variability.	Our audit procedures included evaluating the design effectiveness and implementation of relevant key actuarial controls, including the Appointed Actuary review of the estimate adopted. Historical claims data was a key input to the actuarial estimates. Accordingly, we tested the underlying reports used in the valuation of the outstanding claim liability by agreeing a sample of items back to supporting documentation, including arrears reporting and policy application data. To evaluate the methodologies and assumptions utilised, we with the assistance of PwC actuarial experts developed an understanding of and evaluated the actuarial practices in respect to the gross discounted central estimate and risk margin. In this regard we: • Evaluated whether actuarial methodologies were consistent with those in the industry and in prior years. • Assessed key actuarial assumptions, including claims ratios and relevant economic factors by comparing them with our expectations based on experience, current trends and benchmarks.

Information other than the financial statements and auditor's report

The Directors are responsible for the annual report. Our opinion on the financial statements does not cover the other information included in the annual report and we do not, and will not express any form of assurance conclusion on the other information. At the time of our audit, the Directors have advised that no other information will be included in the annual report.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact.

Responsibilities of the Directors for the financial statements

The Directors are responsible, on behalf of the Company, for the preparation and fair presentation of the financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs NZ and ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board's website at:

https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-2/

This description forms part of our auditor's report.

Who we report to

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

The engagement partner on the audit resulting in this independent auditor's report is Christopher Verhaeghe.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
14 February 2020

Sydney

FINANCIAL REPORT CONTENTS

FINANCIAL STATEMENTS

QBE LENDERS' MORTGAGE INSURANCE LIMITED
New Zealand Branch

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2019

	NOTE	2019 $	2018 $
Gross written premium		-	-
Unearned premium movement	2.5	**129,699**	576,511
Gross earned premium	2.1	**129,699**	576,511
Outward reinsurance premium		-	-
Deferred reinsurance premium movement	2.5	**(58,365)**	(259,430)
Outward reinsurance premium expense		**(58,365)**	(259,430)
Net earned premium (a)		**71,334**	317,081
Gross claims (incurred) releases	2.2	**(17,964)**	174,849
Reinsurance and other recoveries	2.2	**26,577**	12,513
Net claims releases (b)		**8,613**	187,362
Movement in unexpired risk liability (c)	2.5.1	**(95,543)**	-
Reinsurance commission revenue (d)	2.1	**13,190**	58,631
Underwriting and other expenses (e)		**(61,858)**	(137,114)
Underwriting result (a)+(b)+(c)+(d)+(e)		**(64,264)**	425,960
Investment income	2.1	**13,356**	17,137
Insurance (loss) profit		**(50,908)**	443,097
(Loss) profit before income tax		**(50,908)**	443,097
Income tax benefit (expense)	5.1	**14,254**	(124,067)
(Loss) profit after income tax		**(36,654)**	319,030
Other comprehensive income			
Other comprehensive income after income tax		**-**	-
Total comprehensive (loss) income after income tax		**(36,654)**	319,030
(Loss) profit after income tax attributable to:			
Head Office Account		**(36,654)**	319,030
		(36,654)	319,030
Total comprehensive (loss) income after income tax attributable to:			
Head Office Account		**(36,654)**	319,030
		(36,654)	319,030

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

BALANCE SHEET

As at 31 December 2019

	NOTE	2019 $	2018 $
Assets			
Cash and cash equivalents	4.1	**1,102,995**	1,205,203
Trade and other receivables	2.6	**11,339**	9,392
Current tax receivable		**125,055**	26,364
Reinsurance and other recoveries on outstanding claims	2.3	**44,452**	61,148
Deferred insurance costs	2.5	**18,997**	100,351
Deferred tax assets	5.2	**26,752**	-
Total assets		**1,329,590**	1,402,458
Liabilities			
Trade and other payables	2.7	**116,782**	58,716
Deferred tax liabilities	5.2	**-**	6,437
Outstanding claims	2.3	**111,694**	152,191
Unearned premium	2.5	**42,216**	171,915
Unexpired risk liability	2.5.1	**95,543**	-
Unearned reinsurance commission	2.5	**4,294**	17,484
Total liabilities		**370,529**	406,743
Net assets		**959,061**	995,715
Due to Head Office – Australia		**959,061**	995,715

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

STATEMENT OF CHANGES IN BALANCES DUE TO HEAD OFFICE

For the year ended 31 December 2019

2019	**HEAD OFFICE ACCOUNT $**
At 1 January	**995,715**
Loss after income tax	**(36,654)**
Total comprehensive loss	**(36,654)**
Net funding movements	-
At 31 December	**959,061**

2018	**HEAD OFFICE ACCOUNT $**
At 1 January	676,685
Profit after income tax	319,030
Total comprehensive income	319,030
Net funding movements	-
At 31 December	995,715

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

QBE LENDERS' MORTGAGE INSURANCE LIMITED
New Zealand Branch

STATEMENT OF CASH FLOWS

For the year ended 31 December 2019

	NOTE	2019 $	2018 $
Operating activities			
Reinsurance and other recoveries received		**43,273**	83,658
Claims paid		**(58,461)**	-
Other underwriting costs received (paid)		**17,250**	(79,065)
Interest and dividends received		**13,356**	17,137
Income taxes paid		**(117,626)**	(112,280)
Net cash flows from operating activities	6.3	**(102,208)**	(90,550)
Investing activities			
Net cash flows from investing activities		**-**	-
Financing activities			
Net cash flows from financing activities		**-**	-
Net movement in cash and cash equivalents		**(102,208)**	(90,550)
Cash and cash equivalents at the beginning of the year		**1,205,203**	1,295,753
Cash and cash equivalents at the end of the year	4.1	**1,102,995**	1,205,203

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

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2019

1. OVERVIEW

1.1 About the Company

About QBE Lenders' Mortgage Insurance Limited, New Zealand Branch

QBE Lenders' Mortgage Insurance Limited (the Company) is a residential lenders' mortgage insurance company incorporated in Australia and operating in New Zealand as a Branch (the Branch).

About insurance

In simple terms, insurance and reinsurance companies help their customers (consumers, businesses and other insurance companies) to manage risk. More broadly put, insurance companies create value by pooling and redistributing risk. This is done by collecting premium from those that it insures (that is policyholders) and then paying the claims of those that call upon their insurance protection. The Company may also choose to reduce some of its own accumulated risk through the use of outward reinsurance, which is insurance for insurance companies. As not all policyholders will actually experience a claims event, the effective pooling and redistribution of risk lowers the total cost of risk management, thereby making insurance protection more cost effective for all.

The operating model of insurance companies relies on profits being generated:

- by appropriately pricing risk and charging adequate premium to cover the expected payouts that will be incurred over the life of the insurance policy (both claims and operating expenses); and
- by earning a return on the collected premium and funds withheld to pay future claims through the adoption of an appropriate investment strategy.

Insurance therefore serves a critical function of providing customers with the confidence to achieve their business and personal goals through cost effective risk management. This is achieved within a highly regulated environment, designed to ensure that insurance companies maintain adequate capital to protect the interests of policyholders.

1.2 About this report

This financial report includes the financial statements of QBE Lenders' Mortgage Insurance Limited, New Zealand Branch as an individual entity.

The financial report includes the four primary statements, namely the statement of comprehensive income (which comprises profit or loss and other comprehensive income), balance sheet, statement of changes in balances due to Head Office and statement of cash flows, as well as associated notes. Refer to Note 1.2.1 for more details.

Disclosures have been grouped into the following categories in order to assist users in their understanding of our financial statements:

1. **Overview** contains information that impacts the financial report as a whole.
2. **Underwriting activities** brings together all results and balance sheet disclosures relevant to the Branch's insurance activities.
3. **Risk management** provides commentary on the Branch's exposure to various financial and capital risks, explaining the potential impact on the results and balance sheet and how the Branch manages these risks.
4. **Capital structure** provides information about the Branch's cash and the Company's capital.
5. **Tax** includes disclosures in relation to the Branch's tax balances.
6. **Other** includes other required disclosures.

Where applicable within each note, disclosures are further analysed as follows:

- **Overview** provides some context to assist users in understanding the disclosures.
- **Disclosures** (both numbers and commentary) provides required analysis of balances.
- **How we account for the numbers** summarises the accounting policies relevant to an understanding of the numbers.
- **Critical accounting judgements and estimates** explains the key estimates and judgements applied by management in determining the numbers.

The notes include information which the directors believe is required to understand the financial statements and is material and relevant to the operations, balance sheet and results of the Branch. Information is considered material and relevant if:

- the amount in question is significant because of its size or nature;
- it is important to assist in understanding the results of the Branch;
- it helps to explain the impact of significant changes in the Branch's business; or
- it relates to an aspect of the Branch's operations that is important to its future performance.

1.2.1 Basis of preparation

This financial report:

- has been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). It complies with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable financial reporting standards, as appropriate for for-profit entities. The Branch is a for-profit entity registered under the *Companies Act 1993*. The financial statements are prepared in accordance with the requirements of Part 7 of the *Financial Markets Conduct Act 2013*, *Financial Reporting Act 2013* and the *Companies Act 1993*;
- the sole shareholder of the Company has exercised its right under section 211(3) of the *Companies Act 1993* and determined that these financial statements need not comply with paragraphs (a), and (e) to (j) of section 211(1) of the Act;
- has been prepared on a historical cost basis as modified by certain exceptions, the most significant of which is the measurement of the net outstanding claims liability at present value;
- with effect from September 2013, the Branch ceased to write new insurance policies. 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's financial statements;
- is presented in New Zealand dollars; and
- is presented with values rounded to the nearest dollar.

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

New and amended Accounting Standards and Interpretations issued by the New Zealand Accounting Standards Board (NZASB) that are now effective are detailed in note 6.1.

The Branch has not adopted any Accounting Standards and Interpretations that have been issued or amended but are not yet effective.

The Branch's ultimate parent company, QBE Insurance Group Limited (QBE Group) (incorporated in Australia) produces consolidated financial statements in accordance with Australia Accounting Standard Board (AASB) and IFRS for public use, which can be obtained at www.qbe.com or Level 27, 8-12 Chifley Square, Sydney, NSW 2000, Australia.

1.2.2 Critical accounting judgements and estimates

The preparation of the Branch's financial statements requires management to make judgements and estimates that affect reported amounts.

The QBE Group has developed a centralised risk management and policy framework, designed to ensure consistency of approach across a number of operational activities. The Company adopts these, subject to the specific requirements of local markets, legislation and regulation. Such operational activities include underwriting, claims management, actuarial assessment of the outstanding claims liability and investment management.

Sensitivity analyses in respect of critical accounting estimates and judgements are presented in order to provide information and analysis which is meaningful, relevant, reliable and comparable year on year.

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

- net outstanding claims liability (note 2.3);
- unearned premium and deferred insurance costs (note 2.5);
- liability adequacy test (note 2.5.1); and
- deferred income tax (note 5.2).

1.2.3 Foreign currency

Translation of foreign currency transactions and balances

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

Exchange rates

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

	2019		2018	
	PROFIT OR LOSS	**BALANCE SHEET**	**PROFIT OR LOSS**	**BALANCE SHEET**
A$/NZ$	**1.055**	**1.042**	1.080	1.049

2. UNDERWRITING ACTIVITIES

Overview

This section provides analysis and commentary on the Branch's underwriting activities. Underwriting, in simple terms, is the agreement by the insurer to assume insurance risk in return for a premium paid by the insured. The underwriter assesses the quality of the risk and prices it accordingly.

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2019

2.1 Revenue

Overview

Revenue mainly comprises premiums charged for providing insurance coverage. Premiums are classified as direct, being those paid by the policyholder to the insurer.

Other sources of revenue principally comprise amounts recovered from reinsurers under the terms of reinsurance contracts and commission income from reinsurers.

	NOTE	2019 $	2018 $
Gross earned premium			
Direct		**129,699**	576,511
		129,699	576,511
Other revenue			
Reinsurance and other recoveries revenue	2.2	**26,577**	12,513
Reinsurance commission revenue		**13,190**	58,631
		39,767	71,144
Total revenue		**169,466**	647,655

How we account for the numbers

Premium revenue
Premium written comprises amounts charged to policyholders, excluding taxes collected on behalf of third parties. With effect from 2013, the Branch ceased to write new insurance policies.

Premium revenue is recognised in profit or loss from the date of attachment of risk over the period of the insurance contract in accordance with the pattern of the expected incidence of risk, adjusted for policy terminations.

Reinsurance and other recoveries
Reinsurance and other recoveries on paid claims, reported claims not yet paid, and claims incurred but not reported (IBNR) are recognised as revenue. Recoveries are measured as the present value of the expected future receipts.

Reinsurance commission revenue
Reinsurance commission revenue comprises exchange commissions that are a fixed percentage of reinsurance premiums payable. Exchange commissions are recognised in profit or loss on the same basis as reinsurance written premiums, reflecting the pattern of the expected incidence of risk over the period of indemnity, adjusted for policy terminations.

2.2 Net claims expense

Overview

The largest expense for an insurance company is net claims expense, which is the difference between the net outstanding claims liability (as described in note 2.3 below) at the beginning and the end of the financial year plus any claims payments made, net of reinsurance and other recoveries received during the financial year.

	NOTE	2019 $	2018 $
Gross claims releases			
Direct		**17,964**	(174,849)
Reinsurance and other recoveries revenue			
Direct	2.1	**(26,577)**	(12,513)
Net claims recoveries revenue		**(8,613)**	(187,362)
Analysed as follows:			
Movement in net discounted central estimate	2.4.1	**(3,627)**	(165,638)
Movement in risk margin	2.3	**(4,986)**	(21,724)
Net claims recoveries revenue		**(8,613)**	(187,362)

2.3 Net outstanding claims liability

Overview

The net outstanding claims liability comprises the elements described below.

- The gross central estimate (note 2.3.1). This is the provision for expected future claims payments and includes claims reported but not yet paid, claims incurred but which have not yet been reported (IBNR) and estimated claims handling costs.
- Less reinsurance and other recoveries (note 2.3.2). Insurance companies may elect to purchase reinsurance to manage their exposure to any one claim or series of claims. When an insurance company incurs a claim as a result of an insured loss, it may be able to recover some of that claim from the reinsurers or other parties associated with the claim.
- Less an amount to reflect the discount to present value using risk-free rates of return. The net central estimate is discounted to present value recognising that the claim and/or recovery may not be settled for some time. The weighted average risk-free rate used to discount the outstanding claims liability is summarised in note 2.3.4.
- Plus a risk margin (note 2.3.3). A risk margin is added to reflect the inherent uncertainty in the net discounted central estimate of outstanding claims.

	NOTE	2019 $	2018 $
Gross discounted central estimate	2.3.1	**97,608**	133,119
Risk margin	2.3.3	**14,086**	19,072
Gross outstanding claims liability		**111,694**	152,191
Reinsurance and other recoveries on outstanding claims	2.3.2	**(44,452)**	(61,148)
Net outstanding claims liability		**67,242**	91,043

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2019

The table below analyses the movement in the outstanding claims liability, showing separately the movement in gross claims liability and the impact of reinsurance:

	2019			2018		
	GROSS $	REINSURANCE $	NET $	GROSS $	REINSURANCE $	NET $
At 1 January	**152,191**	**(61,148)**	**91,043**	327,040	(132,293)	194,747
Current accident year development in net discounted outstanding claims (note 2.4.2)	**41,923**	**(19,092)**	**22,831**	104,670	(48,080)	56,590
Prior accident year development in net discounted outstanding claims (note 2.4.2)	**(18,973)**	**(7,485)**	**(26,458)**	(257,795)	35,567	(222,228)
Movement in risk margin (note 2.2)	**(4,986)**	**-**	**(4,986)**	(21,724)	-	(21,724)
Released claims recognised in profit or loss	**17,964**	**(26,577)**	**(8,613)**	(174,849)	(12,513)	(187,362)
Claims payments	**(58,461)**	**43,273**	**(15,188)**	-	83,658	83,658
At 31 December	**111,694**	**(44,452)**	**67,242**	152,191	(61,148)	91,043

2.3.1 Gross discounted central estimate

	NOTE	2019 $	2018 $
Gross undiscounted central estimate excluding claims settlement costs		**96,460**	133,379
Claims settlement costs		**2,311**	3,129
Gross undiscounted central estimate		**98,771**	136,508
Discount to present value		**(1,163)**	(3,389)
Gross discounted central estimate	2.3	**97,608**	133,119
Payable within 12 months		**50,738**	64,023
Payable in greater than 12 months		**46,870**	69,096
Gross discounted central estimate	2.3	**97,608**	133,119

How we account for the numbers

The gross discounted central estimate is the present value of the expected future payments for claims incurred and includes reported but unpaid claims, IBNR and claims settlement costs. The gross discounted central estimate is determined by the Appointed Actuary, supported by a team of actuaries. The valuation process includes extensive consultation with claims and underwriting staff as well as senior management. The net discounted central estimate of outstanding claims is subject to a comprehensive independent review at least annually. The risk management procedures related to the actuarial function are explained further in note 3.2.

Critical accounting judgements and estimates

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 due to the time that elapses before a definitive determination of the ultimate claims cost can be made;
- changes in the legal environment, including the interpretation of liability laws and the quantum of damages; and
- changing social, political and economic trends, for example, house price inflation, unemployment and interest rates.

The estimation of IBNR is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims that have been reported to the Company but not yet paid, for which some 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 incurred and the final settlement amount, as a result of additional financing and settlement costs incurred by the lender and changes in property valuations.

Central estimates are determined using a variety of estimation techniques, generally based on an analysis of historical experience which assumes an underlying pattern of claims development and payment. The final selected central estimate is based on a judgemental 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.

The gross central estimate is discounted to present value using the appropriate risk-free rate.

Central estimates are calculated gross of any reinsurance and other recoveries. A separate estimate is made of the amounts recoverable based on the gross central estimate (note 2.3.2).

2.3.2 Reinsurance and other recoveries on outstanding claims

	NOTE	2019 $	2018 $
Reinsurance and other recoveries on outstanding claims - undiscounted		**44,994**	62,742
Discount to present value		**(542)**	(1,594)
Reinsurance and other recoveries on outstanding claims	2.3	**44,452**	61,148
Receivable within 12 months		**23,107**	29,409
Receivable in greater than 12 months		**21,345**	31,739
Reinsurance and other recoveries on outstanding claims	2.3	**44,452**	61,148

How we account for the numbers

The recoverability of amounts due from reinsurers and others is assessed at each balance date to ensure that the balances properly reflect the amounts that are ultimately expected to be received, taking into account counterparty credit risk and the contractual terms of reinsurance contracts. Counterparty credit risk in relation to reinsurance assets is considered in note 3.3. Recoveries are discounted to present value using the appropriate risk-free rate.

2.3.3 Risk Margin

Overview

A risk margin is determined by the Company's Board to reflect the inherent uncertainty in the net discounted central estimate.

The risk margin and the net discounted central estimate are key inputs in the determination of the probability of adequacy, which is a statistical measure of the relative adequacy of the outstanding claims liability to ultimately be able to pay claims. For example, a 90% probability of adequacy indicates that the outstanding claims liability is expected to be adequate 9 years in 10.

	2019 $	2018 $
Risk margin ($)	**14,086**	19,072
Risk margin as a percentage of the net discounted central estimate (%)	**26.5%**	26.5%
Probability of adequacy (%)	**75.0%**	75.0%

Both the Reserve Bank of New Zealand (RBNZ) and the Australian Prudential Regulation Authority (APRA) require a probability of adequacy of 75% for the determination of minimum capital.

How we account for the numbers

NZ IFRS 4 *Insurance Contracts* requires an entity to adopt an appropriate risk margin. The resulting probability of adequacy is not of itself an accounting policy as defined by NZ IAS 8 *Accounting Policies*, *Changes in Accounting Estimates and Errors*. The appropriate level of risk margin is not determined by reference to a fixed probability of adequacy.

Critical accounting judgements and estimates

The determination of the appropriate level of risk margin takes into account the level of uncertainty in the central estimate due to estimation error, data quality, variability of key discount assumptions and possible economic and legislative changes.

The key drivers of uncertainty unique to the Branch's insurance liability are as follows:

- Reliance on consistent arrears management practices and this may change in the future;
- Uncertainties surrounding the global economy, with potential flow-on impacts to the New Zealand economy through future property prices, unemployment and interest rates; and
- Concentration of property losses in a particular region.

2.3.4 Discount rate used to determine the outstanding claims liability

Overview

Claims typically may not settle for some time. As such, the liability is discounted to reflect the time value of money. The table below summarises the weighted average discount rate used to discount the outstanding claims liability.

	2019 YEARS	2018 YEARS
Discount rate	**0.9**	1.9

How we account for the numbers

NZ IFRS 4 requires that the net central estimate is discounted to reflect the time value of money using risk-free rates that are based on current observable, objective rates that relate to the nature, structure and terms of the future obligations.

2.3.5 Weighted average term to settlement

Overview

The weighted average term to settlement refers to the period from the balance date to the expected date of claims settlement. All other factors being equal, a longer weighted average term to settlement generally results in a larger impact on the central estimate from discounting. The weighted average term to settlement of the Branch's outstanding claims liability is summarised below.

	2019 YEARS	2018 YEARS
Weighted average term to settlement	**1.3**	1.3

2.3.6 Net discounted central estimate maturity profile

Overview

The maturity profile is the Branch's expectation of the period over which the net central estimate will be settled. The Branch uses this information to ensure that it has adequate liquidity to pay claims as they are due to be settled and to inform the Branch's investment strategy. The expected maturity profile of the Branch's net discounted central estimate 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
2019	**$**	**27,631**	**15,685**	**5,737**	**2,013**	**939**	**1,151**	**53,156**
2018	$	34,614	22,765	8,836	2,947	1,263	1,546	71,971

2.3.7 Impact of changes in key variables on the net outstanding claims liability

Overview

The impact of changes in key variables used in the calculation of the outstanding claims liability is summarised in the table below. Each change has been calculated in isolation from the other changes and shows the after tax impact on profit assuming that there is no change to any of the other even if, in practice, this may be considered unlikely to occur.

The sensitivities below assume that all changes directly impact profit after income tax. In practice, however, if the central estimate was to increase, at least part of the increase may result in an offsetting change in the level of risk margins rather than in a change to profit after income tax, depending on the nature of the change in the central estimate. Likewise, if the coefficient of variation were to increase, it is possible that the probability of adequacy would reduce from its current level rather than result in a change to profit after income tax.

		PROFIT (LOSS)[1]	
	SENSITIVITY	2019	2018
	%	$	$
Severity	+20	**(10,432)**	(13,287)
	-20	**9,486**	13,287
Claim rates	+20	**(10,400)**	(13,274)
	-20	**9,455**	13,259
Discount rate	+5	**473**	82
	-5	**(473)**	(83)
Coefficient of variation	+20	**(19,276)**	(2,746)
	-20	**(13,783)**	2,746

[1] Net of tax at the prima facie rate of 28%.

2.4 Claims development - net undiscounted central estimate

Overview

The claims development table demonstrates the extent to which the original estimated ultimate claims payments in any one accident year (item (a) in the table below) has subsequently developed favourably (that is, claims cost estimates have reduced) or unfavourably (i.e. further claims expense has been recognised in subsequent years). This table therefore illustrates the variability and inherent uncertainty in estimating the central estimate each year. The ultimate claims cost for any particular accident year is not known until all claims payments have been made, which could be some time into the future. The estimated ultimate claims payments at the end of each subsequent accident year demonstrates how the original estimate has been revised over time (b).

Cumulative actual net claims payments (d) are deducted from the expected ultimate claims payments in each accident year (c) at the current balance date, resulting in the net undiscounted central estimate (e), which is reconciled to the discounted central estimate (f).

The accident year movement (g) reflects the ultimate undiscounted net claims estimate at the end of the current financial year (c) less the equivalent at the end of the previous financial year (b). This is further summarised in note 2.4.1.

The claims development table is presented net of reinsurance. With reinsurance arrangements and with the Branch's risk tolerance managed on a net basis, it is considered neither meaningful nor practicable to provide this information other than on a net accident year basis.

	2015 & PRIOR YEARS $	**2016** $	**2017** $	**2018** $	**2019** $	**TOTAL** $
Net ultimate claims payments:						
(a) Original estimate of net ultimate claims payments		244,687	119,902	55,540	22,105	
(b) One year later		103,859	30,914	29,361	-	
Two years later		58,841	15,818	-	-	
Three years later		58,841	-	-	-	
(c) Current estimate of net ultimate claims payments		58,841	15,818	29,361	22,105	126,125
(d) Cumulative net payments to date		(58,841)	(15,818)	-	-	(74,659)
(e) Net undiscounted central estimate at 31 Dec 2019	-	-	-	29,361	22,105	51,466
Discount to present value						(621)
Claims settlement costs						2,311
Risk margin						14,086
(f) Net outstanding claims liability at 31 Dec 2019 (note 2.3)						67,242
(g) Movement in accident year net undiscounted central estimate (note 2.4.1)	15,188	-	(15,096)	(26,179)	22,105	(3,982)

Uncertainty surrounding claims development is materially resolved within four years.

The development of claims from prior accident years was better than expected at 31 December 2019, leading to an overall release of the central estimate for prior years of $26,087. The release is mainly due to favourable overall claim experiences.

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2019

2.4.1 Reconciliation of claims development table to profit or loss

Overview

The table below reconciles the net increase or decrease in estimated ultimate claims payments in the current financial year from the claims development table (item (g) in note 2.4) to the analysis of current and prior accident year central estimate development recognised in profit or loss (note 2.4.2).

	2019			2018		
	CURRENT ACCIDENT YEAR $	PRIOR ACCIDENT YEARS $	TOTAL $	CURRENT ACCIDENT YEAR $	PRIOR ACCIDENT YEARS $	TOTAL $
Net undiscounted central estimate movement (note 2.4)	**22,105**	**(26,087)**	**(3,982)**	55,540	(219,902)	(164,362)
Movement in claims settlement costs	**1,004**	**(1,823)**	**(819)**	2,525	(6,090)	(3,565)
Movement in discount	**(278)**	**1,452**	**1,174**	(1,475)	3,764	2,289
Movement in net discounted central estimate (note 2.4.2)	**22,831**	**(26,458)**	**(3,627)**	56,590	(222,228)	(165,638)

2.4.2 Net central estimate development

Overview

The table further analyses the current and prior accident year movement in the net discounted central estimate separately identifying the gross and reinsurance components. Prior accident year claims are those claims that occurred in a previous year but for which a reassessment of the claims cost has impacted the result in the current period.

	2019			2018		
	CURRENT ACCIDENT YEAR $	PRIOR ACCIDENT YEARS $	TOTAL $	CURRENT ACCIDENT YEAR $	PRIOR ACCIDENT YEARS $	TOTAL $
Gross central estimate development						
Undiscounted	**42,434**	**(21,710)**	**20,724**	107,399	(264,888)	(157,489)
Discount	**(511)**	**2,737**	**2,226**	(2,729)	7,093	4,364
	41,923	**(18,973)**	**22,950**	104,670	(257,795)	(153,125)
Reinsurance and other recoveries						
Undiscounted	**(19,325)**	**(6,200)**	**(25,525)**	(49,334)	38,896	(10,438)
Discount	**233**	**(1,285)**	**(1,052)**	1,254	(3,329)	(2,075)
	(19,092)	**(7,485)**	**(26,577)**	(48,080)	35,567	(12,513)
Net central estimate development						
Undiscounted	**23,109**	**(27,910)**	**(4,801)**	58,065	(225,992)	(167,927)
Discount	**(278)**	**1,452**	**1,174**	(1,475)	3,764	2,289
Net discounted central estimate development (note 2.4.1)	**22,831**	**(26,458)**	**(3,627)**	56,590	(222,228)	(165,638)

2.5 Unearned premium and deferred insurance costs

Overview

Unearned premium

Gross written premium is earned in profit or loss in accordance with the expected pattern of incidence of risk, adjusted for policy terminations. The unearned premium liability is that portion of gross written premium that the Branch has not yet earned as it represents insurance coverage to be provided by the Branch after the balance date.

Deferred insurance costs

Premium ceded to reinsurers by the Branch in exchange for reinsurance protection is expensed in profit or loss in accordance with the reinsurance contract's expected pattern of incidence of risk, adjusted, where appropriate, for terminations of reinsured policies. The deferred reinsurance premium asset is that portion of the reinsurance premium that the Branch has not yet expensed in profit or loss as it represents reinsurance coverage to be received by the Branch after the balance date.

Acquisition costs are the costs associated with obtaining and recording insurance contracts. Acquisition costs are capitalised and amortised on the same basis as the related premium. At the balance date, deferred acquisition costs represent the capitalised costs incurred to acquire the related unearned premium and are carried forward to a subsequent accounting period in recognition of their future benefit.

Summary of unearned premium and deferred insurance costs balances

	2019	**2018**
	$	**$**
Unearned premium (a)	**42,216**	171,915
To be earned within 12 months	**38,083**	127,089
To be earned in greater than 12 months	**4,133**	44,826
Unearned premium	**42,216**	171,915
Unearned reinsurance commission (b)	**4,294**	17,484
To be earned within 12 months	**3,874**	12,925
To be earned in greater than 12 months	**420**	4,559
Unearned reinsurance commission	**4,294**	17,484
Deferred reinsurance premium	**18,997**	77,362
Deferred acquisition costs	**-**	22,989
Deferred insurance costs (c)	**18,997**	100,351
To be expensed within 12 months	**17,137**	74,185
To be expensed in greater than 12 months	**1,860**	26,166
Deferred insurance costs	**18,997**	100,351
Net premium liabilities (a)+(b)-(c)	**27,513**	89,048

Unearned premium movements

	2019	**2018**
	$	**$**
At 1 January	**171,915**	748,426
Earning of premium written in previous financial years	**(129,699)**	(576,511)
At 31 December	**42,216**	171,915

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For the year ended 31 December 2019

Unearned reinsurance commission income movements

	2019 $	2018 $
At 1 January	**17,484**	76,115
Earning of commission written in previous financial years	**(13,190)**	(58,631)
At 31 December	**4,294**	17,484

Deferred insurance costs movements

	DEFERRED REINSURANCE PREMIUM		DEFERRED ACQUISITION COSTS	
	2019 $	2018 $	2019 $	2018 $
At 1 January	**77,362**	336,792	**22,989**	89,353
Amortisation of costs deferred in previous financial years	**(58,365)**	(259,430)	**(16,532)**	(66,364)
Impairment write-down from deficiency in liability adequacy test (note 2.5.1)	**-**	-	**(6,457)**	-
At 31 December	**18,997**	77,362	**-**	22,989

How we account for the numbers

Unearned Premium

Unearned premium on insurance contracts at balance date is calculated by applying the premium earning pattern to premium written on active policies. There was no change to the earning pattern in 2019. The review of this pattern in the previous year increased the unearned premium liability at 31 December 2018 by $145,194 compared to the balance if the previous earning pattern had been applied.

Unearned reinsurance commission income

Unearned reinsurance commission income is calculated by applying the premium earning pattern, adjusted where necessary for varying indemnity periods, to reinsurance commission received or receivable on active reinsurance polices. There was no change to the pattern in 2019. The review of this pattern in the previous year increased the unearned reinsurance commission liability at 31 December 2018 by $14,766 compared to the balance if the previous earning pattern had been applied.

Deferred insurance costs

Deferred reinsurance premium is calculated by applying the premium earning pattern, adjusted where necessary for varying indemnity periods, to reinsurance premiums paid or payable on active reinsurance policies. There was no change to the pattern in 2019. The review of the earning pattern in the previous year increased the deferred reinsurance premium asset at 31 December 2018 by $65,337 compared to the balance if the previous earning pattern had been applied.

Deferred acquisition costs are calculated by applying the premium earning pattern to acquisition costs incurred on acquiring and recording insurance policies that are still active. The carrying value of deferred acquisition costs is subject to impairment testing in the form of the liability adequacy test (note 2.5.1). There was no change to the earning pattern in 2019. The review of the earning pattern in the previous year increased the deferred acquisition cost asset at 31 December 2018 by $17,854 compared to the balance if the previous earning pattern had been applied.

Critical accounting judgements and estimates

An actuarial analysis of the expected pattern of the incidence of risk over the policy coverage period is used to derive a recognition (earning) pattern for each underwriting year. The pattern is reviewed annually, and requires estimating both the total amount of claims expense expected under the contract and when those claims are expected to arise. These estimations involve the use of significant judgement and are reassessed at the end of each reporting period.

2.5.1 Liability adequacy test

Overview

At each balance date, the Branch is required to assess net premium liabilities (being unearned premium less deferred insurance costs) to determine whether the amount provided is sufficient to pay future claims.

If the present value of expected future claims exceeds the net premium liabilities, the net premium liability is deemed deficient. This deficiency is immediately recognised in profit or loss. In recognising the deficiency, an insurer must first write down any related intangible assets and then deferred acquisition costs before recognising an unexpired risk liability.

Expected present value of future cash flows for future claims including risk margin

	2019 $	2018 $
Undiscounted net central estimate	**92,235**	30,829
Discount to present value	**(4,322)**	(5,081)
	87,913	25,748
Risk margin at the 75th percentile of insurance liabilities	**35,143**	10,299
Expected present value of future cash flows for future claims including risk margin	**123,056**	36,047

The application of the liability adequacy test in respect of the net unearned premium liabilities identified a deficit of $102,000 as at 31 December 2019 (2018: nil). The deficit was recognised as a write-down of deferred acquisition costs of $6,457 and the recognition of an unexpired risk liability of $95,543.

How we account for the numbers

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 claims cash flows, plus an additional risk margin to reflect the inherent uncertainty of the central estimate. The assessment is carried out at the portfolio level, being a portfolio of contracts subject to broadly similar risks and which are managed together as a single portfolio.

Critical accounting judgements and estimates

NZ IFRS 4 requires that this test be carried out at the level of a "portfolio of contracts that are subject to broadly similar risks and are managed together in a single portfolio". As NZ IFRS 4 does not explicitly define "broadly similar risks" or "managed together as a single portfolio", and the Branch is a monoline insurer, the Branch has interpreted these terms to represent the entire portfolio.

The Branch has adopted a risk margin of 40.0% (2018: 40.0%) for the purpose of the liability adequacy test to produce a 75% probability of adequacy in respect of total insurance liabilities. The 75% basis is a recognised industry benchmark in New Zealand, as required by RBNZ, and in Australia, being the minimum probability of adequacy required for Australian licensed insurers by APRA.

2.6 Trade and other receivables

Overview

Trade and other receivables comprise amounts owed to the Branch by Head Office. Balances are repayable on demand and interest free.

	2019 $	2018 $
Trade receivables		
Amounts due from Head Office	**11,339**	9,392
Trade and other receivables	**11,339**	9,392
Receivable within 12 months	**11,339**	9,392
Trade and other receivables	**11,339**	9,392

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

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivables. No receivables are pledged by the Branch as collateral for liabilities or contingent liabilities. Information on the ageing and credit rating of these balances is included in note 3.3.

How we account for the numbers

Receivables are initially recognised at fair value and are subsequently measured at amortised cost less an allowance for expected credit losses (ECL). Any increase or decrease in the loss allowance is recognised in profit or loss within operating expenses.

Critical accounting judgements and estimates

The allowance for ECL is based on the difference between the cash flows due in accordance with the contract and the cash flows that the Company expects to receive. The allowance for ECL reflects judgements and assumptions that take into account prior credit risk and loss history, current and expected future market conditions and individual debtor circumstances. Any shortfall is discounted at an approximation to the asset's original effective interest rate.

The allowance is based on the portion of lifetime ECL that result from possible default events within 12 months from reporting date, unless there has been a significant increase in credit risk since initial recognition, in which case the allowance is based on the lifetime ECL.

The credit risk in relation to amounts due from Head Office is assessed with regard to the credit standing of the Company and policies and practices surrounding the periodic settlements of balances. The Branch has determined that the credit risk has not increased significantly since initial recognition.

The Branch does not foresee losses arising on this receivable from possible default events within 12 months from the reporting date and considers that no allowance for impairment is required at 31 December 2019 (2018: nil).

2.7 Trade and other payables

Overview

Trade and other payables are principally amounts owed to related entities. Amounts due are repayable on demand and interest free.

	2019 $	2018 $
Amounts due to related entities	**116,596**	56,975
Other payables	**186**	1,741
Trade and other payables	**116,782**	58,716
Payable within 12 months	**116,782**	58,716
Trade and other payables	**116,782**	58,716

How we account for the numbers

Amounts due to related entities are initially recognised at fair value and are subsequently measured at amortised cost

3. RISK MANAGEMENT

Overview

The Company is in the business of managing risk, and its ability to satisfy customers' risk management needs is central to what we do. The Company aims to generate wealth and maximise returns for its shareholders by pursuing opportunities that involve risk. Our people are responsible for ensuring that the Company's risks, including those of the Branch, are managed and controlled on a day-to-day basis. The Company aims to use its ability to properly manage risk to provide more certainty and improved outcomes for all stakeholders.

The Australia Pacific division of QBE Group (QBE AusPac), of which the Company is a part, applies a consistent and integrated approach to enterprise risk management (ERM). QBE AusPac's risk management framework sets out the approach to managing key risks and meeting strategic objectives whilst taking into account the creation of value for our shareholders. QBE AusPac's risk management framework is articulated in the Risk Management Strategy (RMS) and Reinsurance Management Strategy (REMS), both of which are approved annually by the Company Board and lodged with APRA.

The framework consists of complementary elements that are embedded throughout the business management cycle and culture of the organisation. Key aspects include risk appetite, governance, reporting, risk assessments, modelling and stress testing, management, and monitoring and risk culture.

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

QBE Group's strategy for managing risk is to:

- achieve competitive advantage by better understanding the risk environments in which the Branch operates;
- give confidence to the business to make objective, risk-based decisions to optimise returns; and
- avoid unwelcome surprises to the achievement of business objectives by reducing uncertainty and volatility through the identification and management of risks.

The framework is supported by a suite of policies that detail QBE AusPac's approach to the key risk categories used by companies within the division to classify risk:

- Strategic risk (note 3.1)
- Insurance risk (note 3.2)
- Credit risk (note 3.3)
- Market risk (refer below)
- Liquidity risk (note 3.4)
- Operational risk (note 3.5)
- Compliance risk (note 3.6)
- Group risk (note 3.7)

The Company has adopted the risk management approach and framework set by QBE Group and QBE AusPac, and applied them to the activities of the Branch, where applicable.

Due to the nature of its activities, the Branch is not exposed to market risk, being the risk of variability in the value of investments due to investment market movement (including equity prices, interest rates and credit spreads); and foreign exchange rate movements.

3.1 Strategic risk

Overview

Strategic risk is the current and prospective impact on earnings and/or capital as a result of strategic business decisions or responsiveness to external change. QBE AusPac classifies strategic risk into five sub-categories, that have been adopted by the Company, as follows:

- business, product, market and distribution approach;
- capital structure, organisational structure, strategic asset planning and management;
- acquisition/disposal decision and negotiation;
- tax planning and decisioning; and
- external environment, including disruption from competitors; economic, social and governance risks; reputational impact; and geo-political and regulatory uncertainty.

The Company's approach to managing strategic risk is underpinned by the QBE AusPac's strategic risk appetite statement that has been adopted by the Company Board and is summarised below.

Business, product and market distribution

- **Business:** The Company is a residential lenders' mortgage insurance Company underwriting business in Australia and New Zealand. The Company Board meets at least quarterly to review performance against business plans. Actual results are monitored and analysed regularly at various levels in the Company to identify adverse trends so that remedial action can be taken at an early stage. One of the key tools used to ensure achievement of business plans is to identify the 'manage to' likely scenarios impacting the plan year, based on events that have occurred or risks identified since plans were set. The Company assesses how these scenarios would impact return on equity (ROE) forecasts and develop and implement bridging actions to drive plan achievability.
- **Products:** The Company reviews the structuring of its insurance products on an ongoing basis in line with developments in market expectations, legislation and claims trends.
- **Market distribution approach:** The Company makes use of banks and other financial institutions to market its insurance products.

The Branch ceased to write new insurance policies in 2013.

Capital structure, organisational structure, strategic asset planning and management

The Internal Capital Adequacy Assessment process (ICAAP) outlines the Company's approach for ensuring adequate capital is maintained over time and for monitoring compliance with regulatory capital requirements and targets.

The ICAAP includes:

- specific capital targets set in the context of the Company's risk profile, the Company Board's risk appetite and regulatory capital requirements;
- plans for how target levels of capital are to be met; and
- potential sources of additional capital, if required.

The ICAAP also sets out the Company's actions and procedures for monitoring compliance with its regulatory capital requirements and capital targets. These include:

- the setting of triggers to alert management to potential breaches of these requirements; and
- actions to avert and rectify potential breaches of these requirements.

Achieving capital targets is dependent on an appropriate level and mix of capital, and effective capital management to yield adequate returns. Oversight of the Company's capital management framework is performed by senior management, the QBE AusPac Executive Risk and Capital Committee and the Company Board Risk and Capital Committee.

Management has a particular focus on the following performance indicators.

- The Company actively manages the components of capital in order to maintain a level of eligible regulatory capital that exceeds APRA requirements. The Company Board set the target level of regulatory capital for 2019 at 1.32-1.44 times (2018: 1.32-1.44 times) the Prescribed Capital Amount (PCA).
- The Company is subject to regulatory requirements to maintain a minimum level of capital to meet obligations to policyholders. It is the Company's policy to maintain a capital base appropriate to its size, business mix, complexity and risk profile which fully complies with and meets or exceeds local regulatory requirements.
- Insurer financial strength ratings provided by the major rating agencies demonstrate the Company's financial strength and claims paying ability.

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

Tax risk management

The Company's approach to managing taxation risk is underpinned by QBE Group Tax Risk Policy.

The Company's approach to tax management is based on the following guiding principles:

- the Company seeks open, honest and transparent relationships with tax authorities in all relevant jurisdictions;
- the Company will comply with all applicable tax laws, regulations and disclosure requirements and pay the amount of tax that is legally required to be paid in all the jurisdictions in which the Company operates;
- the Company engages in efficient tax planning that supports our business and reflects commercial and economic activity – no transaction will be entered into where obtaining a tax benefit is the primary purpose; and
- the Company conducts transactions with other QBE companies on an arm's length basis in accordance with current Organisation for Economic Cooperation and Development (OECD) principles.

External environment, including disruption from competitors; economic, social and governance (ESG) risks; reputational impact; and geo‑political and regulatory uncertainty

The QBE Group Strategic Risk Policy governs the management of risks arising from the external environment.

Competitor actions, geo- political and regulatory uncertainty are monitored and regularly reported to the Company Board.

QBE Group's ESG Risk and Emerging Risk standards operationalise the Company's approach to managing ESG and emerging risks respectively, including climate change. Biannual horizon scans are performed on ESG and emerging risks, including assessment of potential financial and reputational impacts. Risk treatment plans are developed for material risks, which include development of underwriting and investment policy, monitoring frameworks and stress and scenario analysis. ESG risks and emerging risks are regularly reported to the QBE AusPac Executive Risks and Capital Committee and the Company Board Risk and Capital Committee.

Climate change is a material business risk for the Company, potentially impacting our business and customers in the medium to long-term. We have considered potential short‑term scenarios that could affect our insurance business written to date and our current investments, and we expect no material impact on the amounts recognised or disclosed in the financial statements.

3.2 Insurance risk

Overview

Insurance risk is the risk of fluctuations in the timing, frequency and severity of insured events and claims settlements, relative to expectations.

QBE AusPac classifies insurance risk into three sub-categories:

- underwriting;
- insurance concentration; and
- reserving.

The Company's approach to managing insurance risk is underpinned by QBE AusPac's insurance risk appetite statement and Insurance Risk Policy, which have been approved by the Company Board and is summarised below.

Underwriting risk

The Branch ceased to write new insurance policies in 2013.

The Branch is a monoline insurer providing residential lenders' mortgage insurance (LMI) in New Zealand. The Branch 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.

Insurance concentration risk

Insurance concentration risk for a lenders' mortgage insurer is the risk of catastrophic loss resulting from a prolonged economic downturn. The Company operates in Australia, New Zealand (in run-off) and has a subsidiary in Hong Kong. Its exposures are monitored and limits on maximum aggregate exposures to individual borrowers and per property, are contained in underwriting policies and embedded in systems and processes.

The Company is exposed to the possibility of 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. As required by APRA, the Company calculates its insurance concentration risk charge ("ICRC") which is the net probable maximum loss from a APRA prescribed three-year economic or property downturn equivalent to a 1-in-200 year event. As at 31 December 2019, the ICRC was $508.3 million (2018: $501.1 million).

Reserving risk

Reserving risk is managed through the actuarial valuation of insurance liabilities. The valuation of the net central estimate is performed by qualified and experienced actuaries, with reference to historical data and reasoned expectations of future events. The central estimate is subject to a comprehensive independent external review at least annually.

3.3 Credit risk

Overview

Credit risk is the risk of financial loss where a customer, counterparty or issuer fails to meet their financial obligations to the Branch in accordance to the agreed terms. The Branch's exposure to credit risk principally arises from cash and cash equivalents and/or a reduction or delay in repayments or interest payments from the default of counterparties such as mortgagees and reinsurers.

The Company's approach to managing credit risk is underpinned by QBE AusPac's credit risk appetite and Credit Risk Policy, which have been approved by the Company Board and are summarised below.

Reinsurance counterparty credit risk

The Company's objective is to place reinsurance, including that for the Branch, with highly rated counterparties. Concentration of risk with reinsurance counterparties is monitored strictly and regularly by QBE Group Security Committee and is controlled by reference to the following protocols:

- treaty reinsurance is placed in accordance with the requirements of the Company's REMS and security committee guidelines;
- reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historical claims and potential future losses based on the Company's insurance concentrations; and
- exposure to reinsurance counterparties and the credit quality of those counterparties is actively monitored.

Credit risk exposures are calculated regularly and compared with authorised credit limits. In certain cases, the Company requires letters of credit or other collateral arrangements to be provided to guarantee the recoverability of the amount involved. The Company holds $200.1 million (2018: $199.9 million) in collateral to support reinsurance recoveries on outstanding claims, including those of the Branch.

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

	CREDIT RATING						
	AAA $	AA $	A $	BBB $	SPECULATIVE GRADE $	NOT RATED $	TOTAL $
As at 31 December 2019							
Reinsurance recoveries on outstanding claims[1,2]	**-**	**-**	**41,601**	**-**	**-**	**-**	**41,601**
As at 31 December 2018							
Reinsurance recoveries on outstanding claims[1,2]	-	-	56,324	-	-	-	56,324

[1] The Branch has no reinsurance recoveries receivable on paid claims at 31 December 2019 (2018: nil).
[2] Excludes other non-reinsurance recoveries of $2,851 (2018: $4,824).

None of the Branch's reinsurance recoveries are past due or impaired or have terms that have been renegotiated and would otherwise have been past due or impaired (2018: nil).

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2019

Insurance and other credit risk

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

As an insurer, the Branch does not receive 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, the master policies require an insured to notify the insurer of a default within fourteen days of the end of the month when the total amount due is unpaid and in arrears by more than ninety days. For reporting and internal tracking purposes, the Branch does not consider a loan to be in default until it has been delinquent for three 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 collected the single premium from a prospective borrower and remitted the amount to the Branch. Under a standard LMI policy, premium payment was required before policy cover was incepted, which eliminated 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.

Investment and Treasury credit risk

The Company, including the Branch, only transacts with investment counterparties within the limits outlined in the delegated authorities. Investment counterparty exposure limits are applied to individual counterparty exposures and to multiple exposures within the one group of related companies in relation to cash deposits. Counterparty exposure limit compliance is monitored daily. The Branch's principal exposures relate to cash and cash equivalents.

The following table provides information regarding the Branch's aggregate credit risk exposure at the balance date in respect of the major classes of financial assets. The analysis classifies the assets according to S&P counterparty credit ratings. AAA is the highest possible rating. Rated assets falling outside the range of AAA to BBB are classified as speculative grade.

	CREDIT RATING						
	AAA **$**	**AA** **$**	**A** **$**	**BBB** **$**	**SPECULATIVE GRADE** **$**	**NOT RATED** **$**	**TOTAL** **$**
As at 31 December 2019							
Cash and cash equivalents	**-**	**1,102,995**	**-**	**-**	**-**	**-**	**1,102,995**
As at 31 December 2018							
Cash and cash equivalents	-	1,205,203	-	-	-	-	1,205,203

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

3.4 Liquidity risk

Overview

Liquidity risk is the risk of insufficient liquid assets to meet liabilities as they fall due or only being able to achieve the required level of liquidity at excessive cost. The Company's liquidity risk arises due to the nature of insurance activities where the timing and amount of cash outflows are uncertain.

The Company's approach to managing liquidity risk is underpinned by QBE AusPac's liquidity risk appetite and Liquidity Risk Policy, which have been approved by the Company Board.

The Company, including the Branch, manages liquidity risk using a number of tools, as follows:

- cash flow targeting;
- maintaining a minimum proportion of liabilities in liquid assets;
- cash flow forecasting; and
- stress testing and contingency planning.

Liquidity is managed using a number of cash flow forecasting and targeting tools and techniques. Cash flow forecasting and targeting is conducted at operational level and involves actively managing operational cash flow requirements.

To supplement the cash flow targeting and to ensure that there are sufficient liquid funds available to meet insurance and investment obligations, a minimum percentage of the Company's liabilities is held, at all times, in cash and liquid securities. The Company also maintains a defined proportion of funds under management in liquid assets.

The Company actively forecasts cash flow requirements, including for the Branch, to identify future cash surpluses and shortages to optimise invested cash balances and limit unexpected calls from the investment pool. The Company limits the risk of liquidity shortfalls resulting from mismatches in the timing of claims payments and receipts of claims recoveries by negotiating cash call clauses in reinsurance contracts and seeking accelerated settlements for large reinsurance recoveries.

The following table summarises the maturity profile of the Branch's financial liabilities based on the remaining contractual obligations.

	1 YEAR OR LESS $	1 TO 3 YEARS $	3 TO 5 YEARS $	OVER 5 YEARS $	TOTAL $
As at 31 December 2019					
Trade and other payables	**116,782**	**-**	**-**	**-**	**116,782**
As at 31 December 2018					
Trade and other payables	58,716	-	-	-	58,716

The maturity profile of the Branch's net discounted central estimate is analysed in note 2.3.6.

The maturity of the Branch's directly held interest-bearing financial assets is shown in the table below.

		INTEREST BEARING FINANCIAL ASSETS MATURING IN						
		1 YEAR OR LESS $	1 TO 2 YEARS $	2 TO 3 YEARS $	3 TO 4 YEARS $	4 TO 5 YEARS $	OVER 5 YEARS $	Total $
As at 31 December 2019								
Floating rate	$	**1,102,995**	**-**	**-**	**-**	**-**	**-**	**1,102,995**
Weighted average interest rate	%	**0.15%**						**0.15%**
As at 31 December 2018								
Floating rate	$	1,205,203	-	-	-	-	-	1,205,203
Weighted average interest rate	%	0.15%						0.15%

3.5 Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events (including legal risk).

Operational risk can materialise in a number of forms including internal fraud, external fraud, employment practices and workplace safety, improper business practices, damage to physical assets, business disruption and system failures and execution, delivery and process management.

The Company's approach to managing operational risk is underpinned by QBE AusPac's operational risk appetite and Operational Risk Policy, which have been approved by the Company Board.

The Company, including the Branch, identifies and assesses operational risk through:

- The Risk and Control Self-Assessment (RCSA) process, which identifies and assesses the key risks to achieving business objectives and is conducted at business unit level.
- The Operational Risk Appetite Statement, which sets out the nature and level of risk the Company Board is willing to take in pursuit of the organisation's objectives. The Operational Risk Appetite Statement is measured through an assessment of the control environment, key risk indicators, issues and incidents.
- The emerging risk process, which identifies and assesses new risks, which are characterised by incomplete but developing knowledge or existing risks that develop in new or surprising ways.
- The scenario analysis process, which assesses the impact of potentially extreme scenarios and the appropriateness of our contingency planning.

3.6 Compliance risk

Overview

Compliance risk is the risk of legal or regulatory penalties, financial loss or impacts and non-financial loss or impacts (including reputational damage) resulting from a breach of obligations. Obligations refers to those in legislation, regulation, industry codes and standards, internal polices and ethical and business standards.

The Company's approach to managing compliance risk is underpinned by QBE AusPac's compliance risk appetite, which have been approved by the Company Board and is summarised below.

The Company, including the Branch, manages compliance risk through its governance, culture, stakeholder management and strategy approach. There are six components for managing compliance risk with defined responsibilities across the three lines of defence:

- identify compliance obligations and controls;
- embed compliance obligations across systems and process;
- communicate and train staff on compliance requirements;
- monitor obligations and controls;
- identify and rectify issues, incidents and breaches; and
- report on and assess the state of compliance.

Compliance management is subject to continuous improvement, recognising changes in the regulatory and legal environment and industry, customer and community expectations.

3.7 Group Risk

Overview

Group risk is the risk a division arising specifically from being part of the wider QBE Group, including financial impact and loss of support from the parent company.

The Company's approach to managing group risk is underpinned by QBE AusPac's risk appetite, which have been approved by the Company Board and is summarised below.

Sources of group risk may include group initiatives or strategies with a material impact on one or more divisions, shared global reinsurance programs, inter-company loans and shared use of centralised group functions (such as for procurement and information technology). Group risk also includes the potential risk from reputational contagion.

The Company, including the Branch, manages group risk through various systems, controls and processes, including the use of intercompany transactions and balances accounting guidance, transfer pricing guidelines and investment management agreements.

4. CAPITAL STRUCTURE

Overview

QBE Group's objective in managing capital is to maintain an optimal balance between debt and equity in order to reduce the overall cost of capital whilst satisfying the capital adequacy requirements of regulators and rating agencies, providing financial security for our policyholders and continuing to provide an adequate return to shareholders. As a wholly owned member of the group, the Company has adopted the capital management policies and framework of the QBE Group.

Details of the Company's approach to capital risk management are disclosed in note 3.1.

4.1 Cash and cash equivalents

	2019 **$**	**2018** **$**
Cash at bank on hand	**171,706**	236,606
Overnight money	**931,289**	968,597
	1,102,995	1,205,203
Analysed as follows:		
Floating interest rate	**1,102,995**	1,205,203
	1,102,995	1,205,203

How we account for the numbers

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

Cash and cash equivalents are initially measured at fair value then subsequently at amortised cost and are subject to an insignificant risk of change in value.

Cash and cash equivalents are subjected to impairment testing using the ECL methodology. The Branch considers that credit risk has not increased significantly since initial recognition, and that these assets represent low credit risks, taking into account the credit standing of the counterparties and the nature of the exposures. The Company foresees negligible credit losses arising on cash and cash equivalents from possible default events within 12 months from the reporting date, and considers that no allowance for impairment is required at 31 December 2019 (2018: $nil).

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

The reconciliation of profit after income tax to cash flows from operating activities is included in note 6.3.

4.2 APRA capital adequacy (Solvency)

Overview

APRA Prudential Standard GPS 110 Capital Adequacy for General Insurers requires that the Company maintain a capital base in excess of its prudential capital requirement as defined under the prudential standard.

The following table discloses the capital adequacy calculated in accordance with the APRA prudential framework for the Company. The 2018 and 2019 position reflects the December quarter APRA return (unaudited).

	2019 A$M	2018 A$M
Eligible Tier 1 capital as defined by APRA		
Contributed equity	**364.3**	364.3
General reserves	**0.5**	0.5
Retained profits[1]	**550.8**	568.8
Insurance liability surplus	**67.6**	51.3
Total equity	**983.2**	984.9
Less: APRA deductions	**75.2**	76.1
Actual solvency capital	**908.0**	908.8
Minimum solvency capital (APRA capital requirement)	**611.7**	639.3
Solvency margin	**296.3**	269.5
Solvency ratio	**1.48**	1.42

[1] Retained profits are in accordance with APRA prudential standards

5. TAX

Overview

Income tax expense is the accounting tax charge for the period and is calculated as the tax payable on the current period taxable income based on the applicable income tax rate, adjusted for changes in deferred tax assets and liabilities attributable to temporary differences and unused tax losses. The relationship between accounting profit and income tax expense is provided in the reconciliation of prima facie tax to income tax expense (note 5.1). Income tax expense does not equate to the amount of tax actually paid to tax authorities as it is based upon the accrual accounting concept.

Accounting income and expenses do not always have the same recognition pattern as taxable income and expenses, creating a timing difference as to when a tax expense or benefit can be recognised. These differences usually reverse over time but until they do, a deferred tax asset or liability is recognised on the balance sheet. Note 5.2 details the composition and movements in deferred tax balances and the key management assumptions applied in recognising tax losses.

The Company's approach to managing tax risk is disclosed in note 3.1.

5.1 Income tax

Reconciliation of prima facie tax to income tax expense

	NOTE	2019 $	2018 $
(Loss) profit before income tax		**(50,908)**	443,097
Prima facie tax (receivable) payable at 28%		**(14,254)**	124,067
Prima facie tax adjusted for non-temporary differences		**(14,254)**	124,067
Income tax (benefit) expense		**(14,254)**	124,067
Analysed as follows:			
Current tax		**18,935**	142,649
Deferred tax		**(33,189)**	(18,582)
		(14,254)	124,067
Deferred tax benefit comprises:			
Deferred tax assets recognised in profit or loss	5.2.1	**(26,752)**	-
Deferred tax liabilities recognised in profit or loss	5.2.2	**(6,437)**	(18,582)
		(33,189)	(18,582)

How we account for the numbers

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

Current tax assets and tax liabilities are offset where the Branch has a legally enforceable right to offset and intends to either settle on a net basis or to realise the asset and settle the liability simultaneously. Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, as appropriate.

5.2 Deferred income tax

	NOTE	2019 $	2018 $
Deferred tax assets	5.2.1	**26,752**	-
Deferred tax liabilities	5.2.2	**-**	6,437

5.2.1 Deferred tax assets

The balance comprises temporary differences attributable to:

	NOTE	2019 $	2018 $
Amounts recognised in profit or loss			
Insurance provisions		**26,752**	-
Deferred tax assets	5.2	**26,752**	-
Deferred tax assets analysed as follows:			
Recoverable within 12 months		**26,752**	-
Recoverable greater than 12 months		**-**	-
		26,752	-

Movements:

	NOTE	2019 $	2018 $
At 1 January		**-**	**-**
Amounts recognised in profit or loss	5.1	**26,752**	**-**
At 31 December		**26,752**	**-**

5.2.2 Deferred tax liabilities

The balance comprises temporary differences attributable to:

	NOTE	2019 $	2018 $
Amounts recognised in profit or loss			
Insurance assets		**-**	6,437
Deferred tax liabilities	5.2	**-**	6,437
Deferred tax liabilities analysed as follows:			
Payable within 12 months		**-**	4,759
Payable greater than 12 months		**-**	1,678
		-	6,437

Movements:

	NOTE	2019 $	2018 $
At 1 January		**6,437**	25,019
Amounts recognised in profit or loss	5.1	**(6,437)**	(18,582)
At 31 December		**-**	6,437

How we account for the numbers

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

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

Deferred tax assets and liabilities are offset in the financial statements when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority.

5.2.3 Tax losses

The Branch has brought to account nil tax losses (2018: nil).

6. OTHER

Overview

This section includes other information that must be disclosed to comply with the New Zealand Accounting Standards or the *Corporations Act 1993*.

6.1 Other accounting policies

6.1.1 New and amended standards adopted by the Branch

The Branch adopted the following new or revised accounting standards which became effective for the annual reporting period commencing on 1 January 2019.

TITLE	
IFRIC Interpretation 23	*Uncertainty over Income Tax Treatments*

6.1.2 New accounting standards and amendments issued but not yet effective

TITLE		OPERATIVE DATE
NZ IFRS 3 amendments	*Definition of a Business*	1 January 2020
NZ IAS 1 and NZ IAS 8 amendments	*Definition of Material*	1 January 2020
2018 NZ Conceptual Framework	*New Zealand Equivalent to the IASB Conceptual Framework for Financial Reporting*	1 January 2020
	Amendments to Conceptual Framework for Financial Reporting	1 January 2020
NZ IFRS 17	*Insurance Contracts*	1 January 2021

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

The Branch currently plans to apply the standards and amendments detailed above for the reporting periods beginning on the operative dates set out above. An initial assessment of the financial impact of the standards and amendments has been undertaken and they are not expected to have a material impact on the Branch's financial statements, except where noted below.

NZ IFRS 17 *Insurance Contracts*

NZ IFRS 17, was adopted by the New Zealand Accounting Standards Board on 10 August 2017. It is currently effective for reporting periods beginning on or after 1 January 2021, but this is expected to be deferred to 1 January 2022 following a tentative decision by the International Accounting Standards Board (IASB) to delay the mandatory implementation date by one year.

The standard will be applicable to general, life and health insurance business and introduces a new 'general model' for recognition and measurement of insurance contracts. It also permits application of a simplified model (which is similar to the current basis on which general insurance is brought to account under NZ IFRS 4) if the liability for remaining coverage under the simplified model would not materially differ from the general model.

The Company has completed an initial impact assessment and additional analysis on key areas of interpretation. The Company anticipates that the general model will be the most appropriate basis for measuring the liability for remaining coverage for the Branch.

This analysis also identified key requirements of AASB 17 where the technical interpretation remains unclear. In addition, the IASB is in the process of considering potential changes to the wording of IFRS 17 to remedy implementation issues identified and it is expected these changes would then be adopted into NZ IFRS 17 during 2020.

Given the potential for changes in NZ IFRS 17 and the broad scope, complexity and lack of general consensus on the interpretation of some key areas of the standard, the impact of NZ IFRS 17 on the Branch's financial statements is still being determined; however, significant disclosure changes and some impact on reported profit or loss are expected. The Company continues to monitor market developments in order to assess the impact of changes and evolving interpretations on the Branch and to prepare financial reporting systems for the required changes. In addition, recent indications from APRA regarding the impact of AASB 17 (the Australian equivalent standard) on both reporting to APRA and the measurement of capital required by APRA are under consideration and the impacts on the Company's implementation project are being assessed.

6.2 Contingent liabilities

Overview

Contingent liabilities are disclosed when the possibility of a future settlement is expected to result in an outflow of resources and is considered to be less than probable but more likely than remote. If the expected settlement of the liability becomes probable, a provision is recognised.

In the normal course of business, the Branch is exposed to contingent liabilities in relation to claims litigation arising out of its insurance and reinsurance transactions and may be exposed to the possibility of contingent liabilities in relation to non-insurance litigation. Provisions are made for non-insurance obligations that are probable and quantifiable.

The Branch had no contingent liabilities as at 31 December 2019 (2018: nil).

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

	2019 $	2018 $
Profit after income tax	**36,654**	319,030
Decrease in net outstanding claims	**(40,497)**	(174,849)
Decrease in unearned premiums	**(129,699)**	(576,511)
Decrease in unearned reinsurance commission	**(13,190)**	(58,631)
Decrease in deferred insurance costs	**81,354**	325,794
Decrease in reinsurance and other recoveries	**16,696**	71,145
Increase in trade and other receivables	**(1,947)**	(1,913)
Increase (decrease) in trade and other payables	**58,066**	(6,402)
Decrease in deferred tax liabilities	**(33,189)**	(18,582)
(Increase) decrease in amounts due from tax authorities for current tax	**(98,691)**	30,369
Increase in unexpired risk liability	**95,543**	-
Cash flows from operating activities	**(102,208)**	(90,550)

6.4 Remuneration of auditors

Overview

The Company may engage the external auditor for non-audit services other than excluded services subject to the general principle that fees for non-audit services should not exceed 50% of all fees paid to the external auditor in any one financial year at the ultimate parent entity level. The Board believes some non-audit services are appropriate given the external auditor's knowledge of the Company. External tax services are generally provided by an accounting firm other than the external auditor. Consistent with prior periods, the external auditor cannot provide the excluded services of preparing accounting records or financial reports or acting in a management capacity.

	2019 $	2018 $
PricewaterhouseCoopers (PwC) – Australian firm		
Audit of financial reports of the Company	**585,350**	600,406
Audit of statutory returns and other assurance services	**170,456**	174,841
	755,806	775,247

6.5 Related parties

6.5.1 Parent entity

The Branch forms part of QBE Lenders' Mortgage Insurance Limited, a Company incorporated and domiciled in Australia.

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

6.5.2 Transactions with related parties

The following material transactions occurred with related parties:

	2019 $	2018 $
Revenue		
Reinsurance recoveries received or receivable from related entities	**(11,585)**	64,159
Expenses		
Management fees paid to related parties	**33,944**	64,866

6.5.3 Outstanding balances arising from transactions with related parties

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

	2019 $	2018 $
Current assets		
Amounts due from related entities	**11,339**	9,392
Reinsurance recoveries from related entity on outstanding claims	**41,601**	56,324
Current liabilities		
Amounts due to related entities	**116,595**	56,975

How we account for the numbers

All transactions were made on normal commercial terms and conditions.

Outstanding balances are unsecured, interest free and repayable on demand.

6.6 Events occurring after reporting date

There is, at the date of this report, no other matter or circumstance that has arisen since 31 December 2019 that, in the opinion of the directors, has significantly affected or may significantly affect the Branch's operations, the results of those operations, or the Branch's state of affairs in future financial periods.