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Sentinel
A Reason to Smile

# SENTINEL ASSURANCE COMPANY LIMITED
## ANNUAL FINANCIAL STATEMENTS
### FOR THE YEAR ENDED 31 March 2010

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## SENTINEL ASSURANCE COMPANY LIMITED

**Annual Financial Statements**
**For the year ended 31 March 2010**

**Contents**

## SENTINEL ASSURANCE COMPANY LIMITED

**Company Directory**
**For the year ended 31 March 2010**

| | |
|---|---|
| **ACTIVITIES:** | Life insurance |
| **DIRECTORS:** | Christopher Laurence COON<br>Ian Robert HENDRY |
| **SHAREHOLDER:** | *Sentinel Limited* |
| **REGISTERED OFFICE & SHARE REGISTRY:** | 87 Hurstmere Road<br>Takapuna<br>Auckland |
| **AUDITORS:** | KPMG<br>P O Box 1584<br>Auckland |
| **BANKERS:** | Commonwealth Bank of Australia, New Zealand Branch<br>P O Box 35<br>Auckland |
| | ASB Bank<br>P O Box 35<br>Auckland |
| **SOLICITORS:** | Hesketh Henry<br>Private Bag 92 093<br>Auckland |
| | Sanderson Weir<br>P O Box 856<br>Shortland Street<br>Auckland |
| **EXTERNAL ACTUARY:** | Davies Financial and Actuarial Limited<br>PO Box 35-258<br>Browns Bay<br>Auckland |

This Annual Report includes the financial statements of Sentinel Assurance Company Limited (the Company) for the year from 1 April 2009 to 31 March 2010.

ANNUAL REPORT DISCLOSURES
The Company's sole shareholder, Sentinel Limited, has passed a resolution under section 211(3) of the Companies Act 1993 ("the Act") in order that the Company need not comply with section 211(1)(a) and (e) to (j) of the Act.

DIRECTORS
Directors of the Company who held office during the period were:

Christopher Laurence COON
Ian Robert HENDRY

DIRECTORS' APPROVAL

For and on behalf of the board on 30 June 2010

C L Coon
Director

I R Hendry
Director

## SENTINEL ASSURANCE COMPANY LIMITED

### Statement of Comprehensive Income

| For the year ended 31 March 2010<br>$ millions | Notes | 2010 | 2009 |
|---|---|---|---|
| **Revenue** | | 20.312 | 18.474 |
| Net premium income | 3 | 17.416 | 15.773 |
| Net investment income | 4 | 0.202 | 1.489 |
| Total net income | | 17.618 | 17.262 |
| *Less:* | | | |
| Operating expenses | 5 | 7.632 | 6.882 |
| Net change in policy liabilities | 8 | 4.192 | 6.402 |
| Net profit before taxation | | 5.794 | 3.978 |
| Less taxation | 6 | 0.000 | 0.000 |
| **Profit for the year** | 8 | 5.794 | 3.978 |
| **Other comprehensive income** | | 0.000 | 0.000 |
| **Total comprehensive income for the year** | | **5.794** | **3.978** |

The accompanying notes form part of these financial statements

## SENTINEL ASSURANCE COMPANY LIMITED
### Statement of Changes in Equity

| $ millions | Share capital | Retained earnings | Total equity |
|---|---|---|---|
| **For the year ended 31 March 2010** | | | |
| Balance at beginning of year | 0.500 | 8.707 | 9.207 |
| Total comprehensive income for year: | | | |
| Profit or loss | 0.000 | 5.794 | 5.794 |
| Other comprehensive income | 0.000 | 0.000 | 0.000 |
| | 0.000 | 5.794 | 5.794 |
| **Balance at 31 March 2010** | 0.500 | 14.501 | 15.001 |
| **For the year ended 31 March 2009** | | | |
| Balance at beginning of year | 0.500 | 4.729 | 5.229 |
| Total comprehensive income for year: | | | |
| Profit or loss | 0.000 | 3.978 | 3.978 |
| Other comprehensive income | 0.000 | 0.000 | 0.000 |
| | 0.000 | 3.978 | 3.978 |
| **Balance at 31 March 2009** | 0.500 | 8.707 | 9.207 |

The accompanying notes form part of these financial statements

## SENTINEL ASSURANCE COMPANY LIMITED
### Statement of Financial Position

| As at 31 March 2010<br>$ millions | Notes | 2010 | 2009 |
|---|---|---|---|
| **Equity** | | | |
| Share capital | 7 | 0.500 | 0.500 |
| Accumulated profit | | 14.501 | 8.707 |
| Total Equity | | 15.001 | 9.207 |
| **Liabilities** | | | |
| Sentinel Limited | 10 | 0.000 | 1.091 |
| Insurance contract reserves | 8 | 29.812 | 34.105 |
| Investment contract liability | 8 | 0.223 | 0.237 |
| Total Liabilities | | 30.035 | 35.433 |
| Total Funds Employed | | 45.036 | 44.640 |
| **Assets** | | | |
| Cash at bank | | 0.011 | 0.006 |
| NZ Government stock | 9 | 0.542 | 0.554 |
| Sentinel Finance Limited | 10 | 9.785 | 8.417 |
| Australian Seniors Finance Pty Limited | 10 | 11.094 | 6.723 |
| Seniors Money International Limited | 10 | 8.856 | 5.717 |
| Insurance contract liabilities ceded | 8 | 14.748 | 23.223 |
| Total Assets | | 45.036 | 44.640 |

The accompanying notes form part of these financial statements

These accounts are authorised for and on behalf of the Board of Directors on 30 June 2010

C L Coon
Director

I R Hendry
Director

## SENTINEL ASSURANCE COMPANY LIMITED

### Statement of Cash Flows

| For the year ended 31 March 2010<br>$ millions | Notes | 2010 | 2009 |
|---|---|---|---|
| **Net Cash from Operating Activities:** | | | |
| Premiums | | 0.000 | 0.000 |
| Interest income | | 0.032 | 0.034 |
| Policy withdrawals | | (0.024) | (6.706) |
| Bank charges | | (0.003) | 0.000 |
| **Net Cash from Operating Activities** | 11 | 0.005 | (6.672) |
| **Net Cash from Investing Activities:** | | 0.000 | 0.000 |
| **Net Cash from Financing Activities:** | | | |
| Receipt / (Payment) of funds from / (to) Sentinel Limited | | 0.000 | 6.655 |
| **Net Cash from Financing Activities** | | 0.000 | 6.655 |
| Net increase in cash and equivalents | | 0.005 | (0.017) |
| Opening Balance | | 0.006 | 0.023 |
| **Closing Balance** | | 0.011 | 0.006 |

The accompanying notes form part of these financial statements

## 1. STATEMENT OF ACCOUNTING POLICIES

*REPORTING ENTITY AND BASIS OF PREPARATION*

The reporting entity is Sentinel Assurance Company Limited (the Company), a wholly owned subsidiary of Sentinel Limited (Sentinel). Sentinel is a wholly owned subsidiary of Seniors Money International Limited (the Parent or Group). Seniors Money International Limited commenced business in February 2004. Principal activities of the Group are the provision of equity release loans and related financial services, initially in New Zealand, and subsequently on an international basis. Sentinel Assurance Company Limited is registered under the Companies Act 1993. The financial statements have been prepared in accordance with New Zealand generally accepted accounting practice, applying International Financial Reporting Standards (IFRS), including New Zealand equivalents, as appropriate to profit-oriented entities. The measurement base adopted is that of historical cost as modified by application of NZ IFRS 4 explained further under specific accounting policies. The financial statements are presented in millions of New Zealand Dollars (NZD) rounded to three decimal places.

The financial statements have been prepared on the basis that the Company is a going concern.

*SPECIFIC ACCOUNTING POLICIES*

**Financial assets and liabilities**
*Classification*
The Company classifies financial instruments into the following categories: cash and cash equivalents, loans and receivables, NZ Government stock, trade and other payables. The classification depends on the purpose for which the assets and liabilities were acquired. Management determines the classification of its assets and liabilities at initial recognition.

*Recognition*
Financial assets and liabilities are recognised on the date the Company becomes party to the contractual provisions of the instrument.

*Measurement*
Fixed interest securities are held at fair value through profit and loss, fair value is determined with reference to quoted prices. Gains and losses arising from the revaluation of investments are included as part of net investment income in the statement of comprehensive income. Loans and advances and other receivables are held at fair value plus any interest accrued to date. Provision is made against impaired loans. Trade and other payables are recognised in the statement of financial position at historical cost plus any interest or additional costs accrued to balance date.

*Provisions*
A provision is recognised when the Company has a present obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If material, provisions are determined by discounting the expected future cash flows at a rate that reflects current market rates and the risks specific to the liability.

## 1. STATEMENT OF ACCOUNTING POLICIES (continued)

**Impairment**
*Financial assets*
At each reporting date the Company assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset that can be reliably estimated. Evidence of impairment is reviewed on a specific asset basis.

**INSURANCE CONTRACTS**
Insurance and reinsurance products entered into by the Company are classified as either insurance contracts or investment contracts. Insurance contracts involve the acceptance of significant insurance risk. Insurance risk is significant when the benefits payable upon the occurrence of the insured event are significantly higher than the benefits payable upon surrender or maturity.

Investment contracts are contracts issued by the Company other than insurance contracts. For the purposes of these financial statements, holders of life insurance contracts and life investment contracts are referred to as policyholders.

**Insurance contract liabilities**
Insurance contract liabilities are calculated using the Margin on Services (MoS) methodology in accordance with New Zealand Society of Actuaries Professional Standard 3: Determination of Life Insurance Policy Liabilities and the requirements of NZ IFRS 4.

Profits are recognised over the life of the policies based on services provided, whereas losses are recognised immediately when they arise. Services used to determine profit recognition include the cost of expected claims, maintenance of policies, and investment management. Policy liabilities are generally determined as the present value of all future expected payments, expenses, taxes and profit margins reduced by expected future premiums and reinsurance recoveries.

**Investment contract liabilities**
Investment contract liabilities are accounted for as a financial liability and recognised at fair value. Movements in fair value are recognised through the statement of comprehensive income.

**Income recognition**
*Interest and investment income*
Interest income is recognised as it accrues. Investment income also includes realised and unrealised changes in the fair value of investments.

*Premium and claims recognition*
Insurance contracts are separated into risk and savings components. Premiums and claims related to risk contracts (or components) are recognised in the statement of comprehensive income as either income or expense. All other premiums and claims are recognised as increases or decreases to policy liabilities in the statement of financial position.

Premiums with a regular due date are recognised when the premium becomes due. Premiums with no due date are recognised on a cash basis. Surrenders are recognised when paid. Death and all other claims are recognised when the liability to the policyholder has been established.

*Reassurance*
Reassurance premiums and claims are recognised separately in the statement of comprehensive income when they become due and payable in accordance with the reassurance agreements. Reinsurance recoveries, when they occur, are also recognised separately in the statement of comprehensive income. Profit shares are treated as a deduction from premiums. The present value of financial reassurance arrangements, adjusted for any reinsurance recoveries, are recognised within policy liabilities in the statement of financial position. Reinsurance reserve deposits and reinsurance recoveries are included, separately from policy liabilities in the statement of financial position.

## 1. STATEMENT OF ACCOUNTING POLICIES (continued)

*Expenses*
Life insurance expenses are categorised into policy acquisition, investment management and maintenance expenses. Policy acquisition expenses are the incremental and directly attributable costs related to the origination and issue of a policy, including commission. Investment management costs are those directly related to management of investments supporting the life insurance fund, whereas maintenance expenses include all other costs of the business including those related to administration of inforce policies. Policy acquisition costs are initially charged to the statement of comprehensive income, however, are effectively deferred over the life of the policy through inclusion in future profit margins. Interest expense is recognised in the statement of comprehensive income as it accrues.

*Life insurance tax*
Life insurers are subject to a special tax regime. Two tax bases are maintained: the life office base which is subject to tax on investment income less expenses plus underwriting income, and the policyholder base which seeks to tax benefits as they accrue to policyholders under the policies. The life insurer pays tax on the higher of the two bases at the company tax rate of 30% (2009: 30%). The life insurer is able to use accumulated imputation credits generated in the life office base to meet any tax liability arising in the policyholder base. As the life insurer is taxed as proxy for the policyholder, returns to policyholders are exempt.

**Goods and Services Tax (GST)**
The Company's activities are exempt supplies for the purposes of GST. Accordingly, all items of income and expenditure are stated inclusive of GST.

**Foreign currency transactions**
Foreign currency transactions are translated to New Zealand currency at the exchange rate ruling at the date of the transaction. Amounts receivable and payable in foreign currency at balance date are translated at the rate at that date. Exchange differences arising from the translation of amounts payable and receivable in foreign currencies are recognised in the statement of comprehensive income.

**Statement of Cash Flows**
The statement of cash flows has been prepared using the direct approach modified by netting the cash flows associated with financing from Seniors Money International Limited.

*Adoption of new accounting standards:*

(i) The Company has applied the requirements of NZ IAS 1 Presentation of Financial Statements (2007) in these financial statements. All owner changes in equity are presented in the statement of changes in equity whereas non-owner changes in equity are included in the statement of comprehensive income. The revised standard does not change the measurement or disclosure of transactions required by other NZ IFRS.

(ii) The Company has applied Improving Disclosures about Financial Instruments (Amendments to NZ IFRS 7) issued in March 2009. The amendments require that fair value measurement disclosures use a three-level hierarchy that reflects the significance of the inputs used in measuring fair values of financial instruments. Specific disclosures are required when fair value measurements are categorised as level 3 (significant unobservable inputs) in the fair value hierarchy. The amendments require that any significant transfers between level 1 and level 2 of the fair value hierarchy be disclosed separately, distinguishing between transfers into and out of each level. Furthermore, changes in valuation techniques from one period to another, including the reasons, are required to be disclosed for each class of financial instruments.

*New accounting standards and interpretations not yet adopted:*
A number of new standards, amendments to standards and interpretations are not yet effective, and have not been applied in preparing these financial statements. None of these will have an effect on the financial statements of the Company, with the exception of: NZ IFRS 9 Financial Instruments. The requirements of this standard represent a significant change from NZ IAS 39 in respect of financial assets. The new standard contains two primary measurement categories for financial assets: amortised cost and fair value, and eliminates the existing NZ IAS 39 categories of held to maturity, available for sale, and loans and receivables. A financial asset would be measured at amortised cost if it is held to collect contractual cash flows of principal and interest on specified dates. All other financial assets would be measured at fair value. These requirements are not expected to substantially change the way the Company currently measures and presents financial instruments.

**Changes in accounting policies**
NZ IFRS accounting policies have been consistently applied throughout the year. Certain comparatives have been reclassified to align with current year presentation.

## 2. USE OF ESTIMATES AND JUDGEMENT

The preparation of a financial report in conformity with NZ GAAP requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable in the circumstances, the results of which form the basis of judgements about the carrying values of assets and liabilities. Actual results may vary from estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

In particular, information about significant areas of estimation uncertainty and critical judgement in applying accounting policies that have the greatest effect on the amount recognised in the financial statements are described in the following areas:

*Life insurance liabilities*
Policy liabilities are determined by qualified actuaries using key assumptions and professional judgements. Key assumptions in determining policy liabilities are as follows:

Policy liabilities have been determined by Mr. Peter Davies B.Bus.Sc., FIA, FNZSA, a Fellow of the New Zealand Society of Actuaries. The Actuary is satisfied as to the nature and quality of the data. The assumptions used in the current year and sensitivities in respect of these assumptions are outlined below.

Solvency reserves have been set by the Directors. Refer Note 8 (e).

Funeral Plan liabilities are calculated as the accumulation of an interpolated scale from the premium at commencement to the projected sum insured at the end of year two.

Term Deposit Bond liabilities have been calculated as the accumulated bond balance including interest and bonus interest.

The negative equity reserve is an accumulation of the previous year's liability, plus interest, plus a proportion of negative equity premiums earned during the year. This proportion equaled 11% for New Zealand (2009: 30%), 8% for Australia (2009: 28%), 36% for Ireland (2009: 48%) and 50% for Spain (2009: 42%).

Discount rate: 6.0% per annum (2009: 5.3%)

House inflation:
New Zealand: An initial 10% reduction, followed by growth of 2.5% per annum (2009: 20% reduction, 2.5% pa growth)
Australia: An initial 10% reduction, followed by growth of 2.0% per annum (2009: 20% reduction, 2.5% pa growth)
Ireland and Spain: An initial 20% reduction, followed by growth of 1.0% per annum (2009: 20% reduction, 2.5% pa growth)

Mortality: Realistic assumptions with mortality improvements (2009: same)

Early repayment:
New Zealand and Australia: 5% per annum (2009: 5%)
Ireland: 1% per annum (2009: 1%)
Spain: 1% per annum (2009: 3%)

The rate of accumulation is reviewed each year to ensure that the principles of NZ IFRS 4 are being adhered to, noting that small variations in assumptions can have a magnified impact on the emergence of profit.

Interest margin over cost of funds:

| | |
|---|---|
| New Zealand | 2.24% (2009: 2.75%) |
| Australia | 1.68% (2009: 2.50%) |
| Ireland | 2.03% (2009: 2.50%) |
| Spain | 2.03% (2009: 2.50%) |

Since all classes of business have been valued on an accumulation basis, there is no break-down of future cash-flows required between premiums, claims, expenses and profit margins.

**$ millions**

## 2. USE OF ESTIMATES AND JUDGEMENT (Continued)

**Sensitivity analysis**
The impact of changes in key outstanding claims variables are summarised below. Each change has been calculated in isolation of the other changes and each change shows the relevant impact assuming that there is no change to the other variables.

The net impact on the policy liabilities given the following changes:

| | Variable change | Change in best estimate liability 2010 | 2009 |
|---|---|---|---|
| Discount rate | +1% | (2.370) | (11.260) |
| | -1% | 4.950 | 20.590 |
| Client interest rate | +1% | 59.640 | 130.870 |
| | -1% | (26.150) | (58.960) |
| Reduction in property values | +10% | 21.150 | 43.690 |
| | -10% | (14.510) | (28.900) |
| House inflation | +1% | (31.240) | (62.610) |
| | -1% | 42.170 | 83.000 |
| Mortality | +10% | (3.070) | (9.340) |
| | -10% | 4.170 | 14.460 |
| Early repayment | +1% | (0.470) | (8.150) |
| | -1% | 1.850 | 15.060 |

The movement in the liability balance would have a net opposite impact on the statement of comprehensive income.

**$ millions**

| **3. NET PREMIUM INCOME** | **2010** | **2009** |
|---|---|---|
| Risk policies: | | |
| No-neg - Sentinel Finance Limited | 5.113 | 4.817 |
| No-neg - Australian Seniors Finance Limited | 6.466 | 5.771 |
| No-neg - Seniors Money International Limited | 6.515 | 5.785 |
| Net reassurance expense | (0.678) | (0.600) |
| Net premium income | 17.416 | 15.773 |

### 4. NET INVESTMENT INCOME

| | | |
|---|---|---|
| Interest income from: | | |
| NZ Government stock - fair value through profit and loss | 0.032 | 0.034 |
| Interest from related parties | 1.031 | 0.887 |
| | 1.063 | 0.921 |
| Unrealised (loss) gain on foreign currency | (0.848) | 0.537 |
| Unrealised (loss) gain on NZ Government stock fair value through profit and loss | (0.013) | 0.031 |
| | 0.202 | 1.489 |

### 5. OPERATING EXPENSES

| | | |
|---|---|---|
| *Included in operating expenses are:* | | |
| Commission paid | 5.428 | 4.912 |

The Parent has paid audit fees on the Company's behalf of $0.039 million (2009: $0.044 million).

All of the operating expenses for the year are deemed policy maintenance expense.

### 6. TAXATION

In respect of the Life Office Base, losses available to carry forward to future income years are $11.462 million (2009: $5.148 million). There are no unrecognised temporary differences carried forward. Taxable income on the Policyholder Base was a loss of $25.831 million for the year (2009: loss $23.136 million), subject to legislation changes and assessment by the Inland Revenue Department.

Since 31 March 2010 the Government has announced that the company tax rate will reduce from 30% to 28% effective for years on or after 1 April 2011. The change has no immediate financial effect as the Company has no tax related assets or liabilities.

### 7. SHARE CAPITAL

The Company has issued 500,000 fully paid ordinary shares (2009: 500,000) held by Sentinel Limited. All shares have equal rights to dividends, voting and on winding-up.

**$ millions**

## 8. (a) INSURANCE CONTRACTS

| | 2010 | 2009 |
|---|---|---|
| Balance at beginning of year | 34.105 | 16.413 |
| (Decrease) increase in liabilities recognised in the statement of comprehensive income | (4.293) | 17.692 |
| Balance at end of year | 29.812 | 34.105 |

**Breakdown of insurance contract reserves**

| | 2010 | 2009 |
|---|---|---|
| Future premiums | (274.433) | (363.592) |
| Future reinsurance premiums | 43.125 | 47.368 |
| Future commissions | 82.330 | 109.078 |
| Reinsurance profit share commissions | (17.211) | (13.765) |
| Profit-share payments to policyholders | 22.400 | 38.808 |
| Future claims | 83.879 | 169.758 |
| Profit margins | 89.722 | 46.450 |
| | 29.812 | 34.105 |

## 8. (b) INSURANCE CONTRACTS CEDED

| | 2010 | 2009 |
|---|---|---|
| Balance at beginning of year | 23.223 | 11.749 |
| Movement during the year | (8.475) | 11.474 |
| Balance at end of year | 14.748 | 23.223 |

## 8. (c) INVESTMENT CONTRACTS

| | 2010 Funeral Plan | 2010 Term Deposit Bond | 2010 Total |
|---|---|---|---|
| Balance at beginning of year | 0.237 | 0.000 | 0.237 |
| Investment policies written | 0.000 | 0.000 | 0.000 |
| Withdrawals | (0.024) | 0.000 | (0.024) |
| Increase in liabilities recognised in comprehensive income | 0.010 | 0.000 | 0.010 |
| Balance at end of year | 0.223 | 0.000 | 0.223 |

| | 2009 Funeral Plan | 2009 Term Deposit Bond | 2009 Total |
|---|---|---|---|
| Balance at beginning of year | 0.246 | 6.513 | 6.759 |
| Investment policies written | 0.000 | 0.000 | 0.000 |
| Withdrawals | (0.014) | (6.692) | (6.706) |
| Increase in liabilities recognised in comprehensive income | 0.005 | 0.179 | 0.184 |
| Balance at end of year | 0.237 | 0.000 | 0.237 |

**$ millions**

| **8. (d) SOURCES OF PROFIT** | **2010** | **2009** |
|---|---|---|
| *The profit for the year has originated as follows:* | | |
| Surplus arising from experience | 5.681 | 3.811 |
| Investment contract surplus | 0.016 | (0.070) |
| Interest on assets in excess of policy liabilities | 0.097 | 0.237 |
| Total | 5.794 | 3.978 |

| **8. (e) SOLVENCY POSITION** | | |
|---|---|---|
| Prudential reserves | 1.767 | 6.447 |
| Total assets less Insurance contract liabilities ceded | 30.288 | 21.417 |
| Prudential margin | 28.521 | 14.970 |
| *Equity retained for solvency purposes* | 14.710 | 9.207 |

The Directors have been provided with the results of a solvency calculation under Professional Standard No 5: Solvency Reserving for Life Insurance Business (PS5.01), issued by the New Zealand Society of Actuaries, which applies for reporting periods commencing after 31 March 2009. Reserves calculated under PS5.01 total $30.0 million (2009: $20.2 million). Under PS5.01, premiums receivable are treated as inadmissible assets. The Directors note that the Company has premiums receivable of $29.7 million (2009: $20.9 million) from related parties with a common shareholding, who are themselves the beneficiaries of the Company's negative equity insurance policies.

The Directors also note that it would be counter-productive from the Group's solvency perspective to realise these inter-company balances in cash, as that would increase external borrowing. The Directors are confident that the Company is able to meet its future commitments on its negative equity insurance contracts based on a conservative view of future client lending rates, future house price inflation, and future mortality and early repayment rates, as well as its commitments to Term Deposit Bond and Funeral Plan policyholders, based on its current level of capital. The Directors consider equity of $14.7 million (2009: $9.2 million) to be non-distributable and is retained for solvency purposes.

**9. NZ GOVERNMENT STOCK**

The Public Trust holds the statutory insurance deposit on behalf of the Company: $0.525 million 6% New Zealand Government stock, maturity 15 November 2011 (2009: same).

**$ millions**

## 10. RELATED PARTIES

The Company works with the Group members to optimise capital allocation and usage of funding facilities. This leads to the flow of funds between the companies as needs dictate. Intercompany balances may be settled net.

### 10. (a) TRANSACTIONS WITH OTHER GROUP ENTITIES

Related party transactions include transactions with other companies in the Group. The Company has entered into a number of transactions with related parties in the normal course of business. A summary of related party transactions during the period and outstanding balances at the statement of financial position date were as follows:

| | 2010 | 2009 |
|---|---|---|
| Premium income - Seniors Money International Limited | 6.515 | 5.785 |
| Premium income - Sentinel Finance Limited | 5.113 | 4.817 |
| Premium income - Australian Seniors Finance Pty Limited | 6.466 | 5.771 |
| Interest income - Australian Seniors Finance Pty Limited | 0.496 | 0.411 |
| Interest income - Seniors Money International Limited | 0.163 | 0.212 |
| Interest income - Sentinel Finance Limited | 0.372 | 0.264 |
| Management fee expense - Seniors Money International Limited | 0.606 | 0.459 |
| Management fee expense - Seniors Money International (Europe) Limited | 0.574 | 0.588 |
| No-neg profit share - Australian Seniors Finance Pty Limited | 0.999 | 0.879 |
| Commission expense - Seniors Money International Limited | 1.954 | 1.736 |
| Commission expense - Sentinel Limited | 1.534 | 1.445 |
| Commission expense - Australian Seniors Finance Pty Limited | 1.940 | 1.731 |
| | | |
| Receivable from Seniors Money International Limited | 8.856 | 5.717 |
| Receivable from Sentinel Finance Limited | 9.785 | 8.417 |
| Receivable from Australian Seniors Finance Pty Limited | 11.094 | 6.723 |
| Owing to Sentinel Limited | 0.000 | 1.091 |

The Company is owned by Sentinel Limited which is owned in turn by Seniors Money International Limited, (the Parent), a company incorporated in New Zealand. Sentinel Limited promotes and sells equity release loans to seniors in New Zealand. The Company insures the 'negative equity' risk provided by Sentinel and Seniors Money International to its customers. Sentinel Finance Limited, a fellow subsidiary, is involved in the ownership and financing of the loans to customers in New Zealand. The reinsurance premium due to Hannover Re is settled net with the reinsurance finance provided to other group members by Hannover Re.

The Parent has subsidiary operations in Australia, Ireland and Spain. The net costs associated with the negative equity insurance for the Ireland and Spanish subsidiaries is carried by the Parent. The receivable due by the Parent to the Company is the accumulated net cost of the risk cover.

Group companies have financed their operations with debt provided by the Commonwealth Bank of Australia (CBA) and also Hannover Re. The Parent, in conjunction with arrangements made with CBA for the extension of banking facilities to the Group until 30 September 2011, has agreed with Hannover Re that no payments are required to Hannover Re before 30 September 2011 unless the related equity release loans are refinanced. Further to the arrangements with CBA and Hannover Re described above, the Company has agreed that payment of the insurance premiums, charged to Group companies for negative equity risk, will be deferred.

## 11. CASH FLOW RECONCILIATION

| | 2010 | 2009 |
|---|---|---|
| **Profit for the year** | 5.794 | 3.978 |
| Unrealised loss on NZ Government stock | 0.013 | (0.031) |
| Unrealised foreign currency loss (gain) | 0.848 | (0.537) |
| Increase in policy liabilities | 4.192 | 6.402 |
| Commission | 5.428 | 4.912 |
| Contribution to Group operating expenses | 2.201 | 1.970 |
| Reassurance premiums | 0.678 | 0.600 |
| Withdrawals | (0.024) | (6.706) |
| Interest from related parties | (1.031) | (0.887) |
| No-neg premium income | (18.094) | (16.373) |
| **Net Cash from Operating Activities** | 0.005 | (6.672) |

## 12. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

Exposure to financial risk arises in the normal course of the Company's business. The Company's risk management strategy and policies are set by the Parent's board of directors and monitored through its audit committee. The main categories of financial risk identified by the Company are credit, insurance and treasury, which are explained below.

*Credit risk*
The Company has credit risk on the reinsurance receivables from Hannover Re when claims arise. Hannover Re has a credit rating of AA- (Standard and Poors). Credit risk also arises on the negative equity premium receivables due from Group members. Any claims payable in future will be first applied against unpaid premiums.

The maximum credit risk held by the Company is the carrying value of the assets reported in the statement of financial position.

*Insurance risk*
Insurance risk is the risk of loss pursuant to an insurance contract. The Group provides a 'no negative equity' guarantee to its customers. This is underwritten by the Company.

The Company manages this risk through establishment of reserves sufficient to meet anticipated claims along with prudential margins to cover unfavourable experience. The Company's exposure to negative equity risk is reduced by reassurance with Hannover Re. Hannover Re has a Standard and Poors long term credit rating of AA- (2009: AA-).

The Company has instituted normal insurance management disciplines to ensure insurance risk is properly managed, including asset/liability matching, solvency and capital adequacy.

The insurance reserves as recorded in the statement of financial position should be greater than the likely incidence of claims, however, the maximum risk held by the Company is the value of the equity release loans written by the Group: $1,261 million (2009: $1,245 million).

*Interest rate risk*
Interest rate risk is the risk of loss arising from exposure to adverse changes in interest rates. Interest on loans to Group companies is set quarterly. Term Deposit Bonds have a 12 month term and progressively mature through the year. The interest rate offered is revised on maturity with the aim of retaining the majority of the funds.

*Liquidity risk*
Liquidity risk is the risk the Company is not able to meet its financial obligations as they arise. This relates principally to policy liabilities and is managed via maturity and withdrawal analysis matched with the assets of the Company.

*Fair value of financial instruments*
The carrying value of the Company's financial instruments approximates their fair values on the basis that they either reprice to market rate, are due to be settled within three months or are carried at fair value.

The Company measures fair values using the following hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Quoted market price from an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e derived from prices).
- Level 3: Valuation techniques using significant unobservable inputs.

The fair value of NZ Government stock is determined by reference to quoted prices (hierarchy level 1). Investment contract liabilities comprise Funeral Plans and Term Deposit Bonds. Funeral Plan liabilities are calculated as the accumulation of an interpolated scale from the premium at commencement to the projected sum insured at the end of year two (level 3). Term deposit bond liabilities are calculated as the accumulated bond balance including interest (level 2).



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**$ millions**

## 12. FINANCIAL RISK MANAGEMENT (continued)

The table below depicts the maturity profile of all financial assets and liabilities categorised by contractual dates. The maturity profile of insurance contracts and reserves is determined by the occupation term of the property used as security for the equity release loans, which in turn is related to how long people will live and remain in their residence. These factors are assessed by the Group's actuaries. Estimates indicate that the insurance cover on new loans have an average life of 11 years while the insurance cover on individual loans could extend beyond 30 years. The maturity profile of insurance contract liabilities ceded and insurance contract reserves is the discounted value.

**Maturity profile:**

| **2010:** | **Up to One Year** | **One to Five Years** | **Over five Years** | **Total** |
|---|---|---|---|---|
| **Asset class** | | | | |
| Cash and cash equivalents | 0.011 | 0.000 | 0.000 | 0.011 |
| NZ Government stock | 0.032 | 0.546 | 0.000 | 0.578 |
| Sentinel Finance Limited | 0.000 | 12.084 | 0.000 | 12.084 |
| Australian Seniors Finance Pty Limited | 0.000 | 14.034 | 0.000 | 14.034 |
| Seniors Money International Limited | 0.000 | 9.919 | 0.000 | 9.919 |
| Insurance contract liabilities ceded | 0.000 | 0.000 | 14.748 | 14.748 |
| | 0.043 | 36.583 | 14.748 | 51.374 |
| **Liability class** | | | | |
| Sentinel Limited | 0.000 | 0.000 | 0.000 | 0.000 |
| Insurance contract reserves | 0.000 | 0.000 | 29.812 | 29.812 |
| Investment contract liabilities | 0.000 | 0.000 | 0.335 | 0.335 |
| | 0.000 | 0.000 | 30.147 | 30.147 |
| **2009:** | | | | |
| **Asset class** | | | | |
| Cash and cash equivalents | 0.006 | 0.000 | 0.000 | 0.006 |
| NZ Government stock | 0.032 | 0.576 | 0.000 | 0.608 |
| Sentinel Finance Limited | 0.000 | 10.395 | 0.000 | 10.395 |
| Australian Seniors Finance Pty Limited | 0.000 | 8.505 | 0.000 | 8.505 |
| Seniors Money International Limited | 0.000 | 6.403 | 0.000 | 6.403 |
| Insurance contract liabilities ceded | 0.000 | 0.000 | 23.223 | 23.223 |
| | 0.038 | 25.879 | 23.223 | 49.140 |
| **Liability class** | | | | |
| Sentinel Limited | 1.091 | 0.000 | 0.000 | 1.091 |
| Insurance contract reserves | 0.000 | 0.000 | 34.105 | 34.105 |
| Investment contract liabilities | 0.000 | 0.000 | 0.335 | 0.335 |
| | 1.091 | 0.000 | 34.440 | 35.531 |

**$ millions**

### 12. FINANCIAL RISK MANAGEMENT (continued)

The following table summarises the Company's exposure to interest rate risk relating to all financial assets and liabilities. Financial assets and liabilities are included at carrying amount, categorised by the earlier of contractual repricing or maturity dates.

**Interest rate repricing:**
**2010:**

| | Up to One Year | One to Five Years | Over five Years | Non-interest bearing | Total |
|---|---|---|---|---|---|
| **Asset class** | | | | | |
| Cash and cash equivalents | 0.000 | 0.000 | 0.000 | 0.011 | 0.011 |
| NZ Government stock | 0.000 | 0.542 | 0.000 | 0.000 | 0.542 |
| Sentinel Finance Limited | 9.785 | 0.000 | 0.000 | 0.000 | 9.785 |
| Australian Seniors Finance Pty Limited | 11.094 | 0.000 | 0.000 | 0.000 | 11.094 |
| Seniors Money International Limited | 8.856 | 0.000 | 0.000 | 0.000 | 8.856 |
| Insurance contract liabilities ceded | 0.000 | 0.000 | 0.000 | 14.748 | 14.748 |
| | 29.735 | 0.542 | 0.000 | 14.759 | 45.036 |
| **Liability class** | | | | | |
| Sentinel Limited | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 |
| Insurance contract reserves | 0.000 | 0.000 | 0.000 | 29.812 | 29.812 |
| Investment contract liabilities | 0.223 | 0.000 | 0.000 | 0.000 | 0.223 |
| | 0.223 | 0.000 | 0.000 | 29.812 | 30.035 |

An increase in interest rates of 1% from the effective rate at year end would increase the Company's comprehensive income and equity by $0.301 million for the succeeding 12 months. A reduction would have the opposite effect.

**2009:**

| | Up to One Year | One to Five Years | Over five Years | Non-interest bearing | Total |
|---|---|---|---|---|---|
| **Asset class** | | | | | |
| Cash and cash equivalents | 0.000 | 0.000 | 0.000 | 0.006 | 0.006 |
| NZ Government stock | 0.000 | 0.554 | 0.000 | 0.000 | 0.554 |
| Sentinel Finance Limited | 8.417 | 0.000 | 0.000 | 0.000 | 8.417 |
| Australian Seniors Finance Pty Limited | 6.723 | 0.000 | 0.000 | 0.000 | 6.723 |
| Seniors Money International Limited | 5.717 | 0.000 | 0.000 | 0.000 | 5.717 |
| Insurance contract liabilities ceded | 0.000 | 0.000 | 0.000 | 23.223 | 23.223 |
| | 20.857 | 0.554 | 0.000 | 23.229 | 44.640 |
| **Liability class** | | | | | |
| Sentinel Limited | 0.000 | 0.000 | 0.000 | 1.091 | 1.091 |
| Insurance contract reserves | 0.000 | 0.000 | 0.000 | 34.105 | 34.105 |
| Investment contract liabilities | 0.237 | 0.000 | 0.000 | 0.000 | 0.237 |
| | 0.237 | 0.000 | 0.000 | 35.196 | 35.433 |

An increase in interest rates of 1% from the effective rate at year end would increase the Company's comprehensive income and equity by $0.212 million for the succeeding 12 months. A reduction would have the opposite effect.

**Capital management**
The Company works with Group members to optimise capital allocation and the usage of funding facilities. The Company's capital includes share capital, retained earnings / (losses) and reserves.

The Company's ultimate parent, Seniors Money International Limited has agreed funding lines with Commonwealth Bank of Australia Limited and reinsurance finance with Hannover Re, and has raised $5.6 million through the issue of Redeemable Preference Shares during the financial year.

### 13. CONTINGENT LIABILITIES

The Company has no contingent liabilities at 31 March 2010 (2009: $nil).

### 14. CAPITAL COMMITMENTS

The Company has no capital commitments at 31 March 2010 (2009: $nil).

# Audit report

## To the shareholder of Sentinel Assurance Company Limited

We have audited the financial statements on pages 5 to 20. The financial statements provide information about the past financial performance of the company and its financial position as at 31 March 2010. This information is stated in accordance with the accounting policies set out on pages 9 to 11.

**Directors' responsibilities**

The Directors are responsible for the preparation of financial statements which give a true and fair view of the financial position of the company as at 31 March 2010 and the results of its operations and cash flows for the year ended on that date.

**Auditors' responsibilities**

It is our responsibility to express an independent opinion on the financial statements presented by the Directors and report our opinion to you.

**Basis of opinion**

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. It also includes assessing:

- the significant estimates and judgements made by the Directors in the preparation of the financial statements;
- whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We conducted our audit in accordance with New Zealand Auditing Standards. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to obtain reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Other than in our capacity as auditors we have no relationship with or interests in the company.

**Unqualified opinion**

We have obtained all the information and explanations we have required.

In our opinion:

- proper accounting records have been kept by the company as far as appears from our examination of those records;

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- the financial statements on pages 5 to 20:
  - comply with New Zealand generally accepted accounting practice;
  - give a true and fair view of the financial position of the company as at 31 March 2010 and the results of its operations and cash flows for the year ended on that date.

Our audit was completed on 2 July 2010 and our unqualified opinion is expressed as at that date.

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Auckland