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# TOWER INSURANCE LIMITED

## FINANCIAL STATEMENTS

## FOR THE YEAR ENDED 30 SEPTEMBER 2010

**TOWER INSURANCE LIMITED**
**FINANCIAL INFORMATION**
**For the year ended 30 September 2010**

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# TOWER INSURANCE LIMITED

# DIRECTORS' REPORT

The Directors of TOWER Insurance Limited present their report and consolidated financial statements of the Company and Group for the year ended 30 September 2010.

During the year the Company and Group undertook its principal activity of providing insurance and insurance related services to its customer base throughout New Zealand, Fiji, Papua New Guinea, Solomon Islands, Cook Islands, Samoa, Tonga and American Samoa.

The consolidated after tax profit attributable to shareholders for the year was $21,937,000 (2009: $16,744,000). Retained profits at the end of the year totalled $64,994,000(2009: $59,557,000). Shareholders' equity at the end of the year totalled $126,999,000 (2008: $119,108,000). The directors consider the state of affairs of the Company and Group to be satisfactory. During the year the directors recommended and paid dividends of $16,500,000 (2009: $23,000,000).

No disclosure has been made in respect of Section 211 (1)(a) and (e) to (j) of the Companies Act 1993 following a unanimous decision by the shareholders in accordance with Section 211 (3) of the Act.

The Company has arranged directors' liability insurance for directors and officers of the Company and its related companies which ensures that generally directors and those officers will incur no monetary losses as a result of actions undertaken by them in the course of their duties. Such insurance arrangements exclude certain actions such as the incurring of penalties or fines that may be imposed for breaches of the law.

The Directors in office at the date of this report are: RA Flannagan and JE Douglas.
The following director left office during the year: EJ O'Sullivan and SJ Boomert.

The Board of Directors of Tower Insurance Limited authorised these financial statements presented on pages 2 to 28 for issue on 23 December 2010.

The Directors wish to thank all staff for their loyalty, application and support during a testing year of change and challenge.

For and on behalf of the Board:

| | | | |
|---|---|---|---|
| Director: | | Director: | |
| Date: | 23 December 2010 | Date: | 23 December 2010 |

**TOWER INSURANCE LIMITED**
**INCOME STATEMENTS**
**For the year ended 30 September 2010**

| | Note | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|---|
| **Revenue** | | | | | |
| Premium revenue from insurance contracts | 21 | 204,845 | 214,619 | 162,819 | 170,388 |
| Less: Outwards reinsurance expense | 21 | (21,651) | (19,497) | (8,468) | (7,167) |
| Net premium revenue | | 183,194 | 195,122 | 154,351 | 163,221 |
| Investment revenue | 3, 21 | 14,062 | 11,193 | 12,855 | 13,930 |
| **Net operating revenue** | | **197,256** | **206,315** | **167,206** | **177,151** |
| **Expenses** | | | | | |
| Claims expense | 21 | (166,452) | (146,621) | (161,471) | (106,872) |
| Less: Reinsurance and other recoveries revenue | 21 | 56,540 | 25,979 | 64,021 | 2,449 |
| **Net claims expense** | | (109,912) | (120,642) | (97,450) | (104,423) |
| Management and sales expenses | 4 | (55,282) | (60,373) | (47,657) | (52,772) |
| **Net claims and operating expenses** | | **(165,194)** | **(181,015)** | **(145,107)** | **(157,195)** |
| **Profit before taxation** | | 32,062 | 25,300 | 22,099 | 19,956 |
| Income tax expense | 5 | 9,613 | 8,008 | 6,355 | 4,907 |
| **Profit for the year** | | **22,449** | **17,292** | **15,744** | **15,049** |
| Profit attributable to minority interests | 19 | (512) | (548) | - | - |
| **Profit for the year attributable to shareholders** | | **21,937** | **16,744** | **15,744** | **15,049** |

The above income statements should be read in conjunction within the accompanying notes.



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**TOWER INSURANCE LIMITED**
**STATEMENTS OF COMPREHENSIVE INCOME**
**For the year ended 30 September 2010**

| | | Group | | Company | |
|---|---|---|---|---|---|
| | | 2010 | 2009 | 2010 | 2009 |
| | Note | NZ$000 | NZ$000 | NZ$000 | NZ$000 |
| **Profit for the year** | | **22,449** | **17,292** | **15,744** | **15,049** |
| **Other comprehensive income:** | | | | | |
| Currency translation differences | | 2,413 | (3,419) | 2,212 | (48) |
| **Other comprehensive income net of taxation** | | **2,413** | **(3,419)** | **2,212** | **(48)** |
| **Total comprehensive income for the year** | | **24,862** | **13,873** | **17,956** | **15,001** |
| **Total comprehensive income attributed to:** | | | | | |
| Shareholders | | 24,312 | 13,861 | 17,956 | 15,001 |
| Minority Interests | | 550 | 12 | - | - |
| | | **24,862** | **13,873** | **17,956** | **15,001** |

The above statements of comprehensive income should be read in conjunction within the accompanying notes.

**TOWER INSURANCE LIMITED**
**BALANCE SHEETS**
**As at 30 September 2010**

| | | Group | | Company | |
|---|---|---|---|---|---|
| | | 2010 | 2009 | 2010 | 2009 |
| | Note | NZ$000 | NZ$000 | NZ$000 | NZ$000 |
| **Assets** | | | | | |
| Cash and cash equivalents | 6 | 67,125 | 31,559 | 54,369 | 17,519 |
| Receivables | 7 | 158,787 | 111,597 | 141,925 | 78,518 |
| Financial assets at fair value through profit or loss | 24 | 184,205 | 210,551 | 154,447 | 184,798 |
| Investment property | 8 | - | - | - | - |
| Deferred acquisition costs | 12 | 13,623 | 12,447 | 11,963 | 11,088 |
| Property, plant and equipment | 13 | 2,787 | 2,893 | 384 | 1,089 |
| Deferred tax asset | 5 | 1,481 | 1,968 | 937 | 1,924 |
| Investment in subsidiaries | 9 | - | - | 4,661 | 4,606 |
| **Total assets** | | **428,008** | **371,015** | **368,686** | **299,542** |
| **Liabilities** | | | | | |
| Payables | 14 | 45,767 | 34,022 | 48,354 | 34,828 |
| Current tax liabilities | | 3,741 | 14,134 | 2,823 | 12,898 |
| Provisions | 15 | 3,188 | 3,834 | 2,822 | 3,442 |
| Insurance liabilities | 16 | 241,105 | 193,670 | 199,235 | 134,738 |
| Deferred tax liability | 5 | 4,284 | 3,555 | 3,849 | 3,568 |
| **Total liabilities** | | **298,085** | **249,215** | **257,083** | **189,474** |
| **Net assets** | | **129,923** | **121,800** | **111,603** | **110,068** |
| **Equity** | | | | | |
| Contributed equity | 17 | 47,900 | 47,900 | 47,900 | 47,900 |
| Retained profits | 18 | 64,994 | 59,557 | 46,606 | 47,362 |
| Reserves | 19 | 14,105 | 11,651 | 17,097 | 14,806 |
| **Total equity attributed to shareholders** | | **126,999** | **119,108** | **111,603** | **110,068** |
| Minority interests | 19 | 2,924 | 2,692 | - | - |
| **Total equity** | | **129,923** | **121,800** | **111,603** | **110,068** |

The financial statements were approved for issue by the Board on 23 December 2010.

Director

Director

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

**TOWER INSURANCE LIMITED**
**STATEMENTS OF CHANGES IN EQUITY**
**For the year ended 30 September 2010**

| **Group** | Attributed to shareholders | | | | | |
|---|---|---|---|---|---|---|
| | **Share capital $000** | **Retained earnings $000** | **Reserves $000** | **Total $000** | **Minority interest $000** | **Total equity $000** |
| **Year ended 30 September 2010** | | | | | | |
| At the beginning of the year | **47,900** | **59,557** | **11,651** | **119,108** | **2,692** | **121,800** |
| **Comprehensive income for the period** | | | | | | |
| Profit for the year | - | 21,937 | - | 21,937 | 512 | 22,449 |
| Currency translation differences | - | - | 2,375 | 2,375 | 38 | 2,413 |
| **Total comprehensive income for the period** | **-** | **21,937** | **2,375** | **24,312** | **550** | **24,862** |
| **Transactions with shareholders** | | | | | | |
| Movement in share based payment reserve | - | - | 79 | 79 | - | 79 |
| Dividends paid | - | (16,500) | - | (16,500) | (318) | (16,818) |
| Other | - | - | - | - | - | - |
| **Total transactions with shareholders** | **-** | **(16,500)** | **79** | **(16,421)** | **(318)** | **(16,739)** |
| **At the end of the year** | **47,900** | **64,994** | **14,105** | **126,999** | **2,924** | **129,923** |

| | Attributed to shareholders | | | | | |
|---|---|---|---|---|---|---|
| | **Share capital $000** | **Retained earnings $000** | **Reserves $000** | **Total $000** | **Minority interest $000** | **Total equity $000** |
| **Year ended 30 September 2009** | | | | | | |
| At the beginning of the year | **47,900** | **66,123** | **14,688** | **128,711** | **3,020** | **131,731** |
| **Comprehensive income for the period** | | | | | | |
| Profit for the year | - | 16,744 | - | 16,744 | 548 | 17,292 |
| Currency translation differences | - | - | (2,883) | (2,883) | (536) | (3,419) |
| **Total comprehensive income for the period** | **-** | **16,744** | **(2,883)** | **13,861** | **12** | **13,873** |
| **Transactions with shareholders** | | | | | | |
| Movement in share based payment reserve | - | 201 | (154) | 47 | - | 47 |
| Dividends paid | - | (23,000) | - | (23,000) | (340) | (23,340) |
| Other | - | (511) | - | (511) | - | (511) |
| **Total transactions with shareholders** | **-** | **(23,310)** | **(154)** | **(23,464)** | **(340)** | **(23,804)** |
| **At the end of the year** | **47,900** | **59,557** | **11,651** | **119,108** | **2,692** | **121,800** |

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

**TOWER INSURANCE LIMITED**
**STATEMENTS OF CHANGES IN EQUITY (CONTINUED)**
**For the year ended 30 September 2010**

**Company**

| | Attributed to shareholders | | | | | |
|---|---|---|---|---|---|---|
| | Share capital $000 | Retained earnings $000 | Reserves $000 | Total $000 | Minority interest $000 | Total equity $000 |
| **Year ended 30 September 2010** | | | | | | |
| At the beginning of the year | 47,900 | 47,362 | 14,806 | 110,068 | - | 110,068 |
| **Comprehensive income for the period** | | | | | | |
| Profit for the year | - | 15,744 | - | 15,744 | - | 15,744 |
| Currency translation differences | - | - | 2,212 | 2,212 | - | 2,212 |
| **Total comprehensive income for the period** | - | 15,744 | 2,212 | 17,956 | - | 17,956 |
| **Transactions with shareholders** | | | | | | |
| Movement in share based payment reserve | - | - | 79 | 79 | - | 79 |
| Dividends paid | - | (16,500) | - | (16,500) | - | (16,500) |
| **Total transactions with shareholders** | - | (16,500) | 79 | (16,421) | - | (16,421) |
| **At the end of the year** | 47,900 | 46,606 | 17,097 | 111,603 | - | 111,603 |

| | Attributed to shareholders | | | | | |
|---|---|---|---|---|---|---|
| | Share capital $000 | Retained earnings $000 | Reserves $000 | Total $000 | Minority interest $000 | Total equity $000 |
| **Year ended 30 September 2009** | | | | | | |
| At the beginning of the year | 47,900 | 55,112 | 15,008 | 118,020 | - | 118,020 |
| **Comprehensive income for the period** | | | | | | |
| Profit for the year | - | 15,049 | - | 15,049 | - | 15,049 |
| Currency translation differences | - | - | (48) | (48) | - | (48) |
| **Total comprehensive income for the period** | - | 15,049 | (48) | 15,001 | - | 15,001 |
| **Transactions with shareholders** | | | | | | |
| Movement in share based payment reserve | - | 201 | (154) | 47 | - | 47 |
| Dividends paid | - | (23,000) | - | (23,000) | - | (23,000) |
| **Total transactions with shareholders** | - | (22,799) | (154) | (22,953) | - | (22,953) |
| **At the end of the year** | 47,900 | 47,362 | 14,806 | 110,068 | - | 110,068 |

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

**TOWER INSURANCE LIMITED**
**NOTES TO THE FINANCIAL STATEMENTS**
**For the year ended 30 September 2010**

TOWER Insurance Limited is a profit-oriented entity incorporated and domiciled in New Zealand. Its registered office and principal place of business is: Level 11, TOWER Centre, 22 Fanshawe Street, Auckland, New Zealand.

## 1. Summary of significant accounting policies

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

### Basis of preparation

This general purpose financial report has been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP), the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS), the New Zealand Companies Act 1993 and the Financial Reporting Act 1993.

The financial statements were authorised for issue by the Board of Directors on 23 December 2010.

The financial statements have been prepared on a fair value basis with any exceptions noted in the accounting policies below.

The Company and Group are qualifying entities within the Framework for Differential Reporting for Entities Applying the New Zealand Equivalents to International Financial Reporting Standards Reporting Regime. The Company and Group qualify on the basis that they are not publicly accountable and that there is no separation between owners and the governing body. The Company and Group have taken advantage of all differential reporting concessions available, except for those available under *NZ IAS 12 Income Taxes.*

During the year the Group undertook its principal activity of providing insurance and insurance related services to its customer base throughout New Zealand, Fiji, Papua New Guinea, Solomon Islands, Cook Islands, Samoa, Tonga and American Samoa.

### Principles of consolidation

These consolidated financial statements incorporate the assets and liabilities of all subsidiaries of TOWER Insurance Limited ("Company" or "parent entity") as at 30 September 2010 and the results of all subsidiaries for the year then ended. TOWER Insurance Limited and its subsidiaries together are referred to in this financial report as the Group or the consolidated entity.

Subsidiaries are all those entities over which the consolidated entity has control, being the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the consolidated entity controls another entity.

The results of any subsidiaries acquired during the year are consolidated from the date on which control is transferred to the consolidated entity and the results of any subsidiaries disposed of during the year are consolidated up to the date control ceases.

The acquisition of controlled entities is accounted for using the purchase method of accounting.

The share of net assets of controlled entities attributable to minority interests is disclosed separately in the balance sheet, income statement and statement of comprehensive income.

Intercompany transactions and balances between Group entities are eliminated on consolidation.

### Specific accounting policies

**(a) Premium revenue**

Premium revenue is recognised in the period in which the premiums are earned during the term of the contract.

The proportion of premiums not earned in the income statement at the reporting date is recognised in the balance sheet as unearned premium liability.

Premiums on unclosed business are brought to account using estimates based on the previous year's actual unclosed business with due allowance made for any changes in the pattern of new business and renewals.



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**1. Summary of significant accounting policies (cont.)**

**(b) Investment revenue**

Investment revenue is recognised as follows:

*(i) Dividends and distributions*

Revenue is recognised on an accruals basis when the right to receive payment is established.

*(ii) Property income*

Property income is recognised on an accruals basis.

*(iii) Interest income*

Interest income is recognised on an effective interest method.

*(iv) Fair value gains and losses*

Fair value gains and losses on financial assets at fair value through profit or loss are recognised through the income statement in the period in which they arise.

**(c) Outwards reinsurance**

Premiums ceded to reinsurers under reinsurance contracts are recorded as an outwards reinsurance expense and are recognised over the period of indemnity of the reinsurance contract. Accordingly, a portion of outwards reinsurance premium is treated at balance date as a prepayment.

**(d) Claims expense**

Claims expenses are recognised when claims are notified with the exception of claims incurred but not reported for which a provision is estimated (discussed in Note 2 (a)).

**(e) Policy acquisition costs**

Acquisition costs incurred in obtaining general insurance contracts are deferred and recognised as assets where they can be reliably measured and where it is probable that they will give rise to premium revenue that will be recognised in subsequent reporting periods.

Deferred acquisition costs are amortised systematically in accordance with the expected pattern of the incidence of risk under the general insurance contracts to which they relate. This pattern of amortisation corresponds to the earning pattern of the corresponding premium revenue.

**(f) Taxation**

*(i) Current tax*

Current tax is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or tax loss for the period. It is calculated using tax rates and tax laws that have been enacted or substantively enacted by reporting date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

*(ii) Deferred tax*

Deferred tax is accounted for using the comprehensive balance sheet liability method in respect of temporary differences arising from differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax base of those items.

Deferred tax assets and liabilities are recognised for temporary differences at the tax rates expected to apply when the assets are recovered or liabilities settled, based on the tax rates enacted or substantively enacted for each jurisdiction. Deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences or unused tax losses can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of the other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

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

**1. Summary of significant accounting policies (cont.)**

**(f) Taxation (cont.)**

*(iii) Tax consolidation*

TOWER Insurance Limited is part of the New Zealand tax consolidated group of which TOWER Limited is the head entity. All members of the tax consolidated group are jointly and severally liable for the tax liabilities of the group.

*(iv) Income tax expense*

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

*(v) GST*

All revenues, expenses and certain assets are recognised net of goods and services taxes (GST) except where the GST is not recoverable. In these circumstances the GST is included in the related asset or expense. Receivables and payables are reported inclusive of GST. The net GST payable to or recoverable from the tax authorities as at balance date is included as a receivable or payable in the balance sheet.

**(g) Foreign currency**

*(i) Functional and presentation currencies*

The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates. The consolidated Group financial statements are presented in New Zealand dollars.

*(ii) Transactions and balances*

In preparing the financial statements of the individual entities transactions denominated in foreign currencies are translated into the reporting currency using the exchange rates in effect at the transaction dates. Monetary items receivable or payable in a foreign currency, including forward exchange contracts, are translated at reporting date at the closing exchange rate.

Translation differences on non-monetary items such as financial assets held at fair value through profit or loss are reported as part of their fair value gain or loss.

Exchange differences arising on the settlement or retranslation of monetary items at year end exchange rates are recognised in the income statement.

*(iii) Consolidation*

For the purpose of preparing consolidated financial statements the assets and liabilities of subsidiaries with a functional currency different to the Company are translated at the closing rate at the balance sheet date. Income and expense items for each subsidiary are translated at a weighted average of exchange rates over the period, as a surrogate for the spot rates at transaction dates. Exchange differences are taken to the Foreign Currency Translation Reserve and recognised in the statement of comprehensive income and the statement of changes in equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and are translated at the closing rate with movements recorded through the Foreign Currency Translation Reserve in the statement of changes in equity.

On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statement.

**(h) Cash and cash equivalents**

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

**1. Summary of significant accounting policies (cont.)**

**(i) Receivables**

Receivables are recognised initially at fair value. Due to the short term nature of these assets the recoverable value, i.e. allowing for doubtful debts, will be the fair value.

**(j) Property, plant and equipment**

Property, plant and equipment is initially recorded at cost including transaction costs and subsequently measured at cost less any subsequent accumulated depreciation and impairment losses.

Depreciation is calculated using the straight line method to allocate their cost or revalued amounts, net of any residual amounts, over their useful lives.

The assets' useful lives are reviewed and adjusted if appropriate at each balance date. An asset's carrying amount is written down immediately to its recoverable amount if it is considered that the carrying amount is greater than its recoverable amount.

| | |
|---|---|
| Computer equipment | 3-5 years |
| Furniture & fittings | 5 years |
| Motor vehicles | 5 years |
| Buildings | 50-100 years |
| Leasehold property improvements | 3-12 years |

**(k) Impairment of non financial assets**

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

**(l) Financial instruments**

The Group classifies its financial assets in the following categories: at fair value through profit or loss and loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

All purchases and sales of financial assets classified as fair value through profit or loss that require delivery within the timeframe established by regulation or market convention ("regular way" purchases and sales) are recognised at trade date, which is the date the Group commits to purchase or sell the assets. Loans and deposits are recognised at settlement date, which is the date that the assets are delivered or received.

*(i) Financial assets at fair value through profit or loss*

Financial assets at fair value through profit or loss comprise of financial assets that are either held for trading or designated on initial recognition at fair value through profit or loss. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term or if so designated by management. Designation by management takes place when it is necessary to eliminate or significantly reduce measurement or recognition inconsistencies or if related financial assets or liabilities are managed and evaluated on a fair value basis.

Financial assets at fair value through profit or loss are stated at fair value, with any resultant gain or loss recognised in the income statement. The net gain or loss recognised in the income statement includes any dividend or interest earned on the financial assets.

*(ii) Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. The Group's loans and receivables comprise trade and other receivables and cash and cash equivalents in the balance sheet. Loans and receivables are measured at amortised cost using the effective interest method less any impairment.

**1. Summary of significant accounting policies (cont.)**

**(m) Impairment of financial assets**
Financial assets, with the exception of those measured at fair value through profit or loss, are assessed for indicators of impairment at each reporting date. Financial assets are impaired when there is objective evidence that the estimated future cash flows of the asset have been impacted as a result of one or more events that occurred after the initial recognition of the financial asset.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the assets' carrying amount and the present value of the estimated future cash flows, discounted at the original effective interest rate.

For all financial assets, other than trade receivables, the carrying amount is reduced by the impairment loss directly. For trade receivables the carrying amount is reduced via an allowance account, against which an uncollectible trade receivable is written off. A trade receivable is deemed to be uncollectible upon notification of insolvency of the debtor or upon receipt of similar evidence that the Group will be unable to collect the amount. Changes in the carrying amount of the allowance account are recognised in the income statement.

A previously recognised impairment loss is reversed when, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment loss was initially recognised.

In respect of financial assets carried at amortised cost, with the exception of trade receivables, the impairment loss is reversed through the income statement to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised. Subsequent recoveries of trade receivables previously written off are credited against the allowance account.

**(n) Investment in subsidiaries**
Investment in subsidiaries are carried at historical cost less any impairment and translated into the reporting currency using the exchange rates in effect at the transaction dates.

**(o) Leased assets**
Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Operating lease payments are recognised as an expense in the periods the services are received over the period of the lease.
Benefits received and receivable for entering into an operating lease are recognised on a straight line basis over the term of the lease.

**(p) Payables**
These amounts represent liabilities for goods and services provided to the Group prior to the end of the financial year which are unsettled.

**(q) Provisions**
Provisions are only recognised when the Group has a present legal or constructive obligation as a result of a past event or decision, and it is more likely than not that an outflow of resources will be required to settle the obligation. Provisions are recognised at the best estimate of future cash flows discounted to present value where the effect is material.

**(r) Employee entitlements**
Provision is made for employee entitlements for services rendered up to the balance date. This includes salaries, wages, bonuses, annual leave and long service leave, but excludes share-based payments. Liabilities arising in respect of employee entitlements expected to be settled within 12 months of the reporting date are measured at their nominal amounts. All other employee entitlements are measured at the present value of the estimated future cash outflows to be made in respect of services provided up to the balance date. In determining the present value of future cash outflows, discount rates used are based on the interest rates attaching to government securities which have terms to maturity approximating the terms of the related liability.

**1. Summary of significant accounting policies (cont.)**

**(s) General insurance liabilities**

Outstanding claims are measured at the central estimate of the present value of expected future payments after allowing for inflation and superimposed inflation and discounted at the risk free rate.

The expected future payments include those in relation to claims reported but not yet paid, claims incurred but not yet reported (IBNR), claims incurred but not enough reported (IBNER) and anticipated claims handling costs. Claims handling costs include costs that can be associated directly with individual claims, such as legal and other professional fees, and costs that can only be indirectly associated with individual claims, such as claims administration costs. In addition a risk margin is added to the claims provision to recognise the inherent uncertainty of the central estimate.

Provision has been made for the estimate of claim recoveries from third parties in respect of general insurance business. Liability adequacy testing is performed in order to recognise any deficiencies in the income statement arising from the carrying amount of the unearned premium liability less any related deferred acquisition costs and intangible assets not meeting the estimated future claims under current insurance conditions. Liability adequacy testing is performed at a portfolio level of contracts that are subject to broadly similar risks and are managed together as a single portfolio.

**(t) Share based payments**

The Group issues share-based compensation packages to senior executives as part of their remuneration packages.

These options are measured at fair value at grant date and expensed over the period during which the employee becomes unconditionally entitled to the options, based on the estimate of shares that will eventually vest. Fair value at grant date is measured using a binomial model, taking into account the specific conditions of the options issued. The determination of fair value excludes the impact of any non-market vesting conditions which are allowed for in assumptions about the number of options that are expected to be exercisable. When an expense is recognised there is an equal and opposite entry made to the share option reserve in equity. When the options are exercised the receipt of the exercise price is transferred to share capital.

Where there is a tax deduction allowable in relation to the share option scheme this is recognised in the income statement, to the extent of the tax credit commensurate to the expense recognised in the income statement, with the balance reported through the share option reserve in equity.

Where terms are changed during the period that increase the cost of the options then this is recognised over the remaining vesting period. Where terms are changed during the period that decrease the cost of the options then there is no change to the expense recognised.

**(u) Investment property**

Investment property, which is property held to earn rentals and capital appreciation, is measured at its fair value at the reporting date. Gains or losses arising from changes in the fair value of investment property are included in profit or loss in the period in which they arise.

**(v) Comparatives**

Where necessary, comparative information has been reclassified to achieve consistency in disclosure with the current year.

**2. Critical accounting judgements and estimates**

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

**(a) Claims liabilities under general insurance contracts**

Provision is made at the end of the year for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported to the Group.

The estimated cost of claims includes direct expenses to be incurred in settling claims gross of the expected value of salvage and other recoveries. The Group takes all reasonable steps to ensure that it has appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

**2. Critical accounting judgements and estimates (cont.)**
**(a) Claims liabilities under general insurance contracts (cont.)**

The estimation of claims incurred but not reported (IBNR) is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Group, where more information about the claim event is generally available. IBNR claims may often not be apparent to the insured until many years after the events giving rise to the claims has happened. In calculating the estimated cost of unpaid claims the Group uses a variety of estimation techniques, generally based on statistical analyses of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which may cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in Group processes which might accelerate or slow down the development and (or) recording of paid or incurred claims, compared with statistics from previous periods;
- changes in the legal environment;
- the effects of inflation;
- changes in the mix of business;
- the impact of large losses; and
- movements in industry benchmarks.

A component of these estimation techniques is usually the estimation of the cost of notified but not paid claims. In estimating the cost of these the Group has regard to the claim circumstances as reported, any information available from loss adjusters and information on the cost of settling claims with similar characteristics in previous periods.

Large claims impacting each relevant business class are generally assessed separately, being measured on a case by case basis or projected separately in order to allow for the possible distortive effect of the development and incidence of these large claims.

Where possible the Group adopts multiple techniques to estimate the required level of provisions. This assists in giving greater understanding of the trends inherent in the data being projected. The projections given by the various methodologies also assist in setting the range of possible outcomes. The most appropriate estimation technique is selected taking into account the characteristics of the business class and the extent of the development of each accident year.

Provisions are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable from reinsurers based on the gross provisions.

Details of specific assumptions used in deriving the outstanding claims liability at year end are detailed in Note 21.

**(b) Assets arising from reinsurance contracts**
Assets arising from reinsurance contracts are also computed using the above methods. In addition, the recoverability of these assets is assessed on a periodic basis to ensure that the balance is reflective of the amounts that will ultimately be received, taking into consideration factors such as counterparty and credit risk. Impairment is recognised where there is objective evidence that the Group may not receive amounts due to it and these amounts can be reliably measured.

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **3. Investment revenue** | | | | |
| **Fixed interest securities** | | | | |
| Interest income | 9,367 | 8,553 | 7,636 | 6,765 |
| Net realised gain | 113 | 211 | 113 | 292 |
| Net unrealised gain / (loss) | 1,704 | (700) | 1,704 | (700) |
| | **11,184** | **8,064** | **9,453** | **6,357** |
| **Equity securities** | | | | |
| Dividend income | 1,328 | 3,191 | 2,055 | 8,014 |
| Net unrealised gain | 1,480 | 1,250 | 1,389 | 1,029 |
| | **2,808** | **4,441** | **3,444** | **9,043** |
| **Property securities** | | | | |
| Property income | 112 | 158 | - | - |
| Net unrealised gain / (loss) | 426 | (1,123) | 426 | (1,123) |
| | **538** | **(965)** | **426** | **(1,123)** |
| **Other investment income** | | | | |
| Other investment (losses) | (468) | (347) | (468) | (347) |
| | **(468)** | **(347)** | **(468)** | **(347)** |
| **Total investment revenue** | **14,062** | **11,193** | **12,855** | **13,930** |

**4. Management and sales expenses**

| | Group 2010 | Group 2009 | Company 2010 | Company 2009 |
|---|---|---|---|---|
| **Included in total management and sales expenses are the following:** | | | | |
| Amortisation of deferred acquisition costs | 12,447 | 13,890 | 11,088 | 12,192 |
| Change in provision for doubtful debts | 19 | (202) | (87) | (61) |
| Depreciation: | | | | |
| Office equipment and furniture | 143 | 893 | 11 | 695 |
| Motor vehicles | 165 | 111 | 92 | 52 |
| Computer equipment | 36 | 209 | 5 | 156 |
| Donations | 1 | - | - | - |
| Fees paid to auditors | | | | |
| Audit of financial statements | - | 390 | - | 254 |
| Employee benefits expense | 22,424 | 27,356 | 19,728 | 24,265 |

TOWER New Zealand Limited paid all fees for the audit services of TOWER Insurance Limited for the year ended 30 September 2010.

**5. Taxation**

**(a) Current tax expense**

| | Group 2010 | Group 2009 | Company 2010 | Company 2009 |
|---|---|---|---|---|
| **Analysis of taxation expense - current and deferred** | | | | |
| Current taxation | 9,346 | 8,865 | 5,581 | 5,957 |
| Deferred taxation | 1,216 | (857) | 1,268 | (1,050) |
| (Over) / under provided in prior years | (949) | - | (494) | - |
| **Income tax expense for the year** | **9,613** | **8,008** | **6,355** | **4,907** |
| The tax expense recognised can be reconciled to the accounting profit as follows: | | | | |
| **Profit before taxation** | 32,062 | 25,300 | 22,099 | 19,956 |
| Income tax at the current rate of 30% (2009: 30%) | 9,619 | 7,590 | 6,630 | 5,987 |
| Taxation effect of non-deductible expenses / non-assessable revenue: | | | | |
| Prior period adjustment | (949) | - | (494) | - |
| Change in tax rates | - | - | - | - |
| Income not assessable for tax | (64) | - | - | (1,072) |
| Other tax differences | 391 | - | 144 | - |
| Taxable/(non-taxable) income from PIEs | (42) | 370 | (42) | 370 |
| Future witholding tax on dividends | 337 | (171) | - | - |
| Release of witholding tax provision | - | - | - | (264) |
| Non deductible expenditure | 321 | 219 | 117 | (114) |
| **Taxation expense** | **9,613** | **8,008** | **6,355** | **4,907** |

In May 2010 legislation was passed to reduce the company tax rate from 30% to 28%. This is effective for the Group from 1 October 2011. There is no financial effect of the change in tax rate to the Company or the Group.

**5. Taxation (Cont.)**
**(b) Deferred tax assets and liabilities**

**Group**

| | Opening balance at 1 October | Charged/ (credited) to income statement | Credited to equity | Transfer to related party | Closing balance at 30 September |
|---|---|---|---|---|---|
| **2010** | NZ$000 | NZ$000 | NZ$000 | NZ$000 | NZ$000 |
| **Movements in deferred tax assets** | | | | | |
| Provisions and accruals | 1,262 | 219 | - | - | 1,481 |
| Unrealised losses | - | - | - | - | - |
| Tax losses | 249 | (249) | - | - | - |
| Other | 457 | (457) | - | - | - |
| **Total deferred tax assets** | 1,968 | (487) | - | - | 1,481 |
| **Movements in deferred tax liabilities** | | | | | |
| Deferred costs | (3,190) | (518) | - | - | (3,708) |
| Fair value | - | (297) | - | - | (297) |
| Other | (365) | 86 | - | - | (279) |
| **Total deferred tax liabilities** | (3,555) | (729) | - | - | (4,284) |
| **Net deferred tax** | (1,587) | (1,216) | - | - | (2,803) |
| **2009** | | | | | |
| **Movements in deferred tax assets** | | | | | |
| Provisions and accruals | 689 | 573 | - | - | 1,262 |
| Unrealised losses | 98 | (98) | - | - | - |
| Tax losses | - | 249 | - | - | 249 |
| Other | 367 | 90 | - | - | 457 |
| **Total deferred tax assets** | 1,154 | 814 | - | - | 1,968 |
| **Movements in deferred tax liabilities** | | | | | |
| Deferred costs | (3,598) | 408 | - | - | (3,190) |
| Fair value | - | - | - | - | - |
| Other | - | (365) | - | - | (365) |
| **Total deferred tax liabilities** | (3,598) | 43 | - | - | (3,555) |
| **Net deferred tax** | (2,444) | 857 | - | - | (1,587) |

**Company**

| | Opening balance at 1 October | Charged/ (credited) to income statement | Credited to equity | Transfer to related party | Closing balance at 30 September |
|---|---|---|---|---|---|
| **2010** | NZ$000 | NZ$000 | NZ$000 | NZ$000 | NZ$000 |
| **Movements in deferred tax assets** | | | | | |
| Provisions and accruals | 1,492 | (558) | - | - | 934 |
| Other | 432 | (429) | - | - | 3 |
| **Total deferred tax assets** | 1,924 | (987) | - | - | 937 |
| **Movements in deferred tax liabilities** | | | | | |
| Deferred costs | (3,190) | (345) | - | - | (3,535) |
| Deferred PIE allocated income | (365) | 51 | - | - | (314) |
| Withholding tax on future dividends | - | - | - | - | - |
| Other | (13) | 13 | - | - | - |
| **Total deferred tax liabilities** | (3,568) | (281) | - | - | (3,849) |
| **Net deferred tax** | (1,644) | (1,268) | - | - | (2,912) |
| **2009** | | | | | |
| **Movements in deferred tax assets** | | | | | |
| Provisions and accruals | 1,603 | (111) | - | - | 1,492 |
| Other | 342 | 90 | - | - | 432 |
| **Total deferred tax assets** | 1,945 | (21) | - | - | 1,924 |
| **Movements in deferred tax liabilities** | | | | | |
| Deferred costs | (3,599) | 409 | - | - | (3,190) |
| Deferred PIE allocated income | - | (365) | - | - | (365) |
| Withholding tax on future dividends | (865) | 865 | - | - | - |
| Other | (175) | 162 | - | - | (13) |
| **Total deferred tax liabilities** | (4,639) | 1,071 | - | - | (3,568) |
| **Net deferred tax** | (2,694) | 1,050 | - | - | (1,644) |



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**5. Taxation (Cont.)**
**(b) Deferred tax assets and liabilities (Cont.)**

| | Group | | Company | |
|---|---|---|---|---|
| | 2010 NZ$000 | 2009 NZ$000 | 2010 NZ$000 | 2009 NZ$000 |
| **Net deferred tax** | | | | |
| Expected to crystallise in the next 12 months | (2,803) | (2,044) | (2,909) | (2,076) |
| Not expected to crystallise in the next 12 months | - | 457 | (3) | 432 |
| | (2,803) | (1,587) | (2,912) | (1,644) |

**6. Cash and cash equivalents**

| | | | | |
|---|---|---|---|---|
| Cash at bank and in hand | 5,724 | 3,621 | 1,915 | 1,197 |
| Deposits at call | 61,401 | 27,938 | 52,454 | 16,322 |
| **Total cash and cash equivalents** | 67,125 | 31,559 | 54,369 | 17,519 |

**7. Receivables**

| | | | | |
|---|---|---|---|---|
| Other debtors, prepayments and accrued income | 474 | 643 | 622 | 808 |
| Outstanding premiums and trade receivables | 82,289 | 78,871 | 71,071 | 70,128 |
| Reinsurance recoveries receivable on outstanding claims and other recoveries | 75,446 | 31,728 | 65,476 | 2,644 |
| *Related party receivables* | 578 | 355 | 4,756 | 4,938 |
| **Total receivables** | 158,787 | 111,597 | 141,925 | 78,518 |

Outstanding premiums and trade receivables above are presented net of allowance for credit losses and impairment. Movement in the allowance for credit losses and impairment during the reporting period was as follows:

| | | | | |
|---|---|---|---|---|
| Outstanding premiums and trade receivables | 83,596 | 80,159 | 71,459 | 70,603 |
| Allowance for doubtful debts | (1,307) | (1,288) | (388) | (475) |
| | 82,289 | 78,871 | 71,071 | 70,128 |
| | | | | |
| Balance at 1 October | (1,288) | (1,490) | (475) | (536) |
| Impairment loss recognised during the year | (19) | 202 | 87 | 61 |
| Balance at 30 September | (1,307) | (1,288) | (388) | (475) |

The allowance for credit losses and impairment in relation to trade receivables is provided for based on estimated recoverable amounts determined by reference to current customer circumstances and past default experience. In determining the recoverability of a trade receivable the Group considers *any change in the credit quality of the trade receivable from the date the credit was initially granted up* to the reporting date. The Group has provided fully for receivables over 120 days past due. Trade receivables between 60 days and 120 past due are provided for based on estimated irrecoverable amounts determined by reference to past due default experience.

**8. Investment property**

| | | | | |
|---|---|---|---|---|
| Opening balance at 1 October | - | 2,450 | - | - |
| Reclassified as property, plant and equipment | - | (2,538) | - | - |
| Other adjustments | - | 88 | - | - |
| **Closing balance at 30 September** | - | - | - | - |

Investment property was reclassified as property, plant and equipment on 1 April 2009.

**9. Investment in subsidiaries**

| | | | | |
|---|---|---|---|---|
| Investments in controlled entities | - | - | 4,661 | 4,606 |

**10. Controlled entities**
The major trading subsidiaries incorporated into the consolidated financial statements, all of which have a common balance date with the Company and undertake insurance activities are as follows:

| | Domicile | Ownership |
|---|---|---|
| TOWER Insurance (Cook Islands) Limited | Cook Islands | 100% |
| TOWER Insurance (Fiji) Limited | Fiji | 100% |
| TOWER Insurance (PNG) Limited | Papua New Guinea | 100% |
| National Pacific Insurance Limited | Samoa | 70% |

The Company has accumulated retained earnings held by offshore susidiaries totalling $14,360,663 (2009: $9,607,773) which if paid to the parent by way of dividend would incur withholding taxes of up to 17%.

## 11. Related parties

All transactions between companies within the TOWER group were conducted at arms length. Trade amounts owing between related parties are payable under normal commercial terms. No related party debts have been written off or forgiven during the year.
Related party receivable and payable balances of TOWER Insurance Limited at the reporting date were as follows:

| Related party | 2010 NZ$000 | 2009 NZ$000 | Nature of relationship | Type of transactions |
|---|---|---|---|---|
| TOWER Limited | 113 | - | Ultimate parent | Tax gain |
| TOWER Health & Life Limited | 464 | 340 | Fellow subsidiary | Commission |
| TOWER Managed Funds Limited | - | 15 | Fellow subsidiary | Operating expenses |
| TOWER Financial Services Group Limited | (7,678) | - | Parent of TOWER Insurance Limited | Tax losses |
| TOWER New Zealand Limited | (4,112) | (1,158) | Fellow subsidiary | Recoveries, loan and tax losses |
| TOWER Life (N.Z.) Limited | (2,638) | - | Fellow subsidiary | Tax losses |
| TOWER Capital Limited | (409) | - | Fellow subsidiary | Tax losses |
| TOWER Asset Management Limited | (96) | (105) | Fellow subsidiary | Investment management fees |
| TOWER Medical Insurance Limited | (20) | - | Fellow subsidiary | Tax losses |
| TOWER Insurance (Fiji) Limited | (123) | 311 | Subsidiary | Management, IT services & reinsurance settlements |
| TOWER Insurance (PNG) Limited | 954 | 1,130 | Subsidiary | Management, IT services & reinsurance settlements |
| TOWER Insurance (Cook Islands) Limited | (1,165) | 190 | Subsidiary | Management, IT services & reinsurance settlements |

TOWER Insurance Limited enters into transactions with its related parties in the normal course of business. Transactions during the year included partial settlement of intercompany balances and intercompany dividends as shown below:

| | | | | |
|---|---|---|---|---|
| TOWER Limited | 113 | - | Ultimate parent | Tax gain |
| TOWER Financial Services Group Limited | (7,678) | - | Parent of TOWER Insurance Limited | Tax losses |
| TOWER Financial Services Group Limited | (16,500) | (23,000) | Parent of TOWER Insurance Limited | Dividend |
| TOWER Health & Life Limited | 210 | 470 | Fellow subsidiary | Commission |
| TOWER Health & Life Limited | 471 | - | Fellow subsidiary | Tax gain |
| TOWER Medical Insurance Limited | 106 | - | Fellow subsidiary | Commission |
| TOWER Medical Insurance Limited | (20) | - | Fellow subsidiary | Tax losses |
| TOWER Asset Management Limited | (383) | (376) | Fellow subsidiary | Investment management fees |
| TOWER Managed Funds Limited | - | 387 | Fellow subsidiary | Operating expenses |
| TOWER New Zealand Limited | (3,717) | - | Fellow subsidiary | Tax losses |
| TOWER New Zealand Limited | (19,008) | - | Fellow subsidiary | Cost recoveries |
| TOWER New Zealand Limited | 1 | - | Fellow subsidiary | Transfer of intangible assets |
| TOWER New Zealand Limited | 794 | - | Fellow subsidiary | Transfer of fixed assets |
| TOWER New Zealand Limited | 763 | (4,170) | Fellow subsidiary | Loan |
| TOWER Life (N.Z.) Limited | (2,638) | - | Fellow subsidiary | Tax losses |
| TOWER Capital Limited | (409) | - | Fellow subsidiary | Tax losses |
| TOWER Insurance (Cook Islands) Limited | 671 | 595 | Subsidiary | Management, IT services & reinsurance settlements |
| TOWER Insurance (Fiji) Limited | 1,838 | 1,526 | Subsidiary | Management, IT services & reinsurance settlements |
| TOWER Insurance (PNG) Limited | 2,280 | 1,908 | Subsidiary | Management, IT services & reinsurance settlements |
| National Pacific Insurance Limited | 380 | 378 | Subsidiary | Management, IT services & reinsurance settlements |



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**TOWER INSURANCE LIMITED**
**NOTES TO THE FINANCIAL STATEMENTS**
**For the year ended 30 September 2010**

| | Group | | Company | |
|---|---|---|---|---|
| | 2010 NZ$000 | 2009 NZ$000 | 2010 NZ$000 | 2009 NZ$000 |
| **12. Deferred acquisition costs** | | | | |
| Opening balance at 1 October | 12,447 | 13,890 | 11,088 | 12,192 |
| Acquisition costs deferred during the period | 13,623 | 12,447 | 11,963 | 11,088 |
| Current period amortisation | (12,447) | (13,890) | (11,088) | (12,192) |
| **Closing balance at 30 September** | 13,623 | 12,447 | 11,963 | 11,088 |
| **13. Property, plant and equipment** | | | | |
| Computer equipment cost | 509 | 2,145 | 17 | 1,649 |
| Accumulated depreciation | (472) | (1,958) | (9) | (1,501) |
| **Net book value at 30 September** | 37 | 187 | 8 | 148 |
| Office equipment cost | 1,485 | 4,532 | 434 | 3,988 |
| Accumulated depreciation | (1,138) | (4,127) | (411) | (3,293) |
| **Net book value at 30 September** | 347 | 405 | 23 | 695 |
| Motor vehicles cost | 1,121 | 940 | 496 | 340 |
| Accumulated depreciation | (629) | (534) | (143) | (94) |
| **Net book value at 30 September** | 492 | 406 | 353 | 246 |
| Land and buildings | 1,911 | 1,895 | - | - |
| Accumulated depreciation | - | - | - | - |
| **Net book value at 30 September** | 1,911 | 1,895 | - | - |
| **Total net book value at 30 September** | 2,787 | 2,893 | 384 | 1,089 |

A large proportion of computer and office equipment was transferred to TOWER New Zealand Limited on 1 October 2009. The Company has been charged a management fee in return by TOWER New Zealand Limited for the use of these assets.

| | Group 2010 | Group 2009 | Company 2010 | Company 2009 |
|---|---|---|---|---|
| **14. Payables** | | | | |
| Trade payables | 19,476 | 20,527 | 17,579 | 19,119 |
| Other payables | 5,582 | 4,884 | 4,850 | 4,353 |
| Reinsurance payables | 5,756 | 7,348 | 6,460 | 7,141 |
| Related party payables | 14,953 | 1,263 | 19,465 | 4,215 |
| **Total payables** | 45,767 | 34,022 | 48,354 | 34,828 |
| **15. Provisions** | | | | |
| Employee benefits | 3,188 | 3,834 | 2,822 | 3,442 |
| **Total provisions** | 3,188 | 3,834 | 2,822 | 3,442 |
| **16. Insurance liabilities** | | | | |
| Unearned premiums | 99,604 | 96,914 | 81,421 | 80,702 |
| Outstanding claims | 141,501 | 96,756 | 117,814 | 54,036 |
| **Total insurance liabilities** | 241,105 | 193,670 | 199,235 | 134,738 |
| **17. Contributed equity** | | | | |
| **Share capital** | | | | |
| Fully paid ordinary shares | 47,900 | 47,900 | 47,900 | 47,900 |
| | 47,900 | 47,900 | 47,900 | 47,900 |
| **Fully paid ordinary shares** | | | | |
| Opening balance at 1 October | 47,900 | 47,900 | 47,900 | 47,900 |
| **Closing balance at 30 September** | 47,900 | 47,900 | 47,900 | 47,900 |
| **Represented by:** | **Number of shares** | | **Number of shares** | |
| Ordinary shares authorised, issued and fully paid (no par value) | 49,017,980 | 49,017,980 | 49,017,980 | 49,017,980 |
| **Fully paid ordinary shares** | | | | |
| Opening balance at 1 October | 49,017,980 | 49,017,980 | 49,017,980 | 49,017,980 |
| **Closing balance at 30 September** | 49,017,980 | 49,017,980 | 49,017,980 | 49,017,980 |

All shares rank equally with one vote attached to each share.

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **18. Retained profits** | | | | |
| **Retained profits** | | | | |
| Opening balance at 1 October | 59,557 | 66,123 | 47,362 | 55,112 |
| Net profit for the year attributable to shareholders | 21,937 | 16,744 | 15,744 | 15,049 |
| Dividend paid | (16,500) | (23,000) | (16,500) | (23,000) |
| Transfer from share based payment reserve | - | 201 | - | 201 |
| Other | - | (511) | - | - |
| **Closing balance at 30 September** | **64,994** | **59,557** | **46,606** | **47,362** |

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **19. Reserves** | | | | |
| **Foreign currency translation reserve** | | | | |
| Opening balance at 1 October | (396) | 2,487 | 3,090 | 3,138 |
| Currency translation differences arising during the year | 2,375 | (2,883) | 2,212 | (48) |
| **Closing balance at 30 September** | **1,979** | **(396)** | **5,302** | **3,090** |

Exchange differences arising on translation of foreign controlled entities are taken to the foreign currency translation reserve as described in note 1(g). The reserve is recognised in profit and loss when the net investment is disposed of.

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **Share based payments reserve** | | | | |
| Opening balance at 1 October | 57 | 211 | 57 | 211 |
| Transfer to retained profits | - | (201) | - | (201) |
| Option expense | 79 | 47 | 79 | 47 |
| Closing balance at 30 September | **136** | **57** | **136** | **57** |

The share based payments reserve recognises share options in the parent company, TOWER Limited, held by senior executives employed by TOWER Insurance Limited. Full details relating to the share option schemes are included in the financial statements of TOWER Limited for the year ended 30 September 2010.

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **Capital reserve** | | | | |
| Opening balance at 1 October | 11,990 | 11,990 | 11,659 | 11,659 |
| Closing balance at 30 September | **11,990** | **11,990** | **11,659** | **11,659** |
| | | | | |
| **Total reserves** | **14,105** | **11,651** | **17,097** | **14,806** |
| | | | | |
| **Minority interest** | | | | |
| Opening balance at 1 October | 2,692 | 3,020 | - | - |
| Share in current year profit of subsidiary | 512 | 548 | - | - |
| Dividends paid by subsidiary to minority shareholders | (318) | (340) | - | - |
| Share of foreign currency translation reserve movements | 38 | (536) | - | - |
| Closing balance at 30 September | **2,924** | **2,692** | - | - |

**20. Distributions to shareholders**
A dividend of $16,500,000 was paid during the year ended 30 September 2010 (30 September 2009: $23,000,000).

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **21. Insurance business** | | | | |
| **(a) Analysis of insurance operating result** | | | | |
| Premium revenue | 204,845 | 214,619 | 162,819 | 170,388 |
| Outward reinsurance expense | (21,651) | (19,497) | (8,468) | (7,167) |
| **Net premium income** | 183,194 | 195,122 | 154,351 | 163,221 |
| Claims expense | 166,452 | 146,621 | 161,471 | 106,872 |
| Reinsurance recoveries | (56,540) | (25,979) | (64,021) | (2,449) |
| **Net claims incurred** | 109,912 | 120,642 | 97,450 | 104,423 |
| Acquisition costs | 26,556 | 30,920 | 23,075 | 30,920 |
| Other underwriting expenses | 28,726 | 29,453 | 24,582 | 21,852 |
| **Underwriting result** | 18,000 | 14,107 | 9,244 | 6,026 |
| Net investment income from general insurance business: | | | | |
| Investment revenue | 14,530 | 11,540 | 13,323 | 14,277 |
| Investment expenses | (468) | (347) | (468) | (347) |
| **Net investment income** | 14,062 | 11,193 | 12,855 | 13,930 |
| **Operating surplus before income tax** | 32,062 | 25,300 | 22,099 | 19,956 |

**(b) Net claims incurred**

| Group | 2010 Risks borne in current year NZ$000 | 2010 Risks borne in prior years NZ$000 | 2010 Total NZ$000 | 2009 Risks borne in current year NZ$000 | 2009 Risks borne in prior years NZ$000 | 2009 Total NZ$000 |
|---|---|---|---|---|---|---|
| **Gross claims expense** | | | | | | |
| Direct claims - undiscounted | 175,552 | (10,874) | 164,678 | 144,536 | 120 | 144,656 |
| Discount | (3) | 1,777 | 1,774 | 46 | 1,919 | 1,965 |
| **Gross claims expense** | 175,549 | (9,097) | 166,452 | 144,582 | 2,039 | 146,621 |
| **Reinsurance and other recoveries** | | | | | | |
| Reinsurance and other recoveries revenue - undiscounted | 64,830 | (8,047) | 56,783 | 23,349 | 2,863 | 26,212 |
| Discount | 27 | (270) | (243) | (26) | (207) | (233) |
| **Reinsurance and other recoveries** | 64,857 | (8,317) | 56,540 | 23,323 | 2,656 | 25,979 |
| **Net claims incurred** | 110,692 | (780) | 109,912 | 121,259 | (617) | 120,642 |

| Company | 2010 Risks borne in current year NZ$000 | 2010 Risks borne in prior years NZ$000 | 2010 Total NZ$000 | 2009 Risks borne in current year NZ$000 | 2009 Risks borne in prior years NZ$000 | 2009 Total NZ$000 |
|---|---|---|---|---|---|---|
| **Gross claims expense** | | | | | | |
| Direct claims - undiscounted | 160,250 | (545) | 159,705 | 105,381 | (400) | 104,981 |
| Discount | 1 | 1,765 | 1,766 | - | 1,891 | 1,891 |
| **Gross claims expense** | 160,251 | 1,220 | 161,471 | 105,381 | 1,491 | 106,872 |
| **Reinsurance and other recoveries** | | | | | | |
| Reinsurance and other recoveries revenue - undiscounted | 63,460 | 905 | 64,365 | 931 | 1,653 | 2,584 |
| Discount | - | (344) | (344) | - | (135) | (135) |
| **Reinsurance and other recoveries** | 63,460 | 561 | 64,021 | 931 | 1,518 | 2,449 |
| **Net claims incurred** | 96,791 | 659 | 97,450 | 104,450 | (27) | 104,423 |

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

**21. Insurance business (Cont.)**

**(c) Net outstanding claims**

**i) Net outstanding claims liability**

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| Central estimate of expected present value of future payments for claims incurred | 69,138 | 72,534 | 56,599 | 60,005 |
| Risk margin | 5,200 | 4,907 | 4,659 | 4,567 |
| Claims handling costs | 5,119 | 4,668 | 4,348 | 3,934 |
| | 79,457 | 82,109 | 65,606 | 68,506 |
| Discount | (13,402) | (17,081) | (13,268) | (17,114) |
| **Net outstanding claims liability** | **66,055** | **65,028** | **52,338** | **51,392** |

**ii) Reconciliation of movements in net discounted outstanding claims liability**

| **Group** | 2010 Gross NZ$000 | 2010 Reinsurance NZ$000 | 2010 Net NZ$000 | 2009 Gross NZ$000 | 2009 Reinsurance NZ$000 | 2009 Net NZ$000 |
|---|---|---|---|---|---|---|
| **Balance brought forward** | 96,756 | (31,728) | 65,028 | 77,398 | (6,624) | 70,774 |
| Effect of change in foreign exchange rates | (2,480) | 576 | (1,904) | (637) | (1,935) | (2,572) |
| Effect of changes in assumptions | 3,498 | (690) | 2,808 | 676 | 77 | 753 |
| Incurred claims for year | 166,452 | (56,541) | 109,911 | 146,621 | (25,979) | 120,642 |
| Claim payments during year | 122,725 | (12,937) | 109,788 | 127,302 | (2,733) | 124,569 |
| **Balance carried forward** | **141,501** | **(75,446)** | **66,055** | **96,756** | **(31,728)** | **65,028** |

**Reconciliation of net undiscounted claims to liability for net outstanding claims**

| | 2010 Gross | 2010 Reinsurance | 2010 Net | 2009 Gross | 2009 Reinsurance | 2009 Net |
|---|---|---|---|---|---|---|
| Long tail outstanding claims undiscounted | 29,622 | (2,769) | 26,853 | 36,682 | (3,556) | 33,126 |
| Discount | (14,382) | 981 | (13,401) | (16,157) | 738 | (15,419) |
| Long tail outstanding claims | 15,240 | (1,788) | 13,452 | 20,525 | (2,818) | 17,707 |
| Short tail outstanding claims | | | 52,603 | | | 47,321 |
| **Total net outstanding claims as per balance sheet** | | | **66,055** | | | **65,028** |

| **Company** | 2010 Gross NZ$000 | 2010 Reinsurance NZ$000 | 2010 Net NZ$000 | 2009 Gross NZ$000 | 2009 Reinsurance NZ$000 | 2009 Net NZ$000 |
|---|---|---|---|---|---|---|
| **Balance brought forward** | 54,036 | (2,644) | 51,392 | 55,778 | (2,076) | 53,702 |
| Effect of change in foreign exchange rates | (3,154) | 549 | (2,605) | (620) | (360) | (980) |
| Effect of changes in assumptions | 3,498 | (690) | 2,808 | 556 | 63 | 619 |
| Incurred claims for year | 161,471 | (64,021) | 97,450 | 106,819 | (2,449) | 104,370 |
| Claim payments during year | 98,037 | (1,330) | 96,707 | 108,497 | (2,178) | 106,319 |
| **Balance carried forward** | **117,814** | **(65,476)** | **52,338** | **54,036** | **(2,644)** | **51,392** |

**Reconciliation of net undiscounted claims to liability for net outstanding claims**

| | 2010 Gross | 2010 Reinsurance | 2010 Net | 2009 Gross | 2009 Reinsurance | 2009 Net |
|---|---|---|---|---|---|---|
| Long tail outstanding claims undiscounted | 25,264 | (1,976) | 23,288 | 30,935 | (2,171) | 28,764 |
| Discount | (14,243) | 975 | (13,268) | (16,009) | 630 | (15,379) |
| Long tail outstanding claims | 11,021 | (1,001) | 10,020 | 14,926 | (1,541) | 13,385 |
| Short tail outstanding claims | | | 42,318 | | | 38,007 |
| **Total net outstanding claims as per balance sheet** | | | **52,338** | | | **51,392** |

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| **iii) Long tail outstanding claims is made up of exposures from:** | | | | |
| Pacific Islands | 3,547 | 4,438 | 115 | 116 |
| Australia | 5,706 | 9,240 | 5,706 | 9,240 |
| Inwards reinsurance business (excl Australia) | 4,199 | 4,029 | 4,199 | 4,029 |
| **Net discounted long tail outstanding claims** | **13,452** | **17,707** | **10,020** | **13,385** |

**21. Insurance business (Cont.)**

**(d) Assumptions adopted in calculation of insurance provisions**
The claims provisions have been assessed having regard to external actuarial assessments.
The actuary used was P. Davies, B.Bus.Sc, FNZSA, FIA, AIA, AIAA.
The actuarial assessments are in accordance with the standards of the Society of Actuaries of New Zealand. The Actuaries were satisfied as to the nature, sufficiency and accuracy of the data used to determine the outstanding claims.

The following assumptions have been made in determining net outstanding claims liabilities:

| | 2010 | 2009 |
|---|---|---|
| - Inflation rates varied from | 1.5% to 8% | 1.5% to 8% |
| - Discount rates varied from | 4% to 6.5% | 4% to 9% |
| - Claims handling expense ratio | 3.6% to 11.1% | 3.3% to 13% |
| - Risk margin | 15% to 20% | 15% to 20% |

**Inflation rate**
Insurance costs are subject to inflationary pressures. Inflation assumptions for all general insurance classes of business are based on current economic indicators.

For motor, property and health classes, for example, claim costs are related to the inflationary pressures of the materials and goods insured as well as labour costs to effect repairs. These costs are expected to increase at a level between appropriate Consumer Price Index (CPI) indices and wage inflation.

**Risk margin**
The overall risk margin is determined allowing for diversification between classes of business and the relative uncertainty of the outstanding claims estimate for each class.

The assumptions regarding uncertainty for each class were applied to the net central estimates and the results were aggregated allowing for diversification in order to arrive at an overall provision which is intended to have a 75% probability of sufficiency.

***Applicable to all long tail and short tail claims***
The weighted average expected term to settlement of outstanding claims based on historical trends is:

| | 2010 | 2009 |
|---|---|---|
| - Short tail claims | within 1 year | within 1 year |
| - Long tail claims in the Pacific Islands | 1.51 to 2.48 years | 1.06 to 2.51 years |
| - Long tail claims in Australia | 8.1 to 8.4 years | 6.9 to 7.9 years |
| - Inwards reinsurance treaties | in excess of 10 years | in excess of 10 years |

**Discount rate**
General insurance outstanding claims liabilities are discounted at a rate equivalent to that inherent in a portfolio of riskless fixed interest securities with coupon and redemption cash flows exactly matching the projected inflation claim cash flows.

General insurance outstanding claims liabilities are discounted to present value using a risk free rate based on ten year government bond rate in New Zealand.

**Claims handling expense**
The estimate of outstanding claims liabilities incorporates an allowance for the future cost of administrating the claims. This allowance is determined after analysing historical claim related expenses incurred by the classes of business.

***Inward reinsurance business***
The Company participated in some inward treaty and pooling arrangements all of which ceased prior to 1985. These claims continue to be run off. Some arrangements have commuted with cedants and other commutations are being sought. Some pooling arrangements are progressing through solvent schemes of arrangement. Information from the cedants has been regular and reserves for these claims have been conservatively assessed and reported by the cedants. Because of the nature of inward treaty and pooling arrangements, it is difficult to have these liabilities reliably actuarially assessed. Accordingly the company has taken a conservative appoarch in assessing these liabilities and has based its reserves on the latest available information from cedants plus IBNR provisions based on recent trends. With the exception of the Australian treaties, the inwards reinsurance business has not been actuarially assessed and does not form part of the sensitivity analysis. All other long tail business is included and has been actuarially assessed.

**21. Insurance business (Cont.)**

**Sensitivity analysis**
Sensitivity analysis is conducted to quantify the exposure to risk of change in the key underlying variables. The movement in any key variable will impact the performance and equity of the Group. The tables below describe how the change in each assumption will affect the insurance liabilities and show an analysis of the sensitivity of the profit or loss and equity net of reinsurance to changes in assumptions.

| | | 2010 | | 2009 | |
|---|---|---|---|---|---|
| Variable | Movement | Group Impact $'000 | Parent Impact $'000 | Group Impact $'000 | Parent Impact $'000 |
| Claim settlement period | + 0.5 years | (290) | (243) | (271) | (248) |
| | - 0.5 years | 290 | 243 | 271 | 248 |
| Claims expenses ratio | increase of 1% | 85 | 74 | 277 | 254 |
| | decrease of 1% | (85) | (74) | (277) | (254) |
| Inflation rates | increase of 1% | 834 | 815 | 978 | 955 |
| | decrease of 1% | (719) | (700) | (755) | (733) |
| Discount rates | increase of 1% | (759) | (741) | (801) | (779) |
| | decrease of 1% | 872 | 853 | 935 | 912 |

**(e) Risk management policies and procedures**
The financial condition and operations of the general insurance business are affected by a number of key risks including insurance risk, interest rate risk, currency risk, market risk, financial risk, compliance risk, fiscal risk and operational risk. Notes on the policies and procedures employed in managing these risks in the general insurance business are set out below.

***(i) Objectives in managing risks arising from insurance contracts and policies for mitigating those risks***
The risk management activities include prudent underwriting, pricing, and management of risk, together with claims management, reserving and investment management. The objective of these disciplines is to enhance the financial performance of the insurance operations.

The key policies in place to mitigate risk arising from writing general insurance contracts include:
- comprehensive management information systems and actuarial models using historical information to calculate premiums and monitor claims;
- monitoring natural disasters such as earthquake, flood, storms and other catastrophes using models; and
- the use of reinsurance to limit the Group's exposure.

***(ii) Terms and conditions of insurance contracts that have a material effect on amount timing and uncertainty of cash flows***
The term and conditions attaching to insurance contracts affect the level of insurance risk accepted by the Group. There are no special terms and conditions in any non standard contracts that have a material impact on the financial statements.

***(iii) Concentration of insurance risk***

| Risk | Source of concentration | Risk Management measures |
|---|---|---|
| An accumulation of risks arising from a natural peril | Insured property concentrations | Accumulation risk modelling, reinsurance protection |
| A large property loss | Fire or collapse affecting one building or a group of adjacent buildings | Maximum acceptance limits, property risk grading, reinsurance protection |
| Inclusion of multiple classes of casualty business in the one event | Response by a multitude of the Group's policies to the one event, for example a construction liability and professional indemnity policy | Purchase of reinsurance clash protection |

**(f) Development of claims**
The following table shows the development of net undiscounted outstanding claims relative to the current estimate of ultimate claims costs for the five most recent years.

**Group**

| | Incident year | | | | | | |
|---|---|---|---|---|---|---|---|
| Ultimate claims cost estimate | Prior NZ$000 | 2006 NZ$000 | 2007 NZ$000 | 2008 NZ$000 | 2009 NZ$000 | 2010 NZ$000 | Total NZ$000 |
| At end of accident year | - | 118,996 | 121,315 | 122,903 | 121,562 | 110,692 | |
| One year later | - | 117,333 | 121,196 | 123,926 | 122,349 | - | |
| Two years later | - | 116,573 | 119,803 | 123,455 | - | - | |
| Three years later | - | 116,498 | 119,625 | - | - | - | |
| Four years later | - | 116,237 | - | - | - | - | |
| Current estimate of ultimate claims cost | - | 116,237 | 119,625 | 123,455 | 122,349 | 110,692 | |
| Cumulative payments | - | (115,610) | (118,189) | (121,575) | (117,933) | (73,571) | |
| Undiscounted central estimate | 23,658 | 627 | 1,436 | 1,880 | 4,416 | 37,121 | 69,138 |
| Discount to present value | 13,283 | 21 | 16 | 17 | 29 | 36 | 13,402 |
| Discounted central estimate | 10,375 | 606 | 1,420 | 1,863 | 4,387 | 37,085 | 55,736 |
| Claims handling expense | | | | | | | 5,119 |
| Risk margin | | | | | | | 5,200 |
| **Net outstanding claims liabilities** | | | | | | | 66,055 |
| Reinsurance recoveries on outstanding claims liabilities and other recoveries | | | | | | | 75,446 |
| **Gross outstanding claims liabilities** | | | | | | | 141,501 |

## 21. Insurance business (Cont.)

**Company**

| Ultimate claims cost estimate | Incident year Prior NZ$000 | 2006 NZ$000 | 2007 NZ$000 | 2008 NZ$000 | 2009 NZ$000 | 2010 NZ$000 | Total NZ$000 |
|---|---|---|---|---|---|---|---|
| At end of accident year | - | 97,561 | 104,364 | 106,718 | 108,718 | 97,003 | |
| One year later | - | 97,827 | 103,794 | 107,439 | 109,756 | - | |
| Two years later | - | 97,871 | 103,519 | 107,281 | - | - | |
| Three years later | - | 97,782 | 103,648 | - | - | - | |
| Four years later | - | 97,705 | - | - | - | - | |
| Current estimate of ultimate claims cost | - | 97,705 | 103,648 | 107,281 | 109,756 | 97,003 | |
| Cumulative payments | - | (97,691) | (103,267) | (106,022) | (106,268) | (67,786) | |
| Undiscounted central estimate | 22,241 | 14 | 381 | 1,259 | 3,488 | 29,217 | 56,600 |
| Discount to present value | 13,261 | - | 3 | 1 | 1 | 2 | 13,268 |
| Discounted central estimate | 8,980 | 14 | 378 | 1,258 | 3,487 | 29,215 | 43,332 |
| Claims handling expense | | | | | | | 4,347 |
| Risk margin | | | | | | | 4,659 |
| **Net outstanding claims liabilities** | | | | | | | **52,338** |
| Reinsurance recoveries on outstanding claims liabilities and other recoveries | | | | | | | 65,476 |
| | | | | | | | |
| **Gross outstanding claims liabilities** | | | | | | | **117,814** |

**(g) Liability adequacy test**
The liability adequacy test has identified a surplus for each portfolio of contracts that are subject to broadly similar risks and are managed together as a single portfolio.

The risk margins adopted in performing the liability adequacy test have been selected to provide a probability of sufficiency of 75%. The outstanding claims liability is set at a level that is appropriate and sustainable to cover the Group's claims obligations after having regard to the prevailing market environment and prudent industry practice.

**(h) Insurer financial strength rating**
TOWER Insurance Limited has an insurer financial strength rating of "A-" (Excellent) issued by AM Best Company Limited.

**(i) Reinsurance programme**
Reinsurance programmes are structured to adequately protect the general insurance companies' solvency and capital positions. The adequacy of reinsurance cover is based on assessing TOWER's exposure in the worst possible scenario. The worst possible scenario for TOWER is a major Wellington earthquake. Each year, as part of setting the coming year's reinsurance premium, comprehensive modelling of the event probability and amount of the Group's exposure is undertaken.

## 22. Operating leases

| | Group 2010 NZ$000 | Group 2009 NZ$000 | Company 2010 NZ$000 | Company 2009 NZ$000 |
|---|---|---|---|---|
| Rent paid under non-cancellable operating leases during the year | 837 | 4,223 | 375 | 3,386 |
| Rent payable under non-cancellable operating leases to the end of the lease terms are: | | | | |
| – Not later than one year | 303 | 2,298 | 37 | 2,113 |
| – Later than one year and not later than five years | 172 | 6,424 | 24 | 6,285 |
| – Later than five years | 132 | 344 | - | 223 |
| | 607 | 9,066 | 61 | 8,621 |

All lease commitments in New Zealand have been centralised across the TOWER Limited Group and taken over by TOWER New Zealand Limited from 1 October 2009. The Company has been charged a management fee in return by TOWER New Zealand Limited.

Operating lease payments represent the future rentals payable for office space under current leases. Leases are entered into for an average of seven years with rental rates reviewed every three years.

## 23. Share based payments

The Company has three executive share option schemes. Each is equity settled and has differing conditions which are set out in the tables below. The exercise prices are set at the average of the share price for the 5 days before grant date. Subject to the discretion of the Board, options are forfeited if an employee leaves the Company before the options vest.

Vesting requirements of each tranche include service and performance conditions. The performance condition is based on a market condition such as total shareholder return achieved at the end of each reporting period. The holders of the options are not entitled to dividend or have other shareholder benefits, including voting rights.

The grant date fair value for options was estimated by using a binomial pricing model. The main inputs to the model were as follows:

| Terms of share schemes | Tranche F | Tranche G | Tranche I |
|---|---|---|---|
| Exercise price after rights issue | $2.10 | $1.38 | $1.93 |
| Grant date | 11-Dec-07 | 5-Dec-08 | 22-Dec-09 |
| Vesting date | 1-Dec-10 | 1-Dec-11 | 3-Dec-12 |
| Expiry date | 1-Dec-13 | 1-Dec-14 | 2-Dec-15 |
| Expected volatility | 20% | 40% | 30% |
| Risk free rate | 5.71% | 4.88% | 6.03% |
| Amount expensed during 2010 year (NZ$) | 45,554 | 26,181 | 6,883 |
| Amount expensed during 2009 year (NZ$) | 40,474 | 6,503 | - |

Expected volatility was determined by looking at the performance of the share price over a number of periods ranging from six months to two years adjusted to remove significant impacts arising from one off events.

The expected life is based on best estimates of management allowing for non-transferability, exercise restrictions and behavioural considerations. The weighted average fair value of options presented under Trance I during the year was $460,508 (2009: Tranche G was $315,600).

**Details of the share options outstanding as at 30 September were as follows:**

| | Number of options | | | Weighted average exercise price (1) |
|---|---|---|---|---|
| **2010** | **Tranche F** | **Tranche G** | **Tranche I** | |
| Outstanding at start of year | 314,533 | 200,000 | - | $1.82 |
| Granted | - | - | 200,000 | $1.93 |
| **Outstanding at the end of the year** | **314,533** | **200,000** | **200,000** | **$1.85** |
| **Exercisable at the end of the year** | - | - | - | $0.00 |
| **2009** | | | | |
| Outstanding at start of year | 314,533 | - | - | $2.19 |
| Granted | - | 200,000 | - | $1.47 |
| **Outstanding at the end of the year** | **314,533** | **200,000** | - | **$1.82** |
| **Exercisable at the end of the year** | - | - | - | $0.00 |

(1) *The weighted average exercise price for outstanding share options at the end of the year has been adjusted for the impact of the rights issue.*
No options are exercisable in 2010 (2009: Nil).

## 24. Financial instruments categories

The analysis of financial assets and liabilities into their categories and classes is set out in the following tables.

| GROUP | Total $000 | Loans and receivables $000 | Designated at fair value through profit or loss $000 |
|---|---|---|---|
| **As at 30 September 2010** | | | |
| **Financial assets** | | | |
| Cash and cash equivalents | 67,125 | 67,125 | - |
| Reinsurance recoveries receivable | 75,446 | 75,446 | - |
| Outstanding premiums and trade receivables | 82,289 | 82,289 | - |
| Related party receivables | 578 | 578 | - |
| Investments in equity securities | 3,049 | - | 3,049 |
| Investments in fixed interest securities | 172,270 | - | 172,270 |
| Investments in property securities | 8,886 | - | 8,886 |
| **Total financial assets** | 409,643 | 225,438 | 184,205 |
| **As at 30 September 2009** | | | |
| **Financial assets** | | | |
| Cash and cash equivalents | 31,559 | 31,559 | - |
| Reinsurance recoveries receivable | 31,728 | 31,728 | - |
| Outstanding premiums and trade receivables | 78,871 | 78,871 | - |
| Related party receivables | 355 | 355 | - |
| Investments in equity securities | 2,923 | - | 2,923 |
| Investments in fixed interest securities | 199,378 | - | 199,378 |
| Investments in property securities | 8,250 | - | 8,250 |
| **Total financial assets** | 353,064 | 142,513 | 210,551 |

| COMPANY | Total $000 | Loans and receivables $000 | Designated at fair value through profit or loss $000 |
|---|---|---|---|
| **As at 30 September 2010** | | | |
| **Financial assets** | | | |
| Cash and cash equivalents | 54,369 | 54,369 | - |
| Reinsurance recoveries receivable | 65,476 | 65,476 | - |
| Outstanding premiums and trade receivables | 71,071 | 71,071 | - |
| Related party receivables | 4,756 | 4,756 | - |
| Investments in fixed interest securities | 145,561 | - | 145,561 |
| Investments in property securities | 8,886 | - | 8,886 |
| **Total financial assets** | 350,119 | 195,672 | 154,447 |
| **As at 30 September 2009** | | | |
| **Financial assets** | | | |
| Cash and cash equivalents | 17,519 | 17,519 | - |
| Reinsurance recoveries receivable | 2,644 | 2,644 | - |
| Outstanding premiums and trade receivables | 70,128 | 70,128 | - |
| Related party receivables | 4,938 | 4,938 | - |
| Investments in fixed interest securities | 176,548 | - | 176,548 |
| Investments in property securities | 8,250 | - | 8,250 |
| **Total financial assets** | 280,027 | 95,229 | 184,798 |



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## 24. Financial instruments categories (cont.)

| GROUP | Total | Financial liabilities at amortised cost |
|---|---|---|
| As at 30 September 2010 | $000 | $000 |
| **Financial liabilities** | | |
| Trade payables | 19,476 | 19,476 |
| Other payables | 5,582 | 5,582 |
| Reinsurance payables | 5,756 | 5,756 |
| Related party payables | 14,953 | 14,953 |
| **Total financial liabilities** | **45,767** | **45,767** |
| **As at 30 September 2009** | | |
| **Financial liabilities** | | |
| Trade payables | 20,527 | 20,527 |
| Other payables | 4,884 | 4,884 |
| Reinsurance payables | 7,348 | 7,348 |
| Related party payables | 1,263 | 1,263 |
| FuturePlan Debenture | - | - |
| **Total financial liabilities** | **34,022** | **34,022** |

| COMPANY | Total | Financial liabilities at amortised cost |
|---|---|---|
| As at 30 September 2010 | $000 | $000 |
| **Financial liabilities** | | |
| Trade payables | 17,579 | 17,579 |
| Other payables | 4,850 | 4,850 |
| Reinsurance payables | 6,460 | 6,460 |
| Related party payables | 19,465 | 19,465 |
| **Total financial liabilities** | **48,354** | **48,354** |
| **As at 30 September 2009** | | |
| **Financial liabilities** | | |
| Trade payables | 19,119 | 19,119 |
| Other payables | 4,353 | 4,353 |
| Reinsurance payables | 7,141 | 7,141 |
| Related party payables | 4,215 | 4,215 |
| **Total financial liabilities** | **34,828** | **34,828** |

## 25. Contingent liabilities

There are no material contingent liabilities at balance date (2009: $Nil).

## 26. Capital commitments

There were no capital commitments as at 30 September 2010 (2009: $Nil).

## 27. Impact of amendments to IFRS

### (A) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group.

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 October 2010 or later periods and the Group has not early adopted them:

- IFRS 9 'Financial Instruments' (effective from 1 January 2013). The standard is the first step in replacing IAS 39 and establishes two primary measurement categories for financial assets: amortised cost and fair value, with classification depending on an entity's business model and the contractual cash flow characteristics of the financial asset. The Company is in the process of evaluating the potential effect of this standard.
- IAS 24, 'Related party disclosures' (effective from 1 January 2011). The revised standard amends the definition of a related party. The Company is in the process of evaluating the potential effect of this standard.
- IFRS 7, 'Financial instruments' (effective retrospectively from 1 January 2011). The amendment emphasises the interaction between quantitative and qualitative disclosures about the nature and extent of risks associated with financial instruments. The Company will apply the IFRS 7 amendments from 1 October 2010.

### (B) Standards, amendments and interpretations to existing effective 2010 or early adopted by the Group

The Group has adopted the following applicable, new and amended IFRS's as of the 1 October 2009:

- IAS 27 (Revised), 'Consolidated and separate financial statements' (effective from 1 July 2009). The revised standard requires that investments in subsidiaries, jointly controlled entities and associated accounted for in accordance with IAS 39 in the parent's separate financial statements should continue to be measured in accordance with IAS 39 when classified as held for sale (or included in a disposal group classified as held for sale). The Group has applied IAS 27 (Revised) to transactions with non-controlling interests from 1 October 2009.
- IAS 1 (Amendment) 'Presentation of financial statements' (effective from 1 January 2009). The revised IAS 1 requires an entity to present all owner changes in equity, separately from non-owner changes in equity, in a statement of changes in equity.

  All non-owner changes in equity (i.e. comprehensive income) are required to be presented in one statement of comprehensive income or two statements (an income statement and a statement of comprehensive income). Components of comprehensive income are not permitted to be presented in the statement of changes in equity. The change in accounting policy has only impacted presentation aspects.
- IFRS 3 (Revised), 'Business combinations' (effective from 1 July 2009). The revised standard continues to apply the acquisition method to business combinations, with some significant changes. For example, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the statement of comprehensive income. There has been no impact during the current financial year. The revised standard will be applied as appropriate in future years.

## 28. Subsequent events

There are no subsequent events relating to the year ended 30 September 2010 that have a material impact on the financial statements.

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## Independent Auditors' Report
to the shareholders of TOWER Insurance Limited

### Report on the Financial Statements

We have audited the financial statements of TOWER Insurance Limited on pages 2 to 28 which comprise the balance sheets as at 30 September 2010, the income statements, statements of comprehensive income and statements of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information for both the Company and the Group. The Group comprises the Company and the entities it controlled at 30 September 2010 or from time to time during the financial year.

*Directors' Responsibility for the Financial Statements*

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

*Auditors' Responsibility*

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

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

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

Other than in our capacity as auditors and providers of other assurance services we have no relationship with, or interests in, TOWER Insurance Limited or any of its subsidiaries.

PRICEWATERHOUSECOOPERS

## Independent Auditors' Report
TOWER Insurance Limited

*Opinion*

In our opinion, the financial statements on pages 2 to 28:

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

(ii) give a true and fair view of the financial position of the Company and Group as at 30 September 2010, and their financial performance for the year then ended.

**Report on Other Legal and Regulatory Requirements**

We also report in accordance with Sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993. In relation to our audit of the financial statements for the year ended 30 September 2010:

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

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

**Restriction on Distribution or Use**

This report is made solely to the Company's shareholders, as a body, in accordance with Section 205(1) of the Companies Act 1993. Our audit work has been undertaken so that we might state to the Company's shareholders those matters which we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Group and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

Chartered Accountants
23 December 2010

Auckland