Westpac Life-NZ- Limited

Annual report

For the year ended 30 September 2019

Westpac Life-NZ- Limited

Contents

This annual report covers Westpac Life-NZ- Limited (the '**Company**') as an individual entity.

Westpac Life-NZ- Limited is a company limited by shares, incorporated and domiciled in New Zealand. Its registered office is:

Westpac on Takutai Square
16 Takutai Square
Auckland

The members of the Board of Directors of the Company ('**Board**') as at the signing date of these financial statements are Ronald James Hill, David Gordon Benison, Karen Lee Silk, Georgina Maida McDonald Croft, and Katherine Anne Morrison.

Westpac Life-NZ- Limited

Directors' report

Pursuant to section 211(3) of the Companies Act 1993, the shareholder of the Company has agreed that the Annual Report of the Company need not comply with the requirements of paragraphs (a), and (e) to (j) of subsection (1) and subsection (2) of section 211.

Accordingly, there is no information to be included in the Annual Report other than the financial statements for the year ended 30 September 2019 and the independent auditor's report on those financial statements.

For and on behalf of the Board of Directors:

Director
24 January 2020

Director
24 January 2020

Westpac Life-NZ- Limited

Statement of comprehensive income for the years ended 30 September

	Note	2019 $'000	2018 $'000
Insurance premium revenue	4	149,308	157,731
Outwards reinsurance premium expense	4	(15,792)	(15,729)
Net premium revenue		133,516	142,002
Investment income	4	8,202	6,923
Commission and other income[1]	4	25,188	22,641
Losses on derivative financial instruments[1]	4	(25,570)	(7,168)
Net revenue		141,336	164,398
Insurance claims and rebate expense	5	(68,951)	(67,731)
Reinsurance recoveries revenue	5	14,594	10,958
Net claims expenses		(54,357)	(56,773)
Changes in policy liabilities	10	32,566	11,824
Other operating expenses	5	(46,601)	(48,543)
Net claims and expenses		(68,392)	(93,492)
Profit before income tax		72,944	70,906
Income tax expense	6	(20,138)	(19,451)
Net profit for the year		52,806	51,455
Other comprehensive income (net of tax)		-	-
Total comprehensive income for the year		52,806	51,455

[1] The Company has made a number of presentational changes to the statement of comprehensive income in the current year. Comparatives have been restated. Refer to Note 1 for further detail.

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

Balance sheet as at 30 September

	Note	2019 $'000	2018 $'000
Assets			
Cash and cash equivalents	14	5,977	5,920
Financial assets at fair value through profit or loss ('FVPL')	9	191,775	200,736
Reinsurance recoveries receivable	16	13,165	10,516
Other assets		2,086	1,912
Total assets		213,003	219,084
Liabilities			
Payables due to related entities	14	4,848	4,632
Derivative financial instruments	14	9,287	2,082
Current tax liabilities		4	3,796
Other liabilities	12	3,281	4,329
Deferred tax liabilities	11	43,060	35,710
Claims reserve	16	41,470	39,722
Policy liabilities	10	(141,687)	(109,121)
Total negative liabilities		(39,737)	(18,850)
Net assets		252,740	237,934
Shareholder's equity			
Share capital	13	79,520	79,520
Retained profits		173,220	158,414
Total Shareholder's equity		252,740	237,934

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

Westpac Life-NZ- Limited

Statement of changes in equity for the years ended 30 September

	Note	Share Capital $'000	Retained Profits $'000	Total $'000
As at 1 October 2017		79,520	164,959	244,479
Year ended 30 September 2018				
Net profit for the year		-	51,455	51,455
Total comprehensive income for the year ended 30 September 2018		-	51,455	51,455
Transactions with owners:				
Dividends paid on ordinary shares	13	-	(58,000)	(58,000)
As at 30 September 2018		79,520	158,414	237,934
Year ended 30 September 2019				
Net profit for the year		-	52,806	52,806
Total comprehensive income for the year ended 30 September 2019		-	52,806	52,806
Transactions with owners:				
Dividends paid on ordinary shares	13	-	(38,000)	(38,000)
As at 30 September 2019		79,520	173,220	252,740

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

Statement of cash flows for the years ended 30 September

	Note	2019[1] $'000	2018[1] $'000
Cash flows from operating activities			
Premiums received		149,360	157,737
Reinsurance payments		(16,759)	(15,661)
Interest income received		289	362
Commission income and other income received		24,963	22,602
Investment income received		1,725	(339)
Derivative financial instruments loss payments		(18,365)	(6,691)
Claims and rebates payments		(67,203)	(60,704)
Reinsurance income received		11,945	14,941
Other operating expenses paid		(46,448)	(47,364)
Income taxes paid		(16,580)	(18,364)
Net cash provided by operating activities	18	22,927	46,519
Cash flows from investing activities			
Sale of investments		122,004	131,212
Purchase of investments		(106,855)	(118,384)
Purchase of property and equipment		(19)	(11)
Net cash provided by investing activities		15,130	12,817
Cash flows from financing activities			
Dividends paid to ordinary shareholders	13	(38,000)	(58,000)
Net cash used in financing activities		(38,000)	(58,000)
Net increase in cash and cash equivalents		57	1,336
Cash and cash equivalents at the beginning of the year		5,920	4,584
Cash and cash equivalents at the end of the year	14	5,977	5,920

[1] The Company has made a number of presentational changes to the statement of comprehensive income in the current year which has also impacted the presentation of the statement of cash flows. Comparatives have been restated. Refer to Note 1 for further detail.

The above statement of cash flows should be read in conjunction with the accompanying notes. Details of the reconciliation of net cash provided by operating activities to net profit are provided in Note 18.

pwc

Westpac Life-NZ- Limited

Notes to the financial statements

Note 1. Financial statement preparation

These financial statements were authorised for issue by the Board on 24 January 2020. The Board has the power to amend and reissue the financial statements.

Westpac Life-NZ- Limited's (the '**Company**') primary activities are the development, underwriting and management of products under life insurance legislation providing insurance cover against the risks of death, disability, redundancy and bankruptcy. The Company also manages some insurance agency arrangements.

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

a. Basis of preparation

(i) Basis of accounting

These financial statements are general purpose financial statements prepared in accordance with the Financial Reporting Act 2013 and the Financial Markets Conduct Act 2013. These financial statements comply with Generally Accepted Accounting Practice, applicable New Zealand equivalents to International Financial Reporting Standards ('**NZ IFRS**') and other authoritative pronouncements of the External Reporting Board ('**XRB**'), as appropriate for for-profit entities. The Company is a Tier 1 entity. These financial statements comply with International Financial Reporting Standards ('**IFRS**'), as issued by the International Accounting Standards Board. The Company is carrying on insurance business in New Zealand and is therefore subject to the requirements set out in the Insurance (Prudential Supervision) Act 2010 ('**IPSA**'), including licensing and supervision by the Reserve Bank of New Zealand ('**RBNZ**'). The Company was granted a full licence by the RBNZ on 1 May 2013.

All amounts in these financial statements have been rounded in thousands of New Zealand dollars unless otherwise stated.

(ii) Comparative revisions

Comparative information has been revised where appropriate to conform to changes in presentation in the current year and to enhance comparability. Where there has been a material misstatement of comparative information the nature of, and the reasons for, the restatement is disclosed in the changes in accounting policies section below or in the relevant note.

(iii) Historical cost convention

The financial statements have been prepared under the historical cost convention, as modified by applying fair value accounting to financial assets and financial liabilities (including derivative instruments) measured at fair value through the profit or loss section of the statement of comprehensive income. The going concern concept has been applied.

(iv) Foreign currency translation

Functional and presentational currency

The financial statements of the Company are presented in New Zealand dollars, which is the Company's functional and presentation currency.

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit or loss section of the statement of comprehensive income.

(v) Changes in accounting policies

Voluntary presentation changes

The following voluntary presentation changes to the statement of comprehensive income (and related notes) have been made to provide more relevant information to the users of the financial statements. These changes have no effect on the measurement of these items and therefore had no impact on retained earnings or net profit.

Statement of comprehensive income

Fee income and other income has been disaggregated into commission and other income and losses on derivative financial instruments as shown in the table below:

	2018		
	Reported $'000	Presentation changes $'000	Restated $'000
Statement of comprehensive income			
Fee income and other income	15,473	(15,473)	-
Commission and other income	-	22,641	22,641
Losses on derivative financial instruments	-	(7,168)	(7,168)

Net premium revenue and other income (Note 4)

- Outwards reinsurance premium expense is now presented as an offsetting item against insurance premium revenue. Accordingly, this note has been renamed from premium revenue and other income to net premium revenue and other income.
- To comply with disclosure requirements, interest income calculated using the effective interest rate method has been presented separately from other interest income.
- Realised gains and unrealised gains on investments in unit trusts are now presented separately for debt securities and equity securities based on the underlying nature of the investments.
- Non-risk fees have been renamed to general insurance commission and is presented as part of commission and other income.

Notes to the financial statements

Note 1. Financial statement preparation (continued)

Net claims and other operating expenses (Note 5)

- Reinsurance recoveries revenue (previously part of total premium revenue and other income in Note 4) is now included as an offsetting item against claims expenses. Accordingly, this note has been renamed from claims, rebates and other operating expenses to net claims and other operating expenses.

b. Financial assets and financial liabilities

(i) Recognition

Purchases and sales of financial assets are recognised on trade-date, the date on which the Company commits to purchase or sell the asset. Financial liabilities are recognised when an obligation arises.

(ii) Classification and measurement

As comparatives have not been restated upon the adoption of NZ IFRS 9 *Financial instruments* (September 2014) (**'NZ IFRS 9'**) the accounting policy applied in 2019 differs to that applied in the comparative period. The accounting policy applied in the comparative period is discussed in Note 22. The accounting policy applied in 2019 is as follows.

The Company classifies its financial assets into the following categories: financial assets at FVPL, derivative financial instruments and financial assets at amortised cost. Financial assets at FVPL relate to local authority securities, investment grade corporate bonds, term deposits and units in unlisted unit trusts. Derivative financial instruments are measured at FVPL. Financial assets at amortised cost include cash and cash equivalents and other assets.

<u>Financial assets</u>

Financial assets are classified based on a) the business model within which the assets are managed, and b) whether the contractual cash flows of the instrument represent solely payment of principal and interest (**'SPPI'**).

The Company determines the business model at the level that reflects how groups of financial assets are managed. When assessing the business model the Company considers factors including how performance and risks are managed, evaluated and reported and the frequency and volume of, and reason for, sales in previous periods and expectations of sales in future periods.

When assessing whether contractual cash flows are SPPI, interest is defined as consideration primarily for the time value of money and the credit risk of the principal outstanding. The time value of money is defined as the element of interest that provides consideration only for the passage of time and not consideration for other risks or costs associated with holding the financial asset. Terms that could change the contractual cash flows so that they may not meet the SPPI criteria include contingent and leverage features, non-recourse arrangements, and features that could modify the time value of money.

Debt instruments

If the debt instruments have contractual cash flows which represent SPPI on the principal balance outstanding they are classified at:

- amortised cost if they are held with a business model which is achieved through holding the financial asset to collect these cash flows, or
- fair value through other comprehensive income (**'FVOCI'**) if they are held with a business model which is achieved both through collecting these cash flows or selling the financial asset, or
- FVPL if they are held with a business model which is achieved through selling the financial asset.

Debt instruments are also measured at FVPL where the contractual cash flows do not represent SPPI on the principal balance outstanding or where it is designated at FVPL to eliminate or reduce an accounting mismatch.

Debt instruments at FVPL are measured at fair value with subsequent changes in fair value recognised in the profit or loss section of the statement of comprehensive income.

<u>Financial liabilities</u>

The Company classifies its financial liabilities into the following categories: financial liabilities at amortised cost and derivative financial instruments. Financial liabilities are measured at amortised cost with the exception of derivative financial instruments which are measured at FVPL. Financial liabilities at amortised cost relate to payables due to related entities and certain other liabilities.

Financial assets and financial liabilities measured at FVPL are recognised initially at fair value. All other financial assets and financial liabilities are recognised initially at fair value plus or minus directly attributable transaction costs respectively.

Further details of the accounting policy for each category of financial asset or financial liability mentioned above is set out in the note for the relevant item.

The Company's policies for determining the fair value of financial assets and financial liabilities are set out in Note 15.

(iii) Derecognition

Financial assets are derecognised when the rights to receive cash flows from the asset have expired, or when the Company has either transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full under a 'pass through' arrangement and transferred substantially all the risks and rewards of ownership.

There may be situations where the Company has partially transferred the risks and rewards of ownership but has neither transferred nor retained substantially all the risks and rewards of ownership. In such situations, the asset continues to be recognised on the balance sheet to the extent of the Company's continuing involvement in the asset.

Financial liabilities are derecognised when the obligation is discharged, cancelled or expires.

(iv) Impairment of financial assets

As comparatives have not been restated upon the adoption of NZ IFRS 9 the accounting policy applied in 2019 differs to that applied in comparative periods. The accounting policy applied in comparative periods is discussed in Note 22. The accounting policy applied in 2019 is as follows.

Notes to the financial statements

Note 1. Financial statement preparation (continued)

Impairment charges are based on an expected loss model which measures the difference between the current carrying amount and the present value of expected future cash flows taking into account past experience, current conditions and multiple probability-weighted macroeconomic scenarios for reasonably supportable future economic conditions.

Impairment charges are recognised in profit or loss, with a corresponding amount recognised as a reduction of the carrying value of the financial asset through an offsetting provision account.

(v) Other assets

As comparatives have not been restated upon the adoption of NZ IFRS 9 the accounting policy applied in 2019 differs to that applied in comparative periods. The accounting policy applied in comparative periods is discussed in Note 22. The accounting policy applied in 2019 is as follows.

Other assets include commissions receivable under insurance agency arrangements and premiums due from policyholders. Commissions receivable are classified as financial assets at amortised cost.

c. Statement of cash flows

Operating, investing and financing activities

Operating activities are the principal revenue-producing activities of the Company and other activities that are not investing or financing activities. Investing activities are the acquisition and disposal of long-term assets and other investments that are not included in cash and cash equivalents. Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the Company.

d. Critical accounting assumptions and estimates

Applying the Company's accounting policies requires the use of judgment, assumptions and estimates which impact the financial information. Significant assumptions and estimates used are included in the policies below.

Uncertainty over valuation of life insurance policy liabilities and claims reserve

Policy liabilities and claims reserve arising from life insurance contracts are computed at each reporting date using statistical and mathematical methods. The valuations are prepared by suitably qualified personnel on the basis of recognised actuarial methods and with due regard to the actuarial principles. The methodology takes into account the risks and uncertainties of the particular classes of business written.

The key factors that may affect the estimation of these liabilities are:

- the rate at which projected future cash flows are discounted;
- the cost of providing benefits and administrating the contracts;
- mortality, morbidity and trauma experience; and
- discontinuance experience, which affects the Company's ability to recover the cost of acquiring new business over the life of the contracts.

In addition, factors such as regulation, competition, interest rates, taxes, rebates values, securities' market conditions and general economic conditions affect the level of these liabilities.

The uncertainties surrounding these assumptions mean that it is likely that the actual observed claims incidence will vary from the liability estimated at the reporting date. See Note 2 for more detail on the valuation of the policy liabilities and the assumptions applied.

Reinsurance recoveries receivable

Reinsurance recoveries receivable 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 Company may not receive amounts due to it and these amounts can be reliably measured.

Fair value of financial instruments

Financial instruments classified as held for trading or designated at fair value through the profit or loss section of the statement of comprehensive income are recognised in the financial statements at fair value. All derivatives are measured and recognised at fair value.

Fair value is obtained from quoted market prices, independent dealer price quotations, discounted cash flow models and option pricing models, which incorporate current market and contractual prices for the underlying instrument, time to expiry, yield curves and volatility of the underlying instrument. The calculation of fair value for any financial instrument may also require adjustment of the quoted price or model value to reflect the cost of credit risk (where not embedded in underlying models or prices used). The process of calculating fair value on illiquid instruments or from a valuation model may require estimation of certain pricing parameters, assumptions or model characteristics. These estimates are calibrated against industry standards, economic models and observed transaction prices.

The fair value of financial instruments is provided in Note 15, as well as the mechanism by which fair value has been derived.

e. Standards adopted during the year ended 30 September 2019

NZ IFRS 9

The Company adopted NZ IFRS 9 on 1 October 2018 which replaces NZ IAS 39 *Financial instruments: Recognition and Measurement* ('NZ IAS 39'). The adoption of NZ IFRS 9 resulted in no impact to retained earnings on 1 October 2018, with no restatement of comparatives as permitted by the standard.

Impairment

NZ IFRS 9 introduces a revised impairment model which requires entities to recognise expected credit losses ('ECL') based on unbiased forward looking information, replacing the incurred loss model under NZ IAS 39 which only recognised impairment if there was objective evidence that a loss had been incurred. The new ECL model did not have a material impact on the Company as the financial assets subject to impairment are those measured at amortised cost which are short term and/or of a high credit quality. As a result, no impairment allowances have been recognised as any such impairment would be wholly insignificant to the Company.

Notes to the financial statements

Note 1. Financial statement preparation (continued)

Classification and measurement

NZ IFRS 9 replaced the classification and measurement model in NZ IAS 39 with a new model that categorises financial assets based on a) the business model within which the assets are managed, and b) whether the contractual cash flows under the instrument represents SPPI.

NZ IFRS 9 did not have a significant impact on the classification or measurement of the Company's financial assets and liabilities as:

- Financial assets at FVPL are designated as such if an accounting mismatch would otherwise occur from the measurement of the related policy liability. Accordingly, these financial assets continue to be classified and measured at FVPL under NZ IFRS 9.
- Cash and cash equivalents and other assets which meet the solely payments of principle and interest criterion and are held for collection of contractual cash flows continue to be measured at amortised cost. These financial assets were previously classified as loans and receivables under NZ IAS 39.
- Derivative financial instruments which were considered held for trading under NZ IAS 39 continue to be classified and measured at FVPL under NZ IFRS 9.
- Payables to related entities and other liabilities in scope of NZ IFRS 9 remain classified and measured as financial liabilities at amortised cost.

The accounting policies for the classification and measurement of financial assets and financial liabilities are and located on page 21 and in the relevant notes to the financial statements for financial assets and financial liabilities.

Hedging

NZ IFRS 9 changes hedge accounting by increasing the eligibility of both hedged items and hedging instruments and introducing a more principles-based approach to assessing hedge effectiveness. Adoption of the new hedge accounting model is optional until the IASB completes its accounting for dynamic risk management project. Until this time, current hedge accounting under NZ IAS 39 can continue to be applied. As the Company does not apply hedge accounting, the NZ IFRS 9 hedge accounting related changes do not have an impact on the financial statements.

NZ IFRS 15 *Revenue from Contracts with Customers* ('NZ IFRS 15')

The Company adopted NZ IFRS 15 on 1 October 2018. It replaced NZ IAS 18 *Revenue* and related interpretations, and applies to all contracts with customers, except leases, financial instruments and insurance contracts. The standard provides a systematic approach to revenue recognition by introducing a five-step model governing revenue measurement and recognition.

This includes:

- identifying the contract with customer;
- identifying each of the performance obligations included in the contract;
- determining the amount of consideration in the contract;
- allocating the consideration to each of the identified performance obligations; and
- recognising revenue as each performance obligation is satisfied.

NZ IFRS 15 did not result in changes to the Company's current accounting treatment of fee and commission income.

f. Future developments in accounting standards

The following new standard and interpretations which may have a material impact on the Company have been issued, but are not yet effective and have not been early adopted by the Company:

NZ IFRS 17 *Insurance Contracts* was issued on 10 August 2017 and will be effective for the 30 September 2022 year end unless early adopted. This will replace NZ IFRS 4 *Insurance Contracts*. The main changes under the standard are:

- the scope of the standard may result in some contracts that are currently "unbundled", i.e. accounted for separately as insurance and investment contracts being required to be "bundled" and accounted for as an insurance contract;
- portfolios of contracts (with similar risks which are managed together) will be required to be disaggregated to a more granular level by both the age of a contract and the likelihood of the contract being onerous in order to determine the recognition of profit over the contract period (i.e. the contractual service margin). The contractual service margin uses a different basis to recognise profit to the current Margin on Services approach for life insurance and therefore the pattern of profit recognition is likely to differ;
- risk adjustments, which reflect uncertainties in the amount and timing of future cash flows, are required for both general and life insurance contracts rather than just general insurance contracts under the current accounting standards;
- the contract boundary, which is the period over which profit is recognised, differs and is determined based on the ability to compel the policyholder to pay premiums or the substantive obligation to provide coverage/services. For some general insurance contracts (e.g. some lender mortgage insurance and reinsurance contracts) this may result in the contract boundary being longer. For life insurance, in particular term renewable contracts, the contract boundary is expected to be shorter. Both will be impacted by different patterns of profit recognition compared to the current standards;
- a narrower definition of what acquisition costs may be deferred;
- an election to recognise changes in assumptions regarding discount rate in other comprehensive income rather than in statement of comprehensive income;
- an election to recognise changes in the fair value of assets supporting policy liabilities in other comprehensive income rather than through statement of comprehensive income;
- reinsurance contracts and the associated liability is to be determined separately to the gross contract liability and may have different contract boundaries; and
- additional disclosure requirements.

The standard is expected to result in a reduction in the level of deferred acquisition costs, however the quantum of this and the profit or loss impacts to the Company are not yet practicable to determine.

On 26 June 2019, the IASB issued an exposure draft proposing a number of amendments to the insurance contracts standard. If approved, these amendments would allow entities to:

- defer acquisition costs for anticipated renewals outside of the initial contract boundary; and

Westpac Life-NZ- Limited

Notes to the financial statements

Note 1. Financial statement preparation (continued)

- recognise a gain in the profit or loss for reinsurance contracts, to offset losses from onerous contracts on initial recognition (to the extent the reinsurance contracts held covers the losses of each contract on a proportionate basis).

In addition, the effective date of the standard would be deferred by one year to be applicable to the Company for the 30 September 2023 financial year, unless early adopted.

NZ IFRIC 23 *Uncertainty over Income Tax Treatments* ('**NZ IFRIC 23**') was issued on 10 August 2017 and will be effective for the 30 September 2020 financial year. NZ IFRIC 23 clarifies the recognition and measurement criteria in NZ IAS 12 *Income Taxes* ('**NZ IAS 12**') where there is uncertainty over income tax treatments, and requires an assessment of each uncertain tax position as to whether it is probable that a taxation authority will accept the position.

Where it is not considered probable, the effect of the uncertainty will be reflected in determining the relevant taxable profit or loss, tax bases, unused tax losses and unused tax credits or tax rates. The amount will be determined as either the single most likely amount or the sum of the probability weighted amounts in a range of possible outcomes, whichever better predicts the resolution of the uncertainty. Judgements will be reassessed as and when new facts and circumstances are presented.

The interpretation is not expected to have a material impact on the Company.

A revised Conceptual Framework ('**Framework**') was issued on 10 May 2018. This will be effective for the Company for the 30 September 2021 financial year. The revised Framework includes new definitions and recognition criteria for assets, liabilities, income and expenses and other relevant financial reporting concepts. The changes are not expected to have a material impact on the Company.

Other amendments to existing standards that are not yet effective are not expected to have a material impact to the Company.

Note 2. Actuarial assumptions and methods

a. Actuarial policies and methods

The effective date of the actuarial valuation of policy liabilities (refer to Note 10) and solvency reserving requirement (refer to Note 19) is 30 September 2019. The actuarial valuation for the Company was prepared by Ian New, who is the Appointed Actuary of the Company and a Fellow of the New Zealand Society of Actuaries.

Policy liabilities for life insurance contracts are amounts which, when taken together with future premiums and investment earnings, are required to meet the payment of future benefits and expenses, and incorporate profit margins on existing business to be released when earned in future periods.

b. Disclosure of assumptions

The valuations included in the reported results are calculated using assumptions about certain key underlying variables. The assumptions are determined by the Appointed Actuary of the Company based on results of annual investigations into the experience of the Company's in force business, industry experience data and data provided by the Company's reinsurers.

After making appropriate checks, the Appointed Actuary of the Company was satisfied as to the accuracy of the data from which the amount of insurance policy liabilities has been determined.

The key assumptions used in determining policy liabilities for the major products are disclosed below.

(i) Discount rates

The discount rates used to determine policy liabilities were as follows:

	2019	2018
Loan Cover	0.745%	1.720%
Bill Protection Insurance, Mortgage Insurance and Flexicover Insurance	0.660%	1.898%
Other Major Products	0.958%	2.650%

These assumed discount rates are gross of tax and net of investment management expenses.

(ii) Profit carriers

The profit carriers for the products which were valued on a projection basis were as follows:

Product	**Profit Carrier**
Term Cover	Premium
Gold Term Cover	Premium
Simplicity Life	Premium
Disability Income Insurance	Premium
Gold Disability Income Insurance	Premium
Flexicover Insurance	Premium
Mortgage Repayment Insurance	Claims
Loan Cover	Claims
Bill Protection Insurance	Premium
Lifetime Guarantee and Kiwilife Senior	Claims
Kiwilife, Kiwicover and Kiwiguard	Premium
Accident Cover	Premium
Ex-Trust Bank Mortgage Insurance	Premium

pwc

Notes to the financial statements

Note 2. Actuarial assumptions and methods (continued)

(iii) Maintenance expenses

The non-commission maintenance expenses allowances assumed were as follows:

Product	2019 Maintenance Expense	2018 Maintenance Expense
Term Cover ($ per annum per policy)	$41.00	$33.00
Gold Term Cover ($ per annum per policy)	$41.00	$33.00
Simplicity Life ($ per annum per policy)	$41.00	$33.00
Disability Income Insurance ($ per annum per policy)	$41.00	$33.00
Gold Disability Income Insurance ($ per annum per policy)	$41.00	$33.00
Flexicover Insurance (% of premiums)	7.0%	5.5%
Mortgage Repayment Insurance (% of original single premium spread over the term)	13.0%	10.0%
Loan Cover (% of original single premium spread over the term)	13.0%	10.0%
Bill Protection Insurance ($ per annum per policy)	$57.00	$46.00
Lifetime Guarantee and Kiwilife Senior ($ per annum per policy)	$57.00	$46.00
Kiwilife, Kiwicover and Kiwiguard ($ per annum per policy)	$41.00	$33.00
Accident Cover ($ per annum per policy)	$41.00	$33.00
Ex-Trust Bank Mortgage Insurance (% of premiums)	7.0%	5.5%

(iv) Inflation and automatic indexation of benefits

Maintenance expenses are assumed to increase at 2.0% per annum (30 September 2018: 2.0% per annum). Term cover policies and disability income insurances with automatic inflation linked indexation of benefits are assumed to have benefit increases of 2.0% per annum (30 September 2018: 2.0% per annum).

(v) Taxation

For the purposes of the actuarial calculations, a taxation rate of 28% (30 September 2018: 28%) has been assumed throughout. A GST taxation rate of 15% (30 September 2018: 15%) has been assumed throughout.

(vi) Rebate values

Future policy rebate values are projected on the basis of the Company's current practice.

(vii) Unit-linked business

The Company has no unit-linked business.

(viii) Participating business

The Company has no participating business.

(ix) Mortality, morbidity and trauma

The projected rates of claims reflect industry experience in New Zealand together with the Company's experience where appropriate. The tables used as a basis for mortality and morbidity assumptions were as follows:

Product	2019	2018
Term Cover and Gold Term Cover	94% of NZ Insured Lives 2008-2010 with adjustments for smoker status and selection	94% of NZ Insured Lives 2008-2010 with adjustments for smoker status and selection
Disability Income Insurance and Gold Disability Income Insurance	Adjusted ADI 2007-2011	Adjusted ADI 2007-2011
Simplicity Life, Kiwilife, Life components of Mortgage Repayment Insurance, Flexicover Insurance, Ex-Trust Bank Mortgage Insurance and Loan Cover	Adjusted NZ Insured Lives 2008-2010	Adjusted NZ Insured Lives 2008-2010
Lifetime Guarantee and Kiwilife Senior	Adjusted NZ Population 2010/12	Adjusted NZ Population 2010/12
Disability components of Mortgage Repayment Insurance, Flexicover Insurance, Ex-Trust Bank Mortgage Insurance, Bill Protection Insurance and Loan Cover	Adjusted ADI 2007-2011	Adjusted ADI 2007-2011
Kiwicover, Kiwiguard and Accident Cover	Adjusted NZ population accident experience 2009/11	Adjusted NZ population accident experience 2009/11
Term Cover and Gold Term Cover	95% Company experience trauma table	95% Company experience trauma table

(x) Rates of discontinuance

Projected rates of discontinuance of policies were as follows:

pwc

Westpac Life-NZ- Limited

Notes to the financial statements

Note 2. Actuarial assumptions and methods (continued)

Product	2019	2018
Term Cover (% per annum)	7.0% to 17.0%	7.0% to 17.5%
Gold Term Cover (% per annum)	7.0% to 16.0%	7.0% to 15.0%
Simplicity Life (% per annum)	10.0%	10.0%
Disability Income Insurance (% per annum)	7.0%	7.0%
Gold Disability Income Insurance (% per annum)	7.0% to 15.0%	7.0% to 15.0%
Flexicover Insurance (% per annum)	12.0%	12.0%
Mortgage Repayment Insurance (% per annum)	15.0%	15.0%
Loan Cover (% per annum)	30.0% to 60.0%	30.0% to 60.0%
Bill Protection Insurance (% per annum)	15.0%	15.0%
Lifetime Guarantee (% per annum)	1.0%	1.0%
Kiwilife Senior (% per annum)	3.0%	3.0%
Kiwilife (% per annum)	10.0%	10.0%
Kiwicover, Kiwiguard (% per annum)	6.0%	6.0%
Accident Cover (% per annum)	6.0%	6.0%
Ex-Trust Bank Mortgage Insurance (% per annum)	15.0%	15.0%

Where a range of discontinuance rates is assumed for a product, the assumption varies by the duration in force of the policy. Where a flat rate of discontinuance is assumed for a product, the assumption is independent of duration.

(xi) Effect of changes in actuarial assumptions

Aside from the changes in discount rates due to changing economic conditions, the changes in actuarial assumptions from 2018 to 2019 set out above had no impact upon the Company's policy liabilities as none of the Company's related product groups is in loss recognition (from 2017 to 2018: nil). Aside from the changes in discount rates which increased profit by $19,151,000 (30 September 2018: increased $3,587,000), the changes in actuarial assumptions had the effect of decreasing the present value of future planned profit margins by $17,822,000 (30 September 2018: decreasing by $292,000). The primary contributors to this impact were:

- ($9,203,000) arising from the changes to projected non-commission maintenance expenses (30 September 2018: nil); and
- ($3,729,000) arising from changes to premium rates (30 September 2018: $3,259,000);
- ($3,003,000) arising from changes to projected rates of morbidity claims (30 September 2018: nil);
- ($1,887,000) arising from the changes to projected rates of discontinuance (30 September 2018: $173,000);
- nil arising from changes to projected investment management expenses (30 September 2018: ($2,773,000));
- nil arising from changes to projected rates of incidence of mortality claims (30 September 2018: ($951,000));

Other modelling changes had the effect of decreasing the present value of future planned profit margins by $9,000 (30 September 2018: increasing by $342,000).

(xii) Sensitivity analysis

The Company conducts sensitivity analysis to quantify exposure to risk of changes in the key underlying variables such as discount rates, maintenance expenses, mortality, morbidity and discontinuances. The valuations included in the reported results and the Company's best estimates of future performance are calculated using certain assumptions about these variables. The movement in any key variable will impact the performance and net assets of the Company and as such represents a risk.

The table below illustrates how changes in key variables would impact the reported profit of the Company.

	2019		2018	
	Change in Variable	**Impact on Future Planned Profit**	Change in Variable	Impact on Future Planned Profit
Changes in discount rates	+0.1%	-1.1%	+0.1%	-1.0%
	-0.1%	1.2%	-0.1%	1.0%
Change in mortality and morbidity	+10%	-9.1%	+10%	-8.8%
	-10%	9.2%	-10%	8.9%
Change of non-commission policy maintenance expense	+10%	-0.7%	+10%	-0.6%
	-10%	0.7%	-10%	0.6%
Change in discontinuance rate	+10%	-11.8%	+10%	-10.9%
	-10%	13.9%	-10%	12.7%

The financial impact of the above changes would emerge through reported profits over future years, except for the impact of changes to discount rates which would result in an immediate one-off impact upon reported profit. The Company currently has a derivative arrangement in place to offset a portion of the financial impact of changes to discount rates. None of the Company's groups of related products are in loss recognition and none would move into loss recognition upon reasonably expected changes in the variables set out in the above table, where the changes are applied individually.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 3. Risk management policies and procedures

a. The Company's Risk Management Programme

The Company's financial condition and operating activities are affected by a number of key financial risks (insurance risk, credit risk, market risk and liquidity risk) as well as non-financial risks (compliance risk, operational risk, conduct risk, reputation risk and environmental, social and governance risk).

The Board determines the Company's overall risk appetite and approves the Risk Management Programme, management strategies, policies and practices to ensure that risks are identified and managed within the context of this appetite.

Inherent in the Company's risk management approach are the requirements to:

- meet regulatory and compliance obligations;
- protect the Company's capital and desired financial strength rating;
- enhance risk-return within the Company's risk appetite;
- achieve transparency of the Company's risk profile; and
- embed adequate controls to guard against excessive risk or undue risk concentration.

Senior management is responsible for implementing and assessing the effectiveness of risk management strategies and internal controls of the Company in accordance with the overarching Risk Management Programme, policies and procedures covering risk identification, rating, assessment, treatment and ongoing management (including reporting).

The life insurance activities of the Company are concerned with the pricing, acceptance and management of the mortality and morbidity risks of lives insured. The risks underwritten by the Company are actively managed to ensure they do not adversely affect the Company's ability to pay benefits and claims when due. Compliance and operational risks are controlled and monitored to maintain the efficiency of the Company as well as to manage the risk of non-compliance.

The Company's Risk Oversight Committee (**'WLL ROC'**) meets quarterly and is responsible for overseeing the effectiveness and implementation of the Risk Management Programme. The WLL ROC oversees and manages all risks inherent in the operations of the Company. Material matters are escalated to the Company's Board, the Westpac Banking Corporation (**'WBC'**) NZ Executive Risk Committee and if required the WBC Board Risk and Compliance Committee, the WBC Board Audit Committee and the CEO of WBC will be notified.

As prescribed by Section 73 of IPSA, the Company maintains the Risk Management Programme and this is reviewed regularly. The Risk Management Programme consists of the Board Risk Appetite Statement and Risk Management Framework.

b. Risk Management Framework

The Company has adopted the 'Three Lines of Defence' approach to risk management which reflects its culture of 'risk is everyone's business' and that all employees are responsible for identifying and managing risk and operating within the Company's desired risk profile. Each 'Line of Defence' is responsible for establishing its own risk controls and processes for determining whether those controls continue to be adequate and effective. Each subsequent 'Line of Defence' also oversees and advises on the adequacy of the processes and controls at the preceding level and considers them in forming its views on the adequacy and effectiveness of risk management.

The Company accepts and manages risks that arise from business activities, provided such risks are within the Company's defined risk appetite and where applicable, the Company receives an appropriate risk-adjusted return for taking those risks.

c. Categories of risks

The key risks that the Company is subject to are specific insurance risks and risks arising from the general business environment.

Note 3. Risk management policies and procedures (continued)

The Risk Management Framework identifies the following broad categories of risk:

- Insurance risk
- Credit risk
- Market risk
- Liquidity risk
- Non-financial risk including capital and regulatory compliance risk

Additional details surrounding the risk management activities relating to the management of these risks follows.

(i) Insurance risk

Insurance risk is the risk of mis-estimation of the expected cost of insured events, volatility in the number or severity of insured events, and mis-estimation of the cost of incurred claims. Insurance risk manifests as the inherent uncertainty as to the occurrence, amount and timing of insurance liabilities. The Company is exposed to this risk through its underwriting philosophy, product design, retention limits, reinsurance arrangements, mortality / morbidity fluctuations and trends, natural disasters and the possibility of pandemics.

To manage insurance risk, the Company has various risk mitigation systems in place:

- Claims fluctuation risk – the Company maintains actuarial models to value the in-force book of individual policies as is used as a key input in the pricing of policies. The Company's claims performance is closely monitored and reported on. Claims fluctuations are managed through reinsurance arrangements;
- Underwriting risk – insurance policies underwritten by the Company are subject to approval by a specialist underwriter who reviews each application against defined standards. The Company ensures that underwriting standards remain up to date and in line with industry and reinsurer standards;
- Reinsurance risk – the Company obtains reinsurance cover for all life insurance policies with a sum insured above the risk retention levels approved by the Board. The Company also has catastrophe reinsurance cover in place;
- Termination risk – the Company actively monitors and manages termination rates; and

Westpac Life-NZ- Limited

Notes to the financial statements

Note 3. Risk management policies and procedures (continued)

- Concentration risk - the Company maintains a retention limit per life and reinsures the excess.

Under the Company's internal reporting system the financial and operating results, mortality and morbidity experience and expenses are monitored quarterly against budget projections. In addition, detailed annual actuarial investigations are performed into the mortality, morbidity and persistency experience of the life insurance products. Concentrations of risk based on individual lives are managed through the use of surplus reinsurance arrangements whereby the Company's maximum exposure to any individual life is capped. The Company also holds catastrophe reinsurance treaties to limit large losses arising from concentrations of risk due to geographical exposure or single events. The Company actively manages its exposure under its retention agreements with its reinsurers. A product pricing process ensures that profitability is not materially impacted by changes to the age and gender profile of the in-force business. The Company conducts sensitivity analysis to quantify exposure to changes in risks affecting the key underlying variables and further detail is provided in Note 2.

(ii) Other financial risks

The Company is exposed to a range of financial risks through its financial assets, reinsurance assets and insurance liabilities. The key components of financial risk are as follows:

- Credit risk - the risk of financial loss where a customer or counterparty fails to meet their financial obligations;
- Market risk - the risk of an adverse impact on earnings resulting from changes in market factors. These risks are monitored daily against a comprehensive limit framework based on longer term risk/return objectives. The principal risk components of this monitoring process are:
  - Interest rate risk - the potential loss arising from changes in the value of financial instruments and policy liabilities, due to changes in market interest rates; and
  - Equity price risk - the potential loss arising from decline in value of equity instruments due to changes in their quoted market value or implied volatilities;
- Liquidity risk - the risk that the Company will not be able to fund assets and meet obligations as they come due.

The Company's policies for managing the above financial risks are set out below.

<u>Credit risk</u>

Financial assets which potentially subject the Company to concentrations of credit risk consist of cash and cash equivalents, financial assets at FVPL, reinsurance recoveries receivable and other assets. Related risks include resilience risk and asset concentration risk.

The following policies and procedures are in place to mitigate the Company's exposure to credit risk:

- exposures to counterparties are monitored and controlled to ensure significant deterioration in credit quality is identified, credit risk management information is accurate and complete and excessive concentrations of credit risk are identified and controlled;
- financial strength ratings of reinsurers are monitored and the Company seeks to maintain reinsurance providers above agreed minimum financial strength ratings;
- credit risk limits for investment assets are defined within a recognised rating scale and managed for the Company by the appointed investment portfolio managers. The Risk Management Framework also sets out acceptable credit quality ratings for investments that may be held; and
- credit risk in respect of customer balances is actively monitored and losses incurred on non-payment of premiums or contributions will only persist during the grace period specified in the policy document until expiry, when the policy is terminated.

As part of its overall risk management programme the Company cedes a proportion of its insurance risk. While these cessions mitigate insurance risk, the amounts recoverable from reinsurers expose the Company to credit risk. Exposure to and the credit quality of reinsurance counterparties are actively monitored.

The maximum exposure to credit risk is represented by the carrying amount of on-balance sheet financial assets (which comprises cash and cash equivalents, financial assets at FVPL, other assets and reinsurance recoveries receivable).

As comparatives have not been restated for the adoption of NZ IFRS 9, the following table is disclosed based on the requirements of NZ IAS 39.

30 September 2018	Neither past due nor impaired					Past Due But not Impaired	
	AAA $'000	AA $'000	A $'000	Not Rated $'000	Subtotal $'000	$'000	Total $'000
Financial assets							
Cash and cash equivalents	-	5,920	-	-	5,920	-	5,920
Financial assets at fair value through profit or loss[1]	2,841	7,013	-	-	9,854	-	9,854
Other assets	-	1,721	-	156	1,877	-	1,877
Insurance assets							
Reinsurance recoveries receivable	-	10,516	-	-	10,516	-	10,516
Total maximum exposure to credit risk	2,841	25,170	-	156	28,167	-	28,167

[1] Debt instruments held in unit trusts are not included in the above disclosure as the unit trusts do not have credit ratings. The unit trusts are indirectly exposed to credit risk, however given the conservative investment mandates, comprising solely fixed interest securities, the credit risk is assessed as low.

<u>Market risk</u>

The main market risk that the Company faces is interest rate risk. This reflects the underlying nature of its investments and liabilities. The Company's investment strategies for the Westpac Life-NZ-Limited Shareholder Fund ('**Shareholder Fund**') and Westpac Life-NZ-Limited Statutory Fund No. 1 ('**Statutory Fund No.1**') are approved by the Board. The investment strategies are reviewed annually.

To manage market risk arising from policy liabilities, the Company uses derivatives to manage interest rate risk. This is achieved by implementing an interest rate swap arrangement.

To mitigate market risk arising from financial assets at fair value through the profit or loss section of the statement of comprehensive income, the Company's investment manager has implemented the following controls:

- trading authorities and responsibilities are clearly delineated at all levels to ensure accountability;

pwc

Notes to the financial statements

Note 3. Risk management policies and procedures (continued)

- a structured system of limits and reporting of exposures against these exist for all trading activities; and
- models are used to determine the risk and impact on statement of comprehensive income.

In addition to these controls, the Company's investment manager uses derivatives to:

- protect an asset or portfolio against a fluctuation in market value;
- reduce the transaction costs of achieving a desired market exposure;
- immediately adjust the asset exposure within the established strategy;
- adjust the duration of fixed interest portfolios; or
- manage the exposure within a portfolio to fluctuations in interest rates and foreign currency exchange rates.

Interest rate risk

Interest rate risk is the potential loss arising from changes in the value of financial instruments due to changes in market interest rates.

The Company is exposed to interest rate risk in that future interest rate movements will affect cash flows, the market value of fixed interest assets, and the market value of unit trusts which hold fixed interest assets.

The Company is also exposed to interest rate risk on obligations arising from its life insurance contracts which is mitigated by the interest rate swap contracts entered into by the Company which creates an economic hedge. The interest rate swap is designed to substantially hedge the impact of interest rate movements on the policy liabilities valuation. For the year ended 30 September 2019 and 2018, there is no material unmatched interest rate risk in the Company and any changes in market interest rates will not materially affect the statement of comprehensive income and equity of the Company. A sensitivity analysis of the policy liabilities is disclosed in Note 2. The interest rate risk created by fixed interest assets and reinsurance recoveries is not deemed material.

Equity price risk

The Company is exposed to equity price risk arising from its investments in unit trusts. The underlying investments of these unit trusts indirectly expose the Company to various risks such as interest rate risk, foreign currency risk and credit risk.

The following table provides the after tax impact on profit or loss and equity for a reasonably possible change in equity prices:

	2019 $'000	2018 $'000
0.5% decrease in unit trust prices	(678)	(687)
0.5% increase in unit trust prices	678	687

Liquidity risk

The liquidity of both physical and derivative positions is factored into the investment decision making process. Considerations include market depth, possible market disruptions and standard settlement times.

The liquidity position of the Company is monitored regularly and funds backing life insurance contracts are significantly invested in readily realisable assets such as cash, short term securities and unit trust investments. Minimum cash balances required to be held are established to ensure that sufficient funds are available to meet all potential policy holder and shareholder obligations.

The following liquidity analysis of financial assets and liabilities presents the contractual undiscounted cash flows receivable and payable, and is based on the remaining period as at balance date to the contractual maturity. The balances in the tables below may not agree to the balance sheet as the tables incorporate all cash flows on an undiscounted basis, including both principal and associated future interest income/expense accruals.

The Company's undiscounted maturity profiles for financial assets and liabilities are as follows:

	30 September 2019				
	No Specific Maturity[1] $'000	Up to 1 Year[2] $'000	1 to 5 Years $'000	Over 5 Years $'000	Total $'000
Financial assets					
Cash and cash equivalents	-	5,977	-	-	5,977
Financial assets at fair value through profit or loss	188,242	3,533	-	-	191,775
Other assets	-	2,050	-	-	2,050
Insurance assets					
Reinsurance recoveries receivable	-	10,145	1,707	1,313	13,165
Total	188,242	21,705	1,707	1,313	212,967
Financial liabilities					
Payables due to related entities	-	4,848	-	-	4,848
Derivative financial instruments	-	9,287	-	-	9,287
Other liabilities	-	2,849	-	-	2,849
Insurance liabilities					
Claims reserve	-	37,867	2,029	1,574	41,470
Total	-	54,851	2,029	1,574	58,454

[1] Amounts classified under 'No Specific Maturity' refer to investments in unit trusts, which can be withdrawn on demand.
[2] Amounts classified under 'Up to 1 Year' refer to all commitments which are either contractually due within the timeframe or payable on demand.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 3. Risk management policies and procedures (continued)

	30 September 2018				
	No Specific Maturity[1] $'000	Up to 1 Year[2] $'000	1 to 5 Years $'000	Over 5 Years $'000	Total $'000
Financial assets					
Cash and cash equivalents	-	5,920	-	-	5,920
Financial assets at fair value through profit or loss	190,882	9,854	-	-	200,736
Other assets	-	1,877	-	-	1,877
Insurance assets					
Reinsurance recoveries receivable	-	8,050	1,241	1,225	10,516
Total	190,882	25,701	1,241	1,225	219,049
Financial liabilities					
Payables due to related entities	-	4,632	-	-	4,632
Derivative financial instruments	-	2,082	-	-	2,082
Other liabilities	-	4,014	-	-	4,014
Insurance liabilities					
Claims reserve	-	36,767	1,471	1,484	39,722
Total	-	47,495	1,471	1,484	50,450

[1] Amounts classified under 'No Specific Maturity' refer to investments in unit trusts, which can be withdrawn on demand.
[2] Amounts classified under 'Up to 1 Year' refer to all commitments which are either contractually due within the timeframe or payable on demand.

(iii) Capital and regulatory compliance risk

The risk of legal or regulatory sanction, financial or reputational loss arising from the Company's failure to abide by the compliance obligations required of the Company.

Effective compliance risk management is about identifying compliance obligations, and implementing and testing controls to ensure these obligations are met. The Company's compliance obligations include all obligations that have an impact on the Company including, but not limited to, obligations arising under IPSA, its related regulations, licence conditions and standards issued by the RBNZ.

The Board and senior management commit to compliance management through the establishment and maintenance of a dedicated compliance function in support of the Risk Management Framework. Staff are required to be proactive in becoming aware of their compliance obligations and implement the obligations in their day to day business activities, including actively monitoring and reporting compliance failures.

The Company maintains a Compliance Plan which set out the measures that it needs to apply to ensure compliance with the relevant compliance obligations.

The Company holds sufficient capital to mitigate the impact of losses which exceed the Company's ongoing surpluses. The Company strictly adheres to minimum regulatory capital requirements. In addition, the Board has defined a target level of capital to be held to ensure ongoing adherence with regulatory minimums.

Solvency reserves maintained by the Company are disclosed in Note 19.

Note 4. Net premium revenue and other income

Accounting policy

Insurance premium revenue

Life insurance premiums with a regular due date are recognised as revenue on an accrual basis. Premiums with no due date are recognised as revenue on a cash received basis. Premiums are shown before deduction of commission. There is no deposit component.

Outwards Reinsurance premium expense

Premium ceded to reinsurers under reinsurance contracts are recognised as outwards reinsurance premium expense presented within net premium revenue in accordance with the pattern of reinsurance service received.

Interest income

Interest income for all interest earning financial assets at amortised cost, detailed within the table below, is recognised using the effective interest rate method.

The effective interest rate method calculates the amortised cost of a financial instrument by discounting the financial instruments estimated future cash receipts or payments to their present value and allocates the interest income, including any fees, premiums or discounts integral to the instrument, over its expected life.

Commission and other income

General insurance commission income which arises from commissions received on insurance business whereby the Company acts as an agent, are recognised in profit or loss when the performance obligation is satisfied by transferring the promised service.

Other income includes refunds received in relation to reinsurance arrangements.

Gain or loss on derivative financial instruments

Realised gains or losses and unrealised gains or losses arising from changes in the fair value of derivative financial instruments are recognised as investment income in the statement of comprehensive income in the period in which they arise. Interest income on financial assets at FVPL is recognised as part of interest income.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 4. Net premium revenue and other income (continued)

	Note	2019[1] $'000	2018[1] $'000
Insurance premium revenue		149,308	157,731
Less: Outwards reinsurance premium expense		(15,792)	(15,729)
Total net premium revenue		133,516	142,002
Interest income			
Deposits with related entities - calculated using the effective interest method	14	9	18
Fixed interest bearing securities - other		284	298
Total interest income		293	316
Gains/(losses) on financial assets at FVPL:			
Realised losses on unit trusts - debt securities		(81)	(63)
Realised gains on unit trusts - equity securities		7,499	5,591
Unrealised gains on unit trusts - debt securities		17	11
Unrealised gains on unit trusts - equity securities		474	1,068
Total gains/(losses) from financial assets at FVPL		7,909	6,607
Total investment income		8,202	6,923
Commission and other Income			
General insurance commission		23,696	20,995
Other		1,492	1,646
Total commission and other income		25,188	22,641
Fair value losses on derivative financial instruments	14	(25,570)	(7,168)
Total premium revenue and other income		141,336	164,398

[1] The Company has made a number of presentational changes to the statement of comprehensive income in the current year. Comparatives have been restated. Refer to Note 1 for further detail.

Note 5. Net claims and other operating expenses

Accounting policy

Claims expenses

All incurred insurance claims are recognised as expenses in the statement of comprehensive income. Claims are recognised in the statement of comprehensive income when the liability to the policy holder under the policy contract has been established, or upon notification of the insured event depending on the type of claim. There is no deposit component.

Reinsurance recoveries revenue

Reinsurance recoveries are recognised as revenue as the underlying claims are incurred and are presented within net claims expenses. Recoveries receivable are measured as the present value of the expected future receipts, calculated on the same basis as the claims reserve.

Rebate expenses

Rebate expenses are expenses of refunding the premium customers paid on the loan cover product, if the customers' Westpac loan is repaid in full before the due date or the Westpac loan is varied during the term.

Policy acquisition expenses

Policy acquisition expenses are the expenses of acquiring new business including commissions and similar distribution expenses, expenses of accepting, issuing and initially recording policies.

Policy maintenance expenses

Policy maintenance expenses are the expenses of administering policies subsequent to sale and maintaining operations such that they are sufficient to service existing policies. These include general growth and development expenses and all operating and management expenses other than policy acquisition and investment management expenses.

Investment management expenses

Investment management expenses are the expenses of managing investment funds.

	2019[1] $'000	2018[1] $'000
Insurance claims[2]	(66,507)	(61,425)
Rebate expenses[2]	(2,444)	(6,306)
Total insurance claims and rebate expense	(68,951)	(67,731)
Reinsurance recoveries revenue	14,594	10,958
Net claims expenses	(54,357)	(56,773)

Notes to the financial statements

Note 5. Net claims and other operating expenses (continued)

	Note	2019 $'000	2018 $'000
Salaries and other staff expenses[3]			
Salaries and wages		4,696	4,380
Defined contribution plan		346	355
Other staff expenses		97	70
Total salaries and other staff expenses	14	5,139	4,805
Other expenses			
Audit fees			
Audit and review of the financial statements		92	92
Other assurance services - solvency return		17	11
GST		4,260	5,481
Management fees		2,475	2,438
Policy expenses		30,608	34,221
Purchased services		3,052	298
Stationery		99	230
Other expenses		859	967
Total other expenses		41,462	43,738
Total other operating expenses		46,601	48,543
Components of other operating expenses:			
Investment management expenses		528	666
Policy acquisition expenses[4]:			
Commissions[5]		3,673	8,732
Other		2,429	3,295
Policy maintenance expenses[4]:			
Commissions[5]		30,019	29,851
Other		9,952	5,999
Total other operating expenses		46,601	48,543

[1] The Company has made a number of presentational changes to the statement of comprehensive income in the current year. Comparatives have been restated. Refer to Note 1 for further detail.

[2] Comparative information for the year ended 30 September 2018 has been restated to correct the classification of expenses between insurance claims and rebate expenses. The impact of the restatement is a decrease for insurance claims from $65,965,000 to $61,425,000 and an increase for rebate expenses from $1,766,000 to $6,306,000.

[3] All employees are employed by Westpac New Zealand Limited ('**WNZL**'), rather than by the Company. WNZL pays these expenses to the employees and are then reimbursed by the Company.

[4] Expenses are categorised into acquisition or maintenance on the basis of time and cost analysis of activities carried out by the Company.

[5] Commissions are gross of GST for the purpose of this disclosure.

Note 6. Income tax expense

Accounting policy

Income tax

The income tax expense for the year comprises current tax and deferred tax. Tax is recognised in the statement of comprehensive income, except to the extent that it relates to items recognised directly in other comprehensive income.

Current tax is the expected tax payable for the year using tax rates and laws for each jurisdiction. Current tax also includes adjustments to tax payable for previous years.

Goods and services tax ('GST')

Where applicable, the profit or loss and assets are recognised net of GST, except to the extent that GST is not recoverable from Inland Revenue. In these circumstances, the GST is recognised as part of the profit or loss or the cost of the asset.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 6. Income tax expense (continued)

	Note	2019 $'000	2018 $'000
Income tax expense			
Current tax			
- Current year		12,757	17,584
- Prior year adjustments		31	(283)
Deferred tax	11		
- Current year		7,350	1,855
- Prior year adjustments		-	295
Total income tax expense		20,138	19,451
Reconciliation of income tax expense to profit before income tax expense			
Profit before income tax expense		72,944	70,906
Tax calculated at tax rate of 28% (30 September 2018: 28%)		20,424	19,854
Tax effect of amounts which are not deductible/(assessable) in calculating taxable income:			
Income not subject to tax		(318)	(420)
Expenses not deductible for tax purposes		1	5
Prior year adjustments		31	12
Total income tax expense		20,138	19,451

Note 7. Imputation credit account

	2019 $'000	2018 $'000
Imputation credits available for use in subsequent reporting periods	20,761	22,359

Note 8. Margin on services profit

	2019 $'000	2018 $'000
Net profit for the year arose from:		
Planned margins of revenues over expenses	40,496	41,343
Difference between actual and assumed experience	649	(1,192)
Profit on non-projected business	2,166	3,143
Investment earnings on assets in excess of policy liabilities	7,276	5,878
Net commission on fire and general agency	4,914	3,722
Adjustments for prior year over/(under) provision	(31)	(13)
Other sources	(2,664)	(1,426)
Loss recognition on groups of related products	-	-
Net profit for the year	52,806	51,455

Note 9. Financial assets at FVPL

Accounting policy

Financial assets at FVPL are the life insurance assets which include investments in unit trusts, government and semi-government bonds, and corporate bonds.

Life insurance assets are designated at FVPL upon initial recognition with changes in fair value included in the profit or loss.

	2019 $'000	2018 $'000
Debt securities		
New Zealand Government and semi-government securities	-	2,012
Corporate bonds	1,015	7,842
Unit trusts	176,883	181,906
Term deposits	2,518	-
Equity securities		
Unit trusts	11,359	8,976
Total financial assets at fair value through profit or loss	191,775	200,736
Amounts expected to be recovered within 12 months	191,775	200,736
Amounts expected to be recovered after 12 months	-	-
Total financial assets at fair value through profit or loss	191,775	200,736

Notes to the financial statements

Note 10. Policy liabilities

Accounting policy

Policy liabilities

Policy liabilities arising from insurance contracts are calculated by using the margin on services methodology in accordance with New Zealand Society of Actuaries Professional Standard 20 *Determination of Life Insurance Policy Liabilities*. Under this methodology, planned profit margins and an estimate of future liabilities are calculated separately for each major product line using applied assumptions at each reporting date. Profit margins are released over each financial period in line with the service that has been provided.

Liability adequacy test

Expected future cash flows are reviewed to establish the present value of the estimated future expenses for the group of related products against the present value of estimated future revenues. Where there is a shortfall in the liabilities, a loss is recognised in the statement of comprehensive income in the reporting period in which the assessment is made.

	Note	2019 $'000	2018 $'000
Balance at the beginning of the year		(109,121)	(97,297)
Changes in policy liabilities reflected in the statement of comprehensive income		(32,566)	(11,824)
Balance at the end of the year (net of reinsurance)		(141,687)	(109,121)
Components of policy liabilities:			
Future policy benefits		1,195,723	1,035,529
Balance of future expenses		679,340	588,077
Planned margins of revenues over expenses		759,358	673,232
Balance of future revenues		(2,733,575)	(2,370,617)
Policy liabilities at the end of the year		(99,154)	(73,779)
Less deferred tax liability element of policy liabilities	11	(42,533)	(35,342)
Balance at the end of the year (net of reinsurance)		(141,687)	(109,121)
Policy liabilities excluding deferred tax liability:			
Amounts expected to be settled within 12 months		(2,664)	1,060
Amounts expected to be settled after 12 months		(139,023)	(110,181)
Total policy liabilities (net of reinsurance)		(141,687)	(109,121)

The balance of future expenses and the balance of future revenues within total policy liabilities specifically relating to the future cost of reinsurance are included in the below reconciliation.

Future cost of reinsurance	2019 $'000	2018 $'000
Balance at the beginning of the year	18,430	16,809
Increase / (decrease) in future cost of reinsurance recognised in the statement of comprehensive income	205	1,621
Balance at the end of the year	18,635	18,430
Maturity analysis		
Amounts expected to be settled within 12 months	513	822
Amounts expected to be settled after 12 months	18,122	17,608

Future cost of reinsurance represents the net present value of expected future reinsurance cash flows. The underlying cash flows are reinsurance premiums less reinsurance recoveries, net of GST and income tax. The positive value of Future cost of reinsurance represents an expense to the Company.

The following analysis presents the maturity profile for the policy liabilities on an undiscounted basis. As such, the balances in the table below do not agree with the policy liabilities disclosed on the balance sheet.

Undiscounted policy liabilities excluding deferred tax liability	Note	2019 $'000	2018 $'000
Up to 1 Year		(2,737)	1,196
1 to 5 Years		(17,177)	(18,621)
Over 5 Years		(141,934)	(139,699)
Total undiscounted policy liabilities		(161,848)	(157,124)

Note 11. Deferred tax liabilities

Accounting policy

Deferred tax accounts for temporary differences between the carrying amounts of assets and liabilities in the financial statements and their values for taxation purposes. Deferred tax is not recognised if the temporary difference arises from the initial recognition of assets and liabilities that affect neither accounting nor taxable profit.

Deferred tax is determined using the enacted or substantively enacted tax rates and laws which are expected to apply when the assets will be realised or the liabilities settled.

Except as noted above, deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Deferred tax assets and liabilities have been offset where they relate to the same taxable entity or group and where there is a legal right and intention to settle on a net basis.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 11. Deferred tax liabilities (continued)

	Note	2019 $'000	2018 $'000
Deferred tax (assets)/liabilities attributable to the following:			
PIE income		1,003	765
Policy liabilities	10	42,533	35,342
Other		(476)	(397)
Balance at the end of the year		43,060	35,710
Amounts expected to be settled within 12 months		1,892	1,272
Amounts expected to be settled after 12 months		41,168	34,438
Balance at the end of the year		43,060	35,710
Movements			
Balance at the beginning of the year		35,710	33,560
Charged to the statement of comprehensive income		7,350	2,150
Balance at the end of the year		43,060	35,710

Deferred tax on policy liabilities

Life insurance policy liabilities represent the net present value of estimated future cash flows and planned profit margins. Using the margin on services methodology, planned after tax profit margins are recognised in the statement of comprehensive income over the period services are provided to policy holders.

Note 12. Other liabilities

Accounting policy

Other liabilities include compliance, regulation and remediation provisions, accrued expenses, bonus provision and other staff benefits. Accrued expenses are primarily premiums payable for reinsurance contracts. Accrued expenses and certain other liabilities are financial liabilities which are measured at amortised cost. The bonus provision and other staff benefits (including wages and salaries, inclusive of non-monetary benefits, and any associated on-costs) (e.g. payroll tax) is calculated based on expected payments. Compliance, regulation and remediation provisions relate to matters pertaining to the provision of services to our customers identified both as a result of regulatory action and internal reviews. An assessment of the likely cost to the Company of these matters (including applicable customer refunds) is made on a case-by-case basis and specific provisions are made where appropriate.

	Note	2019 $'000	2018 $'000
Accrued expenses		733	1,674
Compliance, regulation and remediation provisions[2,3]		1,702	1,427
Other[3]		414	913
Bonus provision and other staff benefits[1]	14	432	315
Total other liabilities		3,281	4,329
Amounts expected to be settled within 12 months		3,281	4,329
Amounts expected to be settled after 12 months		-	-
Total other liabilities		3,281	4,329

[1] Bonus provision and other staff benefits are liabilities payable by the Company to WNZL.

[2] The Company has raised a provision of $1,702,000 during the year ended 30 September 2019. This reflects newly identified issues requiring remediation, together with associated interest and program costs. Unutilised provisions of $1,427,000 were reversed in relation to obligations discharged during the year ended 30 September 2019.

[3] Compliance, regulation and remediation provisions have now been separately presented from the other category. Comparatives have been restated.

Note 13. Shareholder's equity

Accounting policy

Ordinary shares are recognised at the amount paid up per ordinary share net of directly attributable issue costs.

Ordinary share capital

	2019 Number of issued and authorised shares fully paid	2018 Number of issued and authorised shares fully paid
Balance at the beginning of the year	79,520,000	79,520,000
Balance at the end of the year	79,520,000	79,520,000

Ordinary shares

The shares have no par value. Ordinary shares entitle the holder to participate in dividends and, in the event of the Company winding up, to a share of the proceeds in proportion to the number of and amounts paid on the shares held. Each ordinary share entitles the holder to one vote, either in person or by proxy, at a shareholder meeting.

Notes to the financial statements

Note 13. Shareholder's equity (continued)

Dividends

As disclosed in Note 19, the Company is subject to certain regulatory capital requirements. The dividend policy ensures compliance with these requirements.

In the year ended 30 September 2019, the Company paid dividends in respect of the ordinary shares amounting to $38,000,000 (30 September 2018: $58,000,000) to the sole shareholder of the Company, Westpac Financial Services Group-NZ- Limited ('**WFSGNZL**').

Note 14. Related entities

Accounting policy

As comparatives have not been restated upon the adoption of NZ IFRS 9 the accounting policy applied in 2019 differs to that applied in the comparative period. The accounting policy applied in comparative periods is discussed in Note 22. The accounting policy applied in 2019 is as follows.

Related parties

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operating decisions, or one other party controls both. Examples include subsidiaries, associates, joint ventures and superannuation plans as well as key management personnel and their related parties.

Cash and cash equivalents

Cash and cash equivalents include cash at bank, at call money market deposits and other investments in highly liquid assets. Cash equivalents are short-term and highly liquid used in the day-to-day management of the Company that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents are brought to account at the face value or the gross value of the outstanding balance, where appropriate. They are accounted for as financial assets measured at amortised cost.

Derivative financial instruments

Derivative financial instruments are instruments whose values are derived from the value of an underlying asset, reference rate or index and include forwards, futures, swaps and options. Derivatives are presented as an asset where they have a positive fair value at balance date or as a liability where the fair value at balance date is negative. Derivatives with related parties are included in due from/due to related entities.
The Company is exposed to interest rate risk on obligations arising from its life insurance contracts. Interest rate swap derivatives used to mitigate interest rate risk specific to life insurance contracts are not designated into a hedge accounting relationship and are considered economic hedges. The interest rate swap is designed to substantially hedge the impact of interest rate movements on the policy liabilities valuation. These derivatives are measured at FVPL and are disclosed as derivative financial instruments.

Payables due to related entities

This amount includes amounts due to other entities controlled by WBC. Due to related entities includes accrual expense balances due to other related entities. They are measured at amortised cost.

Ultimate parent company

The Company is a wholly-owned subsidiary of WFSGNZL. The ultimate parent company is WBC, which is incorporated in Australia and whose financial statements are available, free of charge, at www.westpac.com.au.

All entities controlled by WBC, either directly or indirectly, are considered to be related entities of the Company. WNZL and BT Funds Management (NZ) Limited ('**BTFMNZL**') are indirect subsidiaries of the ultimate parent company.

Nature of transactions

Current account banking facilities and other financial products are provided by the WBC New Zealand Branch ('**NZ Branch**') to the Company.

Derivative transactions (interest rate swaps) are carried out between the Company and NZ Branch.

The Company received interest on cash deposits with the NZ Branch.

Insurance premium revenue was received from WNZL.

The Company's investment income is earned from the investments managed independently by BT Funds Management (NZ) Limited ('**BTFMNZL**'). The fair value of these investments is disclosed in Note 9.

Investment management services in respect of the Statutory Fund No. 1 and Shareholder Fund (refer to Note 17) are carried out by BTFMNZL and the Company pays investment management fees to BTFMNZL in respect of these services, which include the management of some of the Company's cash and cash equivalents which are deposited with the NZ Branch. The outstanding balance at year end is included in Sundry creditors - BTFMNZL.

Life insurance products are sold on behalf of the Company by WNZL. The Company pays sales commissions to WNZL. The outstanding balance at year end is included in Accrued expenses - WNZL.

Salaries and other staff expenses are reimbursed by the Company to WNZL. Under existing employment agreements, these salaries and other staff expenses relate to employees who are employed by WNZL. Transactions in relation to this related party is arranged on a cost recovery basis. The outstanding balance at year end is included in Sundry creditors - WNZL.

Fees for support services are paid by the Company to WNZL for certain operating costs incurred by WNZL. These transactions are arranged on a cost recovery basis. The outstanding balance at year end is included in Sundry creditors - WNZL.

Transactions with related entities are arranged on commercial terms.

The Company paid dividends to its parent entity, refer to Note 13.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 14. Related entities (continued)

Transactions with related entities

	Note	2019 $'000	2018 $'000
Dividend paid			
Dividend paid to WFSGNZL	13	38,000	58,000
Income			
Interest income from NZ Branch	4	9	18
Insurance premium revenue from WNZL		169	185
Total income		178	203
Expenses			
Investment management fees to BTFMNZL		479	587
Commissions to WNZL		30,557	34,169
Salaries and other staff expenses to WNZL	5	5,139	4,805
Fees for support services to WNZL		1,996	1,851
(Gain)/loss from derivative financial instruments transacted with NZ Branch	4	25,570	7,168
Total expenses		63,741	48,580

Due from and to related entities

	Note	2019 $'000	2018 $'000
Cash and cash equivalents			
Deposits held with NZ Branch		990	2,935
Deposits under the management of BTFMNZL and deposited with NZ Branch		4,987	2,985
Total cash and cash equivalents		5,977	5,920
Total receivables due from related entities		5,977	5,920
Settlement profile:			
Amounts expected to be recovered within 12 months		5,977	5,920
Amounts expected to be recovered after 12 months		-	-
Total receivables due from related entities		5,977	5,920
Payables due to related entities			
Sundry creditors - BTFMNZL		40	48
Sundry creditors - WNZL		161	391
Accrued expenses - WNZL		4,647	4,193
Total payables due to related entities		4,848	4,632
Derivative financial instruments			
Derivative financial instruments transacted with NZ Branch (at fair value)		9,287	2,082
Total derivative financial instruments		9,287	2,082
Other liabilities			
Bonus provision and other staff benefits - WNZL	12	432	315
Total other liabilities		432	315
Total payables due to related entities including derivative financial instruments and other liabilities		14,567	7,029
Settlement profile:			
Amounts expected to be recovered within 12 months		14,567	7,029
Amounts expected to be recovered after 12 months		-	-
Total payables due to related entities		14,567	7,029

The notional amount of the derivative financial instruments at 30 September 2019 was $5,866,400,000 (30 September 2018: $4,590,000,000). The fair value is disclosed in the balance sheet.

Except for cash and cash equivalents and derivative financial instruments, amounts due to and from related entities are normally settled within 90 days.

Key management personnel

Key management personnel are defined as being Directors and senior management of the Company. The Company paid no compensation to its non-independent key management personnel during the year (30 September 2018: nil) as any compensation is paid by WNZL and, where appropriate, is reimbursed by the Company as agreed with WNZL. However, the Company paid short term compensation to its independent key management personnel (Independent Directors) during the year amounting to $190,000 (30 September 2018: $152,000).

All other transactions with key management personnel, their related entities and other related parties are conducted in the ordinary course of business. These transactions principally involve the provision of insurance services.

Note 15. Fair value of financial instruments

Accounting policy

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Notes to the financial statements

Note 15. Fair value of financial instruments (continued)

On initial recognition, the transaction price generally represents the fair value of the financial instrument unless there is observable information available in an active market to the contrary. Where unobservable information is used, the difference between the transaction price and the fair value (day one profit or loss) is only recognised in statement of comprehensive income when the inputs become observable, or over the life of the instrument.

Fair valuation control framework

The Company uses a Fair Valuation Control Framework where the fair value is either determined or validated by a function independent of the originator of the transaction. This framework formalises the policies and procedures used to achieve compliance with relevant accounting, industry and regulatory standards. The framework includes specific controls relating to:

- the revaluation of financial instruments;
- independent price verification;
- fair value adjustments; and
- financial reporting.

The method of determining fair value differs depending on the information available.

Fair value hierarchy

A financial instrument's categorisation within the valuation hierarchy is based on the lowest level input that is significant to the fair value measurement.

The Company categorises all fair value instruments according to the hierarchy described below.

Valuation techniques

The Company applies market accepted valuation techniques in determining the fair valuation of over-the-counter derivatives.

The specific valuation techniques, the observability of the inputs used in valuation models and the subsequent classification for each significant product category are outlined below:

Financial instruments measured at fair value

Level 1 instruments

The fair value of financial instruments traded in active markets based on recent unadjusted quoted prices. These prices are based on actual arm's length basis transactions.

The valuations of Level 1 instruments require little or no management judgment.

There are no financial instruments included in the Level 1 category (30 September 2018: nil).

Level 2 instruments

The fair value for financial instruments that are not actively traded is determined using valuation techniques which maximise the use of observable market inputs. Valuation techniques include:

- the use of market standard discounting methodologies;
- option pricing models; and
- other valuation techniques widely used and accepted by market participants.

Instrument	Balance sheet category	Includes:	Valuation
Debt instruments	Financial assets at FVPL	Term deposits, local authority securities and investment grade corporate bonds	Valued using observable market prices or other widely used and accepted valuation techniques utilising observable market inputs.
Unit trusts	Financial assets at FVPL	Units in unlisted unit trusts	Valued using observable market prices or other widely used and accepted valuation techniques utilising observable market inputs.
Interest rate products	Derivative financial instruments	Interest rate swaps - derivative financial instruments	Industry standard valuation models are used to calculate the expected future value of payments, which is discounted back to a present value. The model's interest rate inputs are benchmark interest rates and active broker quoted interest rates in the swap markets. Interest rate volatilities are sourced from brokers and consensus data providers.

Level 3 instruments

Financial instruments valued where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data due to illiquidity or complexity of the product. These inputs are generally derived and extrapolated from other relevant market data and calibrated against current market trends and historical transactions.

These valuations are calculated using a high degree of management judgment.

There are no financial instruments included in the Level 3 category (30 September 2018: nil).

Analysis of movements between fair value hierarchy levels

During the year, there were no material transfers between levels of the fair value hierarchy (30 September 2018: no material transfers between levels).

Financial instruments not measured at fair value

For cash and cash equivalents, payables due to related entities, other assets and other liabilities which are carried at amortised cost, the carrying amount approximates to fair value. These items are either short-term in nature or reprice frequently, and are of a high credit rating.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 16. Reconciliation of claims reserve and reinsurance recoveries receivable

Accounting policy

Claims reserve

Provision has been made for liabilities in respect of insurance claims notified but not settled at balance date, together with an allowance for incurred but not reported ('**IBNR**') insurance claims.

Reinsurance recoveries receivable

Recoveries receivable represent amounts recoverable from reinsurers, calculated on the same basis as the liability for outstanding claims. Amounts recoverable from reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract.

Reconciliation of claims reserve

	2019 $'000	2018 $'000
Balance at the beginning of the year	39,722	32,695
Release of start of period reserve for claims closed during the year	(22,096)	(14,916)
Changes in claims reserves for the year	24,553	20,606
Changes in IBNR reserve for the year	(709)	1,337
Balance at the end of the year	41,470	39,722
Amounts expected to be settled within 12 months	37,867	36,767
Amounts expected to be settled after 12 months	3,603	2,955
Balance at the end of the year	41,470	39,722

Reconciliation of reinsurance recoveries receivable

	2019 $'000	2018 $'000
Balance at the beginning of the year	10,516	14,499
Release of start of period reinsurance recovery reserve for claims closed during year	(5,602)	(8,697)
Changes in reinsurance recovery reserves for the year	8,234	4,491
Changes in reinsurance recovery IBNR reserve for the year	17	223
Balance at the end of the year	13,165	10,516
Amounts expected to be settled within 12 months	10,145	8,050
Amounts expected to be settled after 12 months	3,020	2,466
Balance at the end of the year	13,165	10,516

Note 17. Statutory Fund

It is a requirement of the IPSA that a life insurer must have at least one statutory fund in respect of its life insurance business. The statutory fund is subject to restrictions imposed under the IPSA. A core requirement is that the assets in the statutory fund are only available to meet the liabilities and expenses of the life insurance business and cannot be used to support any other business of the life insurance company. Distribution of the retained profits of a statutory fund may only be made when certain solvency and other requirements are met.

Westpac Life-NZ- Limited

Notes to the financial statements

Note 17. Statutory Fund (continued)

Disaggregated information by fund is presented below.

	Note	Statutory Fund No. 1 $'000	Shareholder Fund $'000	Total All Funds $'000
Balance sheet as at 30 September 2019:				
Cash and cash equivalents		5,695	282	5,977
Financial assets at fair value through profit or loss		183,610	8,165	191,775
Reinsurance recoveries receivable		13,165	-	13,165
Other assets		139	1,947	2,086
Total assets		202,609	10,394	213,003
Payables due to related entities		3,583	1,265	4,848
Derivative financial instruments		9,287	-	9,287
Current tax (assets)/liabilities		(384)	388	4
Other liabilities		2,887	394	3,281
Deferred tax liabilities		43,032	28	43,060
Claims reserve		41,470	-	41,470
Policy liabilities		(141,687)	-	(141,687)
Total liabilities/(negative liabilities)		(41,812)	2,075	(39,737)
Share capital		79,520	-	79,520
Retained profits		164,901	8,319	173,220
Equity		244,421	8,319	252,740
Statement of comprehensive income for the year ended 30 September 2019:				
Net premium revenue		133,516	-	133,516
Investment income		7,966	236	8,202
Commission and other income		401	24,787	25,188
Losses on derivative financial instruments		(25,570)	-	(25,570)
Net claims expenses		(54,357)	-	(54,357)
Changes in policy liabilities		32,566	-	32,566
Other operating expenses		(27,272)	(19,329)	(46,601)
Profit before income tax		67,250	5,694	72,944
Net profit for the year		48,706	4,100	52,806
Transfer of capital (from)/to funds		(34,000)	34,000	-
Distributions made from funds (refer Note 13)	13	-	(38,000)	(38,000)

Westpac Life-NZ- Limited

Notes to the financial statements

Note 17. Statutory Fund (continued)

	Note	Statutory Fund No. 1 $'000	Shareholder Fund $'000	Total All Funds $'000
Balance sheet as at 30 September 2018:				
Cash and cash equivalents		5,648	272	5,920
Financial assets at fair value through profit or loss		191,898	8,838	200,736
Reinsurance recoveries receivable		10,516	-	10,516
Other assets		190	1,722	1,912
Total assets		208,252	10,832	219,084
Payables due to related entities		3,574	1,058	4,632
Derivative financial instruments		2,082	-	2,082
Current tax liabilities		3,435	361	3,796
Other liabilities		3,069	1,260	4,329
Net deferred tax liabilities/(assets)		35,776	(66)	35,710
Claims reserve		39,722	-	39,722
Policy liabilities		(109,121)	-	(109,121)
Total liabilities/(negative liabilities)		(21,463)	2,613	(18,850)
Share capital		79,520	-	79,520
Retained profits		150,195	8,219	158,414
Equity		229,715	8,219	237,934
Statement of comprehensive income for the year ended 30 September 2018:				
Net premium revenue		142,002	-	142,002
Investment income		6,673	250	6,923
Commission and other income		1,369	21,272	22,641
Losses on derivative financial instruments		(7,168)	-	(7,168)
Net claims expenses		(56,773)	-	(56,773)
Changes in policy liabilities		11,824	-	11,824
Other operating expenses		(31,967)	(16,576)	(48,543)
Profit before income tax		65,960	4,946	70,906
Net profit for the year		47,893	3,562	51,455
Transfer of capital (from)/to funds		(54,000)	54,000	-
Distributions made from funds	13	-	(58,000)	(58,000)

Note 18. Reconciliation of net cash provided by operating activities to net profit for the year

	2019 $'000	2018 $'000
Net profit for the year	52,806	51,455
Adjustments:		
Depreciation	18	16
Fair value gains on financial assets at fair value through profit or loss	(6,187)	(6,900)
Movement in payables due to related entities	216	47
Movement in reinsurance recoveries receivable	(2,649)	3,983
Movement in other assets	(174)	(33)
Movement in derivative financial instruments	7,205	477
Movement in current tax liabilities and deferred tax liabilities	3,558	1,087
Movement in claims reserve	1,748	7,027
Movement in policy liabilities	(32,566)	(11,824)
Movement in other liabilities	(1,048)	1,184
Net cash provided by operating activities	22,927	46,519

Notes to the financial statements

Note 19. Solvency reserves

The Board's policy is to maintain a strong capital base to meet the regulatory requirements. The IPSA requires the Company to comply at all times with the Solvency Standard for Life Insurance Business 2014 (**'Solvency Standard'**) issued by the RBNZ. The Directors have adopted a policy of holding a buffer amount of free capital over and above the minimum level of capital required by the Solvency Standard.

The IPSA requires disclosure of the solvency margins for the statutory fund, the business and assets outside the statutory fund and for the Company as a whole. These solvency margins as at 30 September are shown in the following tables.

	Statutory Fund No. 1 as at 30 September 2019 $'000	**Shareholder Fund as at 30 September 2019 $'000**	**Aggregate for all Funds as at 30 September 2019 $'000**
Actual Solvency Capital	**244,421**	**8,319**	**252,740**
Minimum Solvency Capital	**159,451**	**1,034**	**160,485**
Solvency Margin	**84,970**	**7,285**	**92,255**
Solvency Ratio	**153%**	**805%**	**157%**

	Statutory Fund No. 1 30 September 2018 $'000	Shareholder Fund 30 September 2018 $'000	Aggregate for all Funds 30 September 2018 $'000
Actual Solvency Capital (Audited)	229,306	8,219	237,525
Minimum Solvency Capital (Restated)	140,251[1]	946	141,197[1]
Solvency Margin (Restated)	89,055[1]	7,273	96,328[1]
Solvency Ratio (Restated)	163%[1]	869%	168%[1]

[1] During the current year, the Company revised its methodology with respect to the calculation of the Statutory Fund No. 1's Minimum Solvency Capital. The methodology change in turn impacts the Solvency Margin and Solvency Ratio. The Company's Actual Solvency Capital is not impacted by the methodology change. The change in methodology relates to the treatment of claims reserves which are now calculated on a net of reinsurance recoveries basis, rather than a gross basis, for the purpose of deriving the Policy Liability plus Other Liabilities (a component of the Minimum Solvency Capital calculation). This increased the Minimum Solvency Capital amounts by the value of reinsurance recoveries receivable. The Minimum Solvency Capital, Solvency Margin and Solvency Ratio for the 30 September 2018 comparative period have been restated accordingly. There was no impact to the statement of comprehensive income or the balance sheet in the current period or any prior periods. Refer to Note 21 with regard to the RBNZ's determination of non-compliance with the Solvency Standard in relation to the previous methodology.

The impact of the restatement for the 30 September 2018 comparative period is presented in the table below.

	Statutory Fund No. 1			Aggregate for all Funds		
	30 September 2018 Previously reported $'000	Increase/ (decrease) $'000	30 September 2018 Restated $'000	30 September 2018 Previously reported $'000	Increase/ (decrease) $'000	30 September 2018 Restated $'000
Minimum Solvency Capital	129,735	10,516	140,251	130,681	10,516	141,197
Solvency Margin	99,571	(10,516)	89,055	106,844	(10,516)	96,328
Solvency Ratio	177%	-14%	163%	182%	-14%	168%

The impact of the restatement on the Solvency Ratio for the 30 September 2015 to 2017 reporting periods is presented in the table below.

	30 September 2015 (Unaudited)		30 September 2016 (Unaudited)		30 September 2017 (Unaudited)	
Solvency Ratio (%)	Statutory Fund No. 1	Aggregate for all Funds	Statutory Fund No. 1	Aggregate for all Funds	Statutory Fund No. 1	Aggregate for all Funds
Previously reported	197%	205%	161%	166%	195%	201%
Increase/(decrease)	-19%	-20%	-10%	-10%	-21%	-22%
Restated	178%	185%	151%	156%	174%	179%

Note 20. Contingent assets, contingent liabilities and commitments

There were no contingent assets, contingent liabilities or unrecognised contractual commitments as at 30 September 2019 (30 September 2018: nil).

Westpac Life-NZ- Limited

Notes to the financial statements

Note 21. Subsequent events

On 2 October 2019, the RBNZ informed the Company that the methodology used to calculate the Statutory Fund No. 1's Minimum Solvency Capital was not in compliance with the Solvency Standard during the period from December 2014 to September 2018. In order to address the non-compliance, the RBNZ required that the Company disclose the non-compliance in these financial statements. As a result, the Statutory Fund No. 1's Solvency Ratio and Aggregate Solvency Ratio for these periods have been restated as presented in Note 19.

Note 22. Accounting policies relating to prior years

Due to the adoption of NZ IFRS 9, the accounting policies relating to the accounting for some financial instruments and related balances have changed. The policies applicable to the current year are provided in the relevant note to the financial statements above. As prior comparative years have not been restated, the accounting policies detailed below reflect the policies applicable to financial years prior to 2019 based on NZ IAS 39. Refer to Note 1 for further information.

Accounting policy relating to classification and measurement of financial instruments:

Classification and measurement of financial instruments (Note 1)

The Company classifies its financial assets into the following categories: financial assets at fair value through profit or loss, derivative financial instruments and loans and receivables. Financial assets at fair value through profit or loss relate to local authority securities, investment grade corporate bonds and units in unlisted unit trusts. Derivative financial instruments are classified as held for trading.

The Company classifies its financial liabilities into the following categories: financial liabilities at amortised cost and derivative financial instruments.

Financial assets and liabilities at fair value through profit or loss, including derivative financial instruments, are recognised initially at fair value. Loans and receivables and financial liabilities at amortised cost are carried at amortised cost using the effective interest rate method and are initially recognised at fair value plus directly attributable transaction costs. Realised and unrealised gains or losses arising from changes in the fair value of financial assets and liabilities at fair value through profit or loss and derivative financial instruments are included in profit or loss in the period in which they arise.

The Company's policies for determining the fair value of financial assets and financial liabilities are set out in Note 15.

Other assets (Note 1)

Other assets include commissions receivable under insurance agency arrangements and premiums due from policyholders. Commissions receivable are classified as loans and receivables.

Cash and cash equivalents (Note 14)

Cash and cash equivalents include cash at bank, at call money market deposits and other investments in highly liquid assets. Cash equivalents are short-term and highly liquid used in the day-to-day management of the Company that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents are brought to account at the face value or the gross value of the outstanding balance, where appropriate. They are accounted for as loans and receivables.

Accounting policy relating to impairment:

Impairment of financial assets (Note 1)

The following accounting policy applies to the impairment of financial assets carried at amortised cost.

The Company assesses at each balance date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment charges are recognised if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

If there is objective evidence that an impairment on loans and receivables has been incurred, the amount of the charge is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of a provision account and the amount of the loss is recognised in the statement of comprehensive income. If a financial asset has a variable interest rate, the discount rate for measuring any impairment is the current effective interest rate determined under the contract.

Westpac Life-NZ- Limited

Independent auditor's report

Independent auditor's report

To the shareholder of Westpac Life-NZ- Limited

We have audited the financial statements which comprise:

- the balance sheet as at 30 September 2019;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies.

Our opinion

In our opinion, the accompanying financial statements of Westpac Life-NZ- Limited (the Company), present fairly, in all material respects, the financial position of the Company as at 30 September 2019, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

Basis for opinion

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

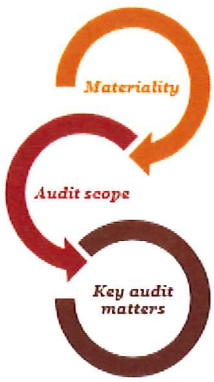
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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

Our firm carries out other assurance services for the Company over the solvency return. In addition, certain partners and employees of our firm may deal with the Company on normal terms within the ordinary course of trading activities of the Company. These matters have not impaired our independence as auditor of the Company.

Our audit approach

Overview



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

Overall materiality: $3,600,000, which represents approximately 5% of profit before tax.

We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Company is most commonly measured by users and is a generally accepted benchmark. The 5% is based on our professional judgement, noting that it is also within the range of commonly accepted profit before tax thresholds.

We have determined that there is one key audit matter:

- Valuation of policy liabilities

Materiality

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

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

Audit scope

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

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

Key audit matters

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

Key audit matter	How our audit addressed the key audit matter
Valuation of policy liabilities As at 30 September 2019 the Company has policy liabilities of $(141.7) million (30 September 2018: $(109.1) million), effectively in an asset position at balance date. The Directors' valuation of these balances involves complex and subjective judgements about future events, both internal and external to the business, for which small changes in assumptions can result in a material impact to the measurement of these balances. We considered this a key audit matter due to the subjective judgements made by the Directors around the key actuarial assumptions used in determining the balances. These key actuarial assumptions represent best estimate assumptions at reporting date and include: • The rate at which projected future cash flows are discounted; • The cost of providing benefits and administering these contracts; • Mortality, morbidity and trauma experience assumptions; and • Discontinuance experience, which affects the Company's ability to recover the cost of acquiring new business over the life of the contracts. Further, the Directors perform a liability adequacy test to ensure that any deficiencies in policy liabilities are appropriately recognised at the reporting date. This involves a comparison of the amount of policy liabilities against the estimated future cash flows calculated based on best estimate assumptions. Any deficiencies in the measurement of insurance policy liabilities are recognised through the statement of comprehensive income. Refer to the following notes in the Company's financial statements: Note 1(d) for critical accounting assumptions and estimates, Note 2 for actuarial assumptions and methods, and Note 10 for policy liabilities.	Together with PwC actuarial experts, we: • Assessed the reasonableness of the key actuarial assumptions. Our assessment of the assumptions included: – Obtaining an understanding of the controls in place to determine the assumptions; – Examining the approach used by management to derive the assumptions by applying our industry knowledge and experience; and – Challenging the key assumptions used by management against past experience, market observable data (as applicable) and our experience of market practice. • Assessed the valuation methodologies used by applying our industry knowledge and experience to compare whether the methodologies and changes to those are consistent with recognised actuarial practices and expectations derived from market experience. • Checked the calculation of the liability adequacy test and assessed the outcome in order to consider whether the policy liabilities are appropriate in the context of a valuation on best estimate assumptions at reporting date. Policy data is a key input to the actuarial estimates. Accordingly, we tested: • The completeness and accuracy of data between source and actuarial valuation systems; and • A sample of premiums received to confirm that they were supported by appropriate documentation. We have no matters to report from the procedures performed.

Information other than the financial statements and auditor's report

The Directors are responsible for the annual report. Our opinion on the financial statements does not cover the other information included in the annual report and we do not express any form of assurance conclusion on the other information.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the financial statements

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

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

Auditor's responsibilities for the audit of the financial statements

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

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

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

This description forms part of our auditor's report.

Who we report to

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

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

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
24 January 2020

Auckland

The Directors
Westpac Life-NZ-Limited
Westpac on Takutai Square
16 Takutai Square
Auckland 1010

Appointed Actuary's Report

This report has been prepared for the directors of Westpac Life-NZ-Limited (**Westpac Life**) under section 78 of the Insurance (Prudential Supervision) Act 2010 (the **Act**).

In my capacity as Appointed Actuary to Westpac Life, I have reviewed the actuarial information contained in, or used in the preparation of, the financial statements of Westpac Life for the year ended 30 September 2019 (**financial statements**). For the purposes of this report "actuarial information" has the meaning given to it in section 77(4) of the Act, supplemented by paragraph 139 of the Solvency Standard for Life Insurance Business 2014 issued by the Reserve Bank of New Zealand (**Solvency Standard**).

My review has included the review and resetting of the best estimate assumptions which are used for valuation purposes, the review of the valuation results as at 30 September 2019, and the review of the solvency calculations and solvency return for Westpac Life as at 30 September 2019. It is Westpac Life's established policy to seek my advice in respect of actuarial information and to adopt that advice in Westpac Life's financial statements.

My review has been carried out in accordance with the relevant Professional Standards issued by the New Zealand Society of Actuaries, and the Solvency Standard.

I have obtained all the information and explanations that I have required from Westpac Life in relation to my review. My review is dependent upon the accuracy of the policy data upon which the policy valuations have been based. Whilst there are a small number of individual policies with erroneous data, in my opinion the policy data as at 30 September 2019 is satisfactory for the purposes of valuing Westpac Life's policy liabilities. There were no limitations placed upon the scope of my review.

In my opinion, and from an actuarial perspective:

(i) the actuarial information contained in the financial statements has been appropriately included in those statements;

(ii) the actuarial information used in the preparation of the financial statements has been used appropriately; and

(iii) as at 30 September 2019, Westpac Life was maintaining a solvency margin within each of the Westpac Life-NZ-Limited Statutory Fund No. 1 and the Westpac Life-NZ-Limited Shareholder Fund, and for Westpac Life as a whole, that would comply under the Solvency Standard.

In my role as Appointed Actuary to Westpac Life, I am an employee of Westpac New Zealand Limited, a related company of Westpac Life. My remuneration and employee benefits are paid by Westpac New Zealand Limited and then reimbursed by Westpac Life. I was a director of Westpac Life prior to 31 July

2012 and I am currently a director of Westpac Life's appointed investment manager, BT Funds Management (NZ) Limited. I hold shares and options in Westpac Banking Corporation, the ultimate holding company of Westpac Life. I am a member of the Westpac New Zealand Staff Superannuation Scheme and a Westpac appointed director of the trustee company for the Westpac New Zealand Staff Superannuation Scheme, the trustee of which holds a group life insurance policy with Westpac Life. I maintain certain personal general insurance policies with IAG New Zealand Limited through the Westpac / IAG agency managed by Westpac Life.

This report is provided solely in my capacity as Westpac Life's Appointed Actuary. To the fullest extent permitted by law, I do not accept responsibility to anyone for the contents of this report, other than the Reserve Bank of New Zealand, Westpac Life, its directors and shareholder.

Ian New
Fellow of the New Zealand Society of Actuaries
Appointed Actuary, Westpac Life-NZ-Limited

24 January 2020