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ZURICH AUSTRALIAN INSURANCE LIMITED

A.B.N. 13 000 296 640

ANNUAL REPORT

For the year ended 31 December 2010

Contents **Page Number**

Zurich Australian Insurance Limited is a company limited by shares, incorporated in and domiciled in Australia. Its registered office and principal place of business is:

5 Blue Street
North Sydney
NSW 2060

A description of the nature of the entity's operations and its principal activities is included in the directors' report on pages 1 – 4.

The annual report was authorised for issue by the directors on 30 March 2011. The Directors have the power to amend and reissue the report.

ZURICH AUSTRALIAN INSURANCE LIMITED

Directors' Report

Your directors present their report on Zurich Australian Insurance Limited ("the Company") for the year ended 31 December 2010.

Directors
The following persons were directors of the Company during the whole of the financial year and up to the date of this report:

Terence John Paradine (Chairman)
David James Parker Smith
Ian Clifton Carroll
Robert Olivier Dolk

The following persons were directors of the Company for part of the financial year or at the date of this report:

Philip Wallace Smith was a director of the Company from the beginning of the financial year until his resignation on 15 July 2010.

Robert Joseph Lehane was an alternate director of the Company from the beginning of the financial year until his resignation on 1 April 2010.

Iain Campbell Howie was appointed as an alternate director of the Company on 1 April 2010 until his resignation on 12 November 2010.

Michael Ronald Vos and James Richard Sykes were appointed as directors of the Company on 15 July 2010 and continue in this office at the date of this report.

Dirk Jan Celina De Nil was appointed as a director of the Company on 15 July 2010 until his resignation on 5 November 2010.

Officers
Cathy Anne Manolios and David George Hallahan were company secretaries of the Company during the whole of the financial year and up to the date of this report.

Principal Activities
The principal activity of the Company during the year was underwriting various classes of General Insurance.

Dividends
Dividends paid by the Company to the Australian parent company, Zurich Financial Services Australia Limited, during the financial year were as follows:

	2010 $'000	2009 $'000
Interim ordinary dividend paid on 29 March 2010	67,500	-
Final ordinary dividend paid on 23 December 2009	-	16,000

ZURICH AUSTRALIAN INSURANCE LIMITED

Directors' Report *(continued)*

Review of Results and Operations

A summary of revenues and results is set out below:

	2010	2009
Revenues and other income	$'000	$'000
Direct premium and inwards reinsurance revenue	1,060,630	1,021,664
Reinsurance and other recoveries	423,365	309,567
Investment income	112,094	95,222
Other income	5,828	7,734
	1,601,917	1,434,187
Results		
Profit for the year	34,735	105,275

All the administrative activities of the Company were performed by its Australian parent entity, Zurich Financial Services Australia Limited. The Company has been charged management service fees of $160,556,563 (2009: $152,057,243) in respect of these activities.

Significant Changes in the State of Affairs
There is no significant change in the state of affairs of the Company during the financial year.

Matters Subsequent to the End of the Financial Year
Subsequent to the end of the financial year, there have been a number of catastrophes which will impact the Company's 2011 results. Refer to Note 30 of the annual report for details.

Apart from this, there is no matter or circumstance which has arisen since 31 December 2010, other than dealt with in the financial statements, that has significantly affected or may significantly affect:

a) the operations in future financial years; or
b) the results of those operations in future financial years; or
c) the state of affairs in future financial years.

Likely Developments and Expected Results of Operations
The directors do not make any reference to likely developments and expected results at this time, apart from comments made elsewhere in this report, as such references could be prejudicial to the interests of policyholders and shareholders. Accordingly, this information has not been included in this report.

Environmental Regulations
The Company has assessed whether there are any particular or significant environmental regulations which apply to it and has determined that there are none.

Insurance of Officers
During the financial year, a related company has paid a premium to insure all present and past directors, secretaries and executive officers of the Company or a related body corporate. The insurance grants indemnity against liabilities permitted to be indemnified by the Company under the Corporations Act 2001. In accordance with normal commercial practice, the insurance policy prohibits disclosure of the terms of the policy including the nature of the liability insured against and the amount of the premium.

ZURICH AUSTRALIAN INSURANCE LIMITED

Directors' Report ***(continued)***

Agreements to indemnify
The Company's constitution provides that the Company may indemnify, to the extent permitted by law, past and present directors and secretaries against any liability incurred as an officer of the Company or any subsidiary of the Company together with legal costs incurred in defending an action for such a liability.

The Company has also entered into various agreements with persons who are current and former officers of the Company and of certain of the Company's related companies. These agreements variously require the Australian parent entity, Zurich Financial Services Australia Limited to indemnify those persons, to the extent permitted by the Corporations Act 2001, against liabilities, some claims and legal costs which they may incur or which are made against them in connection with their position or conduct as officers of the Company and its related companies. The indemnities provided under those agreements are not limited in amount.

Proceedings on Behalf of the Company
No person has applied to the Court under section 237 of the Corporations Act 2001 for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the Company with leave of the Court under section 237 of the Corporations Act 2001.

Rounding of Amounts to the Nearest Thousand Dollars
The Company is a kind referred to in Class Order 98/0100 issued by the Australian Securities and Investments Commission, relating to the "rounding off" of amounts in the Directors' Report and Financial Report. Amounts in the Directors' Report and Financial Report have been rounded off to the nearest thousand dollars in accordance with that Class Order.

Auditor
PricewaterhouseCoopers continues in office in accordance with section 327 of the Corporations Act 2001. A copy of the Auditors' Independence Declaration as required under section 307C of the Corporation Act 2001, is set out on page 4.

This report is made in accordance with a resolution of the directors.

T J Paradine Director	R O Dolk Director

Sydney
30 March 2011

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Auditor's Independence Declaration

As lead auditor for the audit of Zurich Australian Insurance Limited for the year ended 31 December 2010, I declare that to the best of my knowledge and belief, there have been:

a) no contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Zurich Australian Insurance Limited during the period.

V. Papageorgiou

Voula Papageorgiou
Partner
PricewaterhouseCoopers

Sydney
30 March 2011

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ZURICH AUSTRALIAN INSURANCE LIMITED

Statement of Comprehensive Income
For the year ended 31 December 2010

	Notes	2010 $'000	2009 $'000
Premium revenue			
Direct premium revenue	5 (c)	1,048,300	998,802
Inwards reinsurance revenue		12,330	22,862
Outwards reinsurance expense		(255,484)	(241,170)
Net premium revenue		805,146	780,494
Claims expense	8	(995,014)	(787,479)
Reinsurance and other recoveries revenue	8	423,365	309,567
Net claims incurred	8	(571,649)	(477,912)
Gross movement in unexpired risk liability		(8,495)	29,752
Reinsurance recoveries on unexpired risk liability		13,104	(15,075)
Net movement in unexpired risk liability		4,609	14,677
Acquisition costs		(79,168)	(69,318)
Other underwriting expenses		(204,491)	(191,702)
Underwriting expenses		(283,659)	(261,020)
Underwriting result		(45,553)	56,239
Investment income	6	112,094	95,222
Other income	7	5,828	7,734
Net foreign exchange loss		(1,456)	(2,163)
Profit before income tax		70,913	157,032
Income tax expense	9 (a)	(36,178)	(51,757)
Profit for the year	24	34,735	105,275
Other comprehensive income			
Exchange difference on translating foreign operation	24(b)	604	484
Other comprehensive income for the year, net of tax		604	484
Total comprehensive income for the year		35,339	105,759

The above Statement of Comprehensive Income should be read in conjunction with the accompanying notes.

ZURICH AUSTRALIAN INSURANCE LIMITED

Balance sheet
As at 31 December 2010

	Notes	2010	2009
		$'000	$'000
Assets			
Cash and cash equivalents	10	200,637	131,530
Receivables	11	346,727	351,388
Financial assets at fair value through profit or loss	12	1,667,923	1,642,500
Reinsurance and other recoveries	13	924,144	675,158
Deferred acquisition costs	14	41,549	32,149
Other assets	15	190,001	141,739
Deferred tax asset	16	33,143	49,447
Total Assets		3,404,124	3,023,911
Liabilities			
Payables	17	160,963	112,015
Provisions	18	10,769	9,296
Unearned premium	19	645,721	568,255
Unexpired risk liability	20(a)	36,276	28,260
Outstanding claims	21(a)	1,939,755	1,663,284
Total Liabilities		2,793,484	2,381,110
Net Assets		610,640	642,801
Equity			
Contributed equity	22(a)	97,065	97,065
Reserves	23(a)	1,140	536
Retained profits	23(c)	512,435	545,200
Total Equity		610,640	642,801

The above Balance Sheet should be read in conjunction with the accompanying notes.

ZURICH AUSTRALIAN INSURANCE LIMITED

Statement of Changes in Equity
As at 31 December 2010

	Contributed Equity $'000	Reserves $'000	Retained profits $'000	Total $'000
Balance at 1 January 2009	97,065	52	455,925	553,042
Total comprehensive income for the year	-	484	105,275	105,759
Transactions with owners in their capacity as owners:				
Dividends paid to Australian parent entity	-	-	(16,000)	(16,000)
Balance as at 31 December 2009	97,065	536	545,200	642,801
Total comprehensive income for the year	-	604	34,735	35,339
Transactions with owners in their capacity as owners:				
Dividends paid to Australian parent entity	-	-	(67,500)	(67,500)
Balance as at 31 December 2010	97,065	1,140	512,435	610,640

The above Statement of Changes in Equity should be read in conjunction with the accompanying notes.

ZURICH AUSTRALIAN INSURANCE LIMITED

Cash flow statement
For the year ended 31 December 2010

	Notes	2010 $'000	2009 $'000
Cash Flows from Operating Activities			
Premiums and deposits received		821,119	762,209
Claims and related payments		(531,539)	(526,186)
Payment to suppliers and employees		(255,230)	(238,744)
Proceeds from sale of investment assets		95,082	186,116
Payments for purchase of investment assets		(96,250)	(241,444)
Interest received		2,212	1,567
Fees and commissions received		5,088	5,858
Payment to head tax entity		(9,330)	(1,806)
Other income received		-	81
Other expense paid		(148)	-
Dividends received		88,303	91,737
Net cash inflows from operating activities	25	119,307	39,390
Cash Flows from Financing Activities			
Dividends paid		(50,200)	(16,000)
Net cash outflows from financing activities		(50,200)	(16,000)
Net Increase in Cash Held		69,107	23,390
Cash and cash equivalents at the beginning of the financial year		131,530	108,140
Cash and cash equivalents at the end of the financial year	10	200,637	131,530

The above Cash Flow Statement should be read in conjunction with the accompanying notes.

1. Summary of significant accounting policies

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

It is prepared in accordance with the historical cost convention, except in the case of certain financial assets, as noted in the accounting policies below, which are measured on the basis of fair value as required by AASB 139: *Financial Instruments: Recognition and Measurement*, and provisions for long-tail outstanding claims which have been inflated and discounted as required by AASB 1023: *General Insurance Contracts*.

Compliance with IFRSs

The financial statements of Zurich Australian Insurance Limited also comply with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB).

The Company has elected to apply AASB 127 *Consolidated and Separate Financial Statements*. These financial statements are separate financial statements and the Company is exempted from preparing consolidated financial statements. The ultimate Australian parent company, Zurich Financial Services Australia Limited (incorporated in Australia) produces consolidated financial statements in accordance with IFRSs produced for public use, which can be obtained at 5 Blue Street, North Sydney, NSW, 2060.

The Company has elected to apply AASB 8 *Operating Segments*. The Company does not issue any publicly traded debt or equity instruments and is exempted from the disclosure of reportable segments.

Controlled entities

Controlled entities are all those entities over which the Company has the power to govern the financial and operating policies, generally accompanying a shareholder of more than one-half of the voting rights. A list of controlled entities is summarised in Note 28.

Critical accounting estimates

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 2 and 3.

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

(a) Principles of General insurance contracts

The general insurance operations of Zurich Australian Insurance Limited (ZAIL) comprise the underwriting of various classes of direct and reinsurance contracts. These contracts transfer significant insurance risk by agreeing to compensate the insured or reinsured on the occurrence of a specified insured event, such as damage to property or the crystallisation of a third party liability (or the reinsurance thereof), within a given timeframe.

These contracts are defined as general insurance contracts.

(b) Insurance premium and related revenue

Direct and inwards reinsurance premium comprises amounts charged to the policyholders or other insurers, including fire service levies in Australia, but excluding stamp duties, Goods and Services Tax (GST), fire service levies in New Zealand and other amounts collected on behalf of third parties. Inwards reinsurance is insurance contracts entered into by the Company under which the contract holder is another insurer. The earned portion of premiums received and receivable, including bound but not incepted and unclosed business, is recognised as revenue. Premium revenue is treated as earned from the date of attachment of risk. Premiums on unclosed business are brought to account by reference to the previous year's premium processing delays, with due allowance for any changes in the pattern of new business and renewals.

The pattern of recognition of income over the policy or indemnity periods is based on time, which closely approximates the pattern of risks underwritten. The proportion of premiums received and receivable not earned in the Statement of Comprehensive Income at the reporting date is recognised in the Balance Sheet as an unearned premium liability. The unearned portion of commissions and other acquisition costs are also deferred and shown as deferred acquisition costs in the Balance Sheet.

(c) Fee and other revenue

Fee and other revenue are recognised at the time services are provided.

(d) Dividend and interest income

Interest income is recognised in the Statement of Comprehensive Income using the effective interest rate method.

Dividends are recognised when the Company obtains control of the right to receive the revenue. This applies even if they are paid out of pre-acquisition profits. However, the investment may need to be tested for impairment as a consequence, refer to Note 1(o).

(e) Insurance claims and related expenses

Claims expense represents payment for claims (and claims related expenses) and the movement in outstanding claims liabilities.

(f) Outwards reinsurance expense

Amounts paid to reinsurers under insurance contracts held by the Company are recorded as outwards reinsurance expense and are recognised in the Statement of Comprehensive Income from the attachment date over the period of indemnity of the reinsurance contract in accordance with the expected pattern of the incidence of the risk ceded. Accordingly, a portion of outwards reinsurance expense is treated as a prepayment and presented as deferred outward reinsurance expense in other assets on the balance sheet as at reporting date.

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

(g) Income tax
The income tax expense or benefit for the period is the tax payable/receivable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and unused tax losses.

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

Deferred tax assets and liabilities are recognised using the liability method for temporary differences at the tax rates expected to apply when the assets are recovered or liabilities are settled, based on those tax rates which are enacted or substantively enacted. The relevant tax rates are applied to the cumulative amounts of deductible and taxable temporary differences to measure the deferred tax asset or liability. An exception is made for certain temporary differences arising from the initial recognition of an asset or liability. No deferred tax asset or liability is recognised in relation to these temporary differences if they arose in a transaction, other than a business combination, that at the time of the transaction did not affect either accounting profit or taxable profit or loss.

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

Deferred tax liabilities and assets are not recognised for temporary differences between the carrying amount and tax bases of investments in controlled entities where the Company is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

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

Tax consolidation legislation
The Company is part of a tax consolidated group, of which ZCM Asia Holdings Pty Limited is the head entity, and which has implemented the tax consolidation legislation as of 1 October 2003.

The head entity, ZCM Asia Holdings Pty Limited and the entities in the tax consolidated group (including the Company) continue to account for their own current and deferred tax amounts. These tax amounts are measured on a basis approximating the basis as if each entity in the tax consolidated group was a separate taxpayer within that group.

In addition to its own current and deferred tax amounts, ZCM Asia Holdings Pty Limited also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from entities in the tax consolidated group.

Assets or liabilities arising under the tax funding agreement with the tax consolidated entities are recognised as amounts receivable from or payable to other entities in the group.

Any difference between the amounts assumed and amounts receivable or payable under the tax funding agreement are recognised as a contribution to (or distribution from) tax consolidated entities. For further details see income tax Note 9.

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

(h) Goods and Services Tax (GST)

Revenues, expenses and assets, liabilities are disclosed net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Tax Office (ATO). In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or current liability in the Balance Sheet.

Cash flows are included in the Cash Flow Statement on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

(i) Fire brigade and other statutory charges

A liability for fire brigade and other statutory charges is recognised on business written to the balance date. Levies and charges payable are expensed on the same basis as the recognition of premium revenue, with the portion relating to unearned premium being recorded as a prepayment.

(j) Foreign currency translation

The financial statements of the Company are presented in Australian dollars, which is the functional and presentation currency. Foreign currency transactions are initially translated into Australian dollars at the rate of exchange at the date of the transaction. At balance date, amounts payable and receivable in foreign currencies are translated into Australian dollars at rates of exchange current at that date. Resulting exchange differences are brought to account in determining the profit or loss for the year.

The results and financial position of foreign operations are translated into the presentation currency as follows:

- Assets and liabilities at closing rate at balance date.
- Income and expenses at average exchange rate.
- All resulting exchange differences are recognized as a separate component of equity.

(k) Cash and cash equivalents

For the purpose of the Cash Flow Statement, cash includes cash at bank and short term unit trusts investment which are readily convertible to cash on hand and are subject to an insignificant risk of changes in value, net of outstanding bank overdrafts.

(l) Financial assets

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

The Company assesses at each balance date whether there is objective evidence that a financial asset or group of financial assets is impaired.

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

The investment assets of the Company have been determined as being assets backing policy liabilities and are therefore valued at fair value through profit or loss.

It is considered that the use of fair value through profit or loss results in more relevant information because it eliminates or significantly reduces a measurement or recognition inconsistency.

Summary of significant accounting policies *(continued)*

(l) Financial assets *(continued)*

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Company establishes fair value by using valuation techniques. These include reference to the fair values of recent arm's length transactions, involving the same instruments or other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

Purchases and sales of investments are recognised on trade-date – the date on which the Company commits to purchase or sell the asset. Financial assets are initially recognised at cost. These assets are subsequently measured at fair value. Realised, unrealised gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the Statement of Comprehensive Income in the period in which they arise.

Financial assets are derecognised when the right to receive cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

(ii) Receivables

Receivables are carried at cost which is the best estimate of fair value, as they are usually settled within twelve months and subsequently subject to impairment testing. Impairment testing is based on collectibility of receivables and is reviewed on an ongoing basis. An impairment charge is recognised when there is objective evidence that the entity will not be able to collect all amounts due according to the original terms of the contracts. The impairment charge is recognised in the Statement of Comprehensive Income.

(m) Reinsurance and other recoveries receivable

Reinsurance and other recoveries receivable on insurance paid claims, reported claims not yet paid, claims incurred but not reported (IBNR), claims incurred but not enough reported and unexpired risk liabilities are recognised as revenue. Recoveries receivable are assessed in a manner similar to the assessment of outstanding claims. Recoveries receivable in relation to long-tail classes are measured as the present value of the expected future receipts, calculated on the same basis as the liability for outstanding claims to which they relate.

(n) Deferred acquisition costs

The fixed and variable costs of acquiring new business, "the acquisition costs", include commission, advertising, policy issue and underwriting costs, agency expenses and other sales costs.

A portion of acquisition costs relating to unearned premium revenue is deferred and recognised as an asset, where it can be reliably measured and where it is probable that it will give rise to premium revenue that will be recognised in the Income Statement in future periods. Deferred acquisition costs are measured at the lower of cost and recoverable amount and are amortised in accordance with the earning pattern of the corresponding premium revenue.

(o) Impairment of assets

Financial assets measured at fair value, where changes in value are reflected in the Statement of Comprehensive Income, are not subject to impairment testing. Other assets such as receivables are subject to impairment testing.

Assets that have an indefinite useful life, such as identifiable intangible assets, are not subject to amortisation and are tested at least annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of an asset exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value (including realisation costs) and its value in use.

(p) Payables

These amounts represent liabilities for goods and services provided to the Company prior to the end of the financial year and which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

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

(q) Provisions

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are not recognised for future operating losses.

(r) Dividends

Provision is made for the amount of any dividend declared on or before the end of the financial year but not distributed at balance date.

(s) Outstanding claims

The liability for outstanding claims is measured as the central estimate of the present value of expected future claim payments at the reporting date under general insurance contracts issued by the Company, with an additional risk margin to allow for the inherent uncertainty in the central estimate.

The expected future payments include those in relation to claims reported but not yet paid, claims incurred but not reported (IBNR), claims incurred but not enough reported (IBNER) and their associated allocated costs as well as anticipated claims handling costs.

Claims handling costs include those costs that can not be directly associated with individual claims, such as claims administration costs.

The expected future payments are discounted to present value using a risk free rate.

(t) Unexpired risk liabilities

At each reporting date the Company assesses whether the unearned premium liability is sufficient to cover all expected future cash flows relating to future claims against current insurance contracts. This assessment is referred to as the liability adequacy test and is performed separately for each group of contracts subject to broadly similar risks and managed together as a single portfolio.

If the present value of the expected future cash flows relating to future claims plus the additional risk margin to reflect the inherent uncertainty in the central estimate exceeds the unearned premium liability less related intangible assets and related deferred acquisition costs then the unearned premium liability is deemed to be deficient. The Company applies a risk margin to achieve the same probability of sufficiency for future claims as is achieved by the estimate of the outstanding claims liability, see Note 3.

A write down to recoverable amount is recognised when the present value of expected future claims (including settlement costs) in relation to business written to the reporting date exceeds related unearned premium revenue. The entire deficiency, gross and net of reinsurance, is recognised immediately in the income statement. The deficiency is recognised first by writing down any related intangible assets and then related deferred acquisition costs, with any excess being recorded in the Balance Sheet as an unexpired risk liability.

(u) Rounding of amounts

The Company is a kind referred to in Class Order 98/0100 issued by the Australian Securities and Investments Commission, relating to the "rounding off" of amounts in the financial report. Amounts in the financial report have been rounded off to the nearest thousand dollars in accordance with that Class Order.

(v) Comparative information

Where necessary, the amounts shown for the previous year have been reclassified to facilitate comparison.

2. Critical accounting judgements and estimates

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

It has been determined that no critical accounting judgements have been made in the year.

(a) The ultimate liability arising from claims made under insurance contracts

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

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

The estimation of claims incurred but not reported ('IBNR') is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Company, where information about the claim event is generally available. IBNR claims may not be apparent to the insured until many years after the events giving rise to the claims has happened. The long-tailed classes of business will typically display greater variations between initial estimates and final outcomes because there is a greater degree of difficulty in estimating IBNR reserves. For the short-tailed classes, claims are typically reported soon after the claim event, and hence tend to display lower levels of volatility. In calculating the estimated cost of unpaid claims the Company uses a variety of estimation techniques, generally based upon statistical analyses of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in the Company's processes which might accelerate or slow down the development and/or recording of paid or incurred claims, compared with the statistics from previous periods
- changes in the legal environment
- the effects of inflation (both economic/wage and superimposed)
- changes in the mix of business
- the impact of large losses
- movements in industry benchmarks
- medical and technological developments
- changes in policyholder behaviour

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

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

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

Provisions are calculated gross of any reinsurance and non-reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable based upon the gross provisions.

Details of specific assumptions used in deriving the outstanding claims liability at year end are detailed in Note 3.

2. Critical accounting judgements and estimates *(continued)*

(b) Assets arising from reinsurance contracts

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

3. Actuarial assumptions and methods

The Company writes both short-tailed and long-tailed business. The process for determining the value of outstanding claims liabilities including the cost of claims handling is described below.

Case estimates are established by individual claims officers. The provision for large losses is reviewed by senior claims managers. The ultimate undiscounted cost of claims by year of accident and line of business is then established by actuaries using a variety of statistical bases at a line of business level. IBNR is then derived by subtracting from the ultimate cost, the amount of paid claims and case reserves. The estimation of IBNR is subject to a greater degree of uncertainty than the estimate of the cost of settling claims already notified and the estimate of the ultimate cost of long-tail lines is generally more uncertain than the estimate for short-tail lines where claims are often reported and settled within 1 year of occurrence.

The methods used to establish the ultimate cost of claims include the following:

- Projecting ultimate numbers of claims and multiplying by projected ultimate average cost
- Projecting ultimate claim payments
- Projecting ultimate incurred claim amounts
- Applying plan loss ratios to earned premiums

Claims inflation is incorporated into the resulting projected payments, to allow for both general economic/wage inflation as well as any superimposed inflation detected in the modelling of payments experience. Superimposed inflation arises from non-economic factors such as legal developments. Future wage inflation is based on current levels and economic indicators. Future superimposed inflation is assessed based on current trends and industry information.

Projected reinsurance assets are derived using similar methods or applying net to gross ratios.

Projected payments are discounted to allow for the time value of money, based on current Commonwealth Government interest rates.

All these methods rely on future development being consistent with historical development and are thus subject to uncertainty surrounding changes to these patterns from whatever cause. In addition, there is uncertainty arising from the underlying assumptions for future wage inflation and superimposed inflation and of discount rates. Significant events, such as catastrophes, close to the balance sheet date also increase the level of uncertainty. The presence of asbestos claims in the portfolio and the potential emergence of new types of latent claim also increase the potential variability of the outcome.

For these reasons a risk margin is added to the central estimate established above. The establishment of the risk margin takes into account the variability of the outcome of each line of business and the diversification benefit of writing a number of lines of business. The Board and Management have decided that the level of risk margin shall be established to provide a probability of adequacy of 85%. (2009: 85%).

3. Actuarial assumptions and methods *(continued)*

(a) Selected key variables

The following indicators reflect the key variables that have been used in determining the outstanding claims liabilities.

	2010	2010	2009	2009
	Long-tail	Short-tail	Long-tail	Short-tail
Average weighted term to settlement	3.7 years	0.4 years	3.9 years	0.5 years
Discount rate	4.21%	N/A	4.48%	N/A
Wage inflation	4.00%	N/A	4.00%	N/A
Superimposed inflation	0 to 5.5%	N/A	0 to 5.5%	N/A

(b) Sensitivity analysis – insurance contracts

The Company conducts sensitivity analysis to quantify the exposure to risk of changes in the key underlying variables. The valuations included in the reported results are calculated using certain assumptions about these variables as disclosed above. The movement in any key variable will impact the performance and equity of the Company. The tables below give an analysis of the sensitivity of the profit/(loss) and equity, to changes in these assumptions both gross and net of reinsurance.

Impact of changes in key variables

December 2010		**Profit/(loss)**		
		Gross of reinsurance $'000	**Net of reinsurance** $'000	**Equity** $'000
Recognised amounts per the financial statements		(91,954)	34,375	610,640
Variable	**Movement in variable**		**Adjusted amounts**	
Long-tail				
Average weighted term to settlement - years	0.5	(70,981)	50,950	624,216
	-0.5	(109,208)	24,363	597,629
Discount rate	1%	(70,156)	50,799	624,065
	-1%	(112,552)	22,546	595,812
Wage inflation and superimposed inflation rates	1%	(114,859)	22,093	595,359
	-1%	(70,293)	51,740	625,006
Financial assets				
Shift in Yield Curve	1%	(125,958)	3,371	576,637
	-1%	(57,950)	71,379	644,645
Equity Prices	20%	(84,484)	44,845	618,111
	-20%	(99,424)	29,905	603,171

3. Actuarial assumptions and methods *(continued)*

(b) Sensitivity analysis –insurance contracts *(continued)*

December 2009		**Profit/(loss)**		
		Gross of reinsurance $'000	**Net of reinsurance** $'000	**Equity** $'000
Recognised amounts per the financial statements		*67,949*	*105,275*	642,801
Variable	**Movement in variable**		**Adjusted amounts**	
Long-tail	0.5	85,893	117,382	654,908
Average weighted term to settlement – years	-0.5	52,413	94,990	632,516
	1%	90,233	119,869	657,395
Discount rate	-1%	46,111	91,021	628,547
	1%	43,730	89,363	626,889
Wage inflation and superimposed inflation rates	-1%	90,848	120,233	657,759
Financial assets	1%	42,345	79,671	617,197
Shift in Yield Curve	-1%	93,553	130,879	668,405
	20%	81,328	118,654	656,180
Equity Prices	-20%	54,570	91,896	629,422

4. Financial risk management policies and procedures

The Company's activities expose it to a variety of financial risks; market risk (including currency risk), credit risk and liquidity risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Company.

Risk management controls are outlined in the Company's Risk Management Strategy (RMS). The objective of the RMS is to provide a summary of the policies and controls in place to address enterprise risks including certain operational and financial risks and the procedures for assessing compliance with these policies and controls. In addition, the Group's 'Zurich Risk Policy' (ZRP) provides constraints on the mix of investment assets. The Company has delegated its investment management responsibilities to Zurich Investment Management Limited (ZIM), which has in turn negotiated Investment Management Agreements (IMA) with external investment managers, with all funds managed in accordance with these IMA's. The overall investment strategy (and in particular the use of derivatives) is governed by the Zurich Investment Series Consolidated Constitution, the relevant IMA's, and the relevant funds offer documents and Product Disclosure Statements. The use of derivatives is consistent and subordinate to the investment strategy of each of the funds.

The RMS is subject to at least an annual review by the Internal Audit Department. The Internal Audit Department is independent of the day to day operational management of the Company. The Internal Audit Department prepares a report on compliance with the procedures outlined in the RMS.

The following list of factors are considered and addressed as part of the Company's financial risk management policies and procedures.

(a) Market risk

Market risk is the risk of diminution in value of the Company's investment portfolio arising from adverse movements in the levels and volatility of interest rates, foreign exchange rates and equity prices. The risk is minimised by restricting the proportion of assets allowed to be invested in 'real' assets such as equities and property, by restricting the amount of foreign currency exposure and by ensuring that asset and liability term mismatch is controlled. These constraints are all specified in the ZRP. The risk is then controlled by ensuring that all activities are transacted in accordance with approved mandates and by robust and regular monitoring. Market risk analysis is conducted on a regular basis and risk management controls ensure that positions are monitored against the portfolio risk limits. Market risk analysis is conducted on a total portfolio basis, incorporating both physical investments and the effective exposure of all derivative positions. Separate analysis is also performed on derivative positions in isolation.

Refer Note 3 (b) for an analysis of the impact of changes in key assumptions on reported profit and equity of the company. The analysis includes the impact of changes on financial assets.

(b) Net fair value of financial assets and liabilities

On-Balance Sheet

The aggregate carrying values of financial assets and financial liabilities approximate their net fair values. The methods used to determine the carrying values of financial assets and liabilities are included in the Summary of significant accounting policies at Note 1.

Off-Balance Sheet

The Company has potential financial liabilities which may arise from certain contingencies disclosed in Note 26. No material losses are anticipated in respect of any of those contingencies, and the net fair value of those contingencies is assessed as an immaterial amount.

4. Financial risk management policies and procedures *(continued)*

(c) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Apart from reinsurance, the Company has no significant concentrations of credit risk. Where entities have a right of set-off and intend to settle on a net basis, this set-off has been reflected in the financial statements in accordance with accounting standards.

Reinsurance security is monitored continuously taking advantage of the Group's Security Committee analyses and there are strict controls around the use of individual reinsurers. Reinsurance accumulations are also monitored closely and used in deciding the appropriate placement programme at renewal.

With the exception of investments in associates, controlled entities and a NZD500,000 NZ Government bond, the Company does not hold listed equity or debt securities. Instead it gains exposure to these assets by investing in Unit Trusts. The Trusts invest substantially in securities traded in an active market and are priced daily. These investments are disclosed in Note 10 and Note 12 and are not rated by any credit rating agency.

Standard and Poors (S&P) rating for Cash at bank disclosed in Note 10 is AA (2009:AA).

The premiums receivable disclosed in Note 11 include amounts past due but not impaired which are analysed below.

	2010 $'000	2009 $'000
< 30 days	54,409	26,049
31 – 90 days	3,499	1,120
> 91 days	9,867	5,708
Total premiums receivable past due but not impaired	67,775	32,876

Refer Note 5(f) for information on credit quality of reinsurance assets.

All other receivables do not include material amounts that are either past due or impaired.

(d) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close-out market positions.

The risk is controlled by carefully monitoring cash flow, and maintaining suitable floats of readily realisable assets.

The table shows expected cash flows from outstanding claims (notified claims) and unearned premium liability (expected future claims). Both are net of reinsurance and non-insurance recoveries and before risk margin.

4. Financial risk management policies and procedures *(continued)*

d) Liquidity risk *(continued)*

2010	Carrying amount (Undiscounted)	Expected cash flows (undiscounted)				
		0-1 yrs	1-5 yrs	5-10 yrs	10-15 yrs	>15yrs
	$'000	$'000	$'000	$'000	$'000	$'000
Insurance contracts						
Outstanding Claims (Note 13, 21)	1,070,229	454,920	479,223	74,231	18,642	43,214
Premium Liability	372,455	165,283	173,868	32,560	691	52
Total	1,442,684	620,203	653,091	106,791	19,333	43,266

2009	Carrying amount (Undiscounted)	Expected cash flows (undiscounted)				
		0-1 yrs	1-5 yrs	5-10 yrs	10-15 yrs	>15yrs
	$'000	$'000	$'000	$'000	$'000	$'000
Insurance contracts						
Outstanding Claims (Note 13, 21)	1,028,106	397,626	481,548	83,903	19,187	45,842
Premium Liability	347,281	157,516	158,187	30,528	1,004	46
Total	1,375,387	555,142	639,735	114,432	20,191	45,888

A contractual maturity analysis is not provided in respect of other financial liabilities as typically the credit terms for other financial liabilities are up to 31 days.

The Company has no financial guarantee contracts

(e) Derivative holdings

A derivative transaction is a contract where value is derived from the value of an underlying asset or index.

The Company does not generally hold any investments including derivative contracts itself since it invests in unit trusts but these could in turn have exposure to derivative instruments. However, deliberate gearing up or leverage exposure to an asset is not permitted.

The Trusts may use derivatives for portfolio management purposes including managing duration for the purposes of matching liability duration. Derivatives are used as effective alternative to physical assets in order to achieve a desired level of total exposure and as a means to hedge against market movements. Total exposure is the sum of the market value of the physical assets plus the equivalent physical asset value attributed to the derivatives.

The most commonly used derivatives by the Trusts are exchange traded futures contracts and options. Exchange traded futures and options are used to hedge against adverse market fluctuations in the underlying security. Overseas currency options are entered into to hedge exposures to adverse movements in the Australian dollar. Forward foreign exchange contracts are entered into to hedge certain investments exposures denominated in foreign currencies.

Derivatives are valued on a fair value basis such that the Statement of Comprehensive Income and the Balance Sheet reflect all unrealised gains and losses on derivatives.

As at 31 December 2010 there was no significant counterparty exposure to one single entity, other than normal clearing house exposure associated with dealings through recognised exchanges (2009: Nil).

4. Financial risk management policies and procedures *(continued)*

(f) Fair value measurements

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes.

The Company adopted AASB 7 *Financial Instruments: Disclosures* which requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

(a) quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
(b) inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices) (level 2); and
(c) inputs for the asset or liability that are not based on observable market data (unobservable inputs) (level 3).

The following tables present the Company's assets and liabilities measured and recognised at fair value at 31 December 2010 and 31 December 2009.

As at 31 December 2010	**Level 1 $'000**	**Level 2 $'000**	**Level 3 $'000**	**Total $'000**
Unit trust - Equity securities	-	52,776	-	52,776
Unit trust - Debt securities	-	1,572,863	-	1,572,863
Shares in controlled entities	-	-	42,284	42,284
Total	-	1,625,639	42,284	1,667,923

As at 31 December 2009	**Level 1 $'000**	**Level 2 $'000**	**Level 3 $'000**	**Total $'000**
Unit trust - Equity securities	-	52,243	-	52,243
Unit trust - Debt securities	-	1,546,957	-	1,546,957
Shares in controlled entities	-	-	43,300	43,300
Total	-	1,599,200	43,300	1,642,500

The fair value of financial instruments traded in active markets (such as trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Company is the current bid price. These instruments are included in level 1.

Although the investments held by unit trusts are quoted, the units are not. Therefore, the investments in unit trusts do not meet the definition of level 1. The fair values of the units are determined to be a proportion of the net asset value of the unit trust. These instruments are included in level 2.

The fair value of financial instruments that are not traded in an active market (for example, government bond) is determined using valuation techniques. The Company uses a variety of methods and makes assumptions that are based on market conditions existing at the end of each reporting period. Estimated discounted cash flows, are used to determine fair value for the government bonds. These investments are included in level 2.

The fair value of shares in controlled entities is predominantly represented by the fair values of the investment properties held. As the valuation technique for investment properties is based on significant unobservable inputs, they are classified as level 3.

4. Financial risk management policies and procedures *(continued)*

(f) Fair value measurements *(continued)*

The following table presents the changes in level 3 instructions for the year ended 31 December 2010 and 31 December 2009.

	Unlisted equity securities **$'000**
Opening balance 1 January 2009	70,107
Disposals	(2,500)
Losses recognised in statement of comprehensive income	(24,307)
Closing balance 31 December 2009	43,300
Losses recognised in statement of comprehensive income	(1,016)
Closing balance 31 December 2010	42,284

The Company did not have any transfers between levels during the year.

The carrying amount of trade receivables and payables are assumed to approximate their fair values due to their short-term nature. The fair value of financial liabilities approximates the carrying amount, as the impact of discounting is not significant.

5. Insurance contracts - risk management policies and procedures

The financial condition and operation of the Company are affected by a number of key risks including insurance risk, investment market risk (including interest rate risk and currency risk), credit risk, liquidity risk, financial risk, compliance risk and operational risk. Notes on the Company's policies and procedures in respect of managing insurance risks are set out in this note.

(a) Objectives in managing risks arising from insurance contracts and policies for mitigating those risks

The Company has an objective to manage insurance risk thus reducing the volatility of operating profits. In addition to the inherent uncertainty of insurance risk, which can lead to significant variability in the loss experience, profits from insurance business are affected by market factors, particularly competition and movements in asset values. Short-term variability is, to some extent, a feature of insurance business. Various procedures are put in place to control and mitigate the risks faced by the Company depending on the nature of each risk. The Company's exposure to risks is monitored by the Appointed Actuary and this exposure is reported to the Board in the annual Financial Condition Report.

In accordance with General Insurance Prudential Standards GPS 220 Risk Management and GPS 230 Reinsurance Arrangements issued by the Australian Prudential Regulation Authority (APRA), the Board and senior management of the Company have developed, implemented and maintained a sound and prudent Risk Management Strategy (RMS) and a Reinsurance Management Strategy (REMS).

The RMS and REMS identify the Company's policies and procedures, processes and controls that comprise its risk management and control systems. These systems address all material risks, financial and non-financial, likely to be faced by the Company. Annually, the Board certifies to APRA that adequate strategies have been put in place to monitor those risks, that the Company has systems in place to ensure compliance with legislative and prudential requirements and that the Board has satisfied itself as to compliance with the RMS and REMS.

The RMS and REMS have been approved by the Board. Key aspects of the processes established in the RMS to mitigate risks arising from insurance contracts include:

- A formal annual high-level hazard assessment that focuses on key risks that impact the achievement of strategic and business objectives, including the development of action plans for the treatment and continuous monitoring of identified risks. This is bolstered by formal quarterly reviews of risk issues and progress against action plans.
- The maintenance and use of appropriate management information systems, which provide up to date, reliable data on the risks to which the business is exposed at any point in time.
- Actuarial models, using information from the management information systems, are used in calculating premiums and monitoring claims patterns. Past experience and statistical methods are used as part of the process.
- Formally delegated authorities and documented guidelines are followed for underwriting and accepting insurance risks.
- Natural disasters are more challenging to manage. Exposure to such risks is monitored through use of models involving the collation of the Company's exposure and wider environmental data, which support decisions on limiting exposure.
- Reinsurance is used to limit the Company's exposure to large single claims and catastrophes. When selecting a reinsurer the Company only considers those companies on a list approved by Zurich Group, which assesses reinsurer security using rating information from the public domain or gathered through internal investigations. If the Company selects a reinsurer not on the approved list, a separate approval by Zurich Group is required before placing the risk.
- In order to limit concentrations of credit risk in purchasing reinsurance, the Company has regard to existing reinsurance assets including the level of exposure to any single reinsurer or group of related reinsurers. Placing reinsurance with other companies in the Zurich Group is used as an initial step on a significant portion of the reinsurance program to enable group-wide reinsurance purchasing efficiencies.
- The mix of assets in which the Company invests is driven by the nature and term of the insurance liabilities. The management of assets and liabilities is closely monitored to broadly align the sensitivity of asset values to changes in interest rates with the equivalent sensitivity of the expected pattern of claim payments.
- The diversification of business over various classes of insurance and large numbers of uncorrelated individual risks reduces variability in loss experience.

5. Insurance contracts - risk management policies and procedures *(continued)*

(b) Terms and conditions of insurance business

The terms and conditions attaching to insurance contracts affect the level of insurance risk accepted by the Company. The majority of direct insurance contracts written are entered into on a standard form basis. Any non- standard terms and conditions are signed off by appropriately experienced underwriters within a framework, which includes delegated authorities, in line with the RMS.

(c) Concentration of insurance risk

The Company's exposure to concentration of insurance risk is mitigated by a portfolio of diversified individual risks. Specific processes for monitoring identified key concentrations are set out below.

Risk	Source of concentration	Risk management measures
Natural catastrophes	Properties and motor vehicles concentrated in regions that are subject to: • Earthquakes • Cyclones • Hail storms • Other significant natural event	The Company's underwriting strategy requires individual risk premiums to be differentiated in order to reflect the higher loss frequency in particular geographical segments. The Company has modelled aggregated risk using commercially available catastrophe models. Based on the probable maximum loss per the models, the Company purchases catastrophe reinsurance cover to limit exposure to any single event.

Direct premium revenue disclosed in the Statement of Comprehensive Income is split by product in the table below.

	2010 $'000	2009 $'000
Property	243,799	268,785
Motor	257,623	237,563
Marine & Aviation	117,195	113,409
Public & Product Liability	117,504	121,082
Compulsory Third Party (CTP)	105,969	88,419
Employers Liability	81,775	68,685
Professional Indemnity	46,414	33,420
Other	78,021	67,439
Total direct premium revenue	1,048,300	998,802

(d) Development of claims

There is a possibility that changes may occur in the estimate of the Company's obligations at the end of a contract period. The tables in Note 21 show the Company's estimates of total claims outstanding for each accident year at successive year ends for classes of business that are typically resolved in more than one year.

(e) Interest rate risk

None of the financial assets or liabilities arising from insurance or reinsurance contracts entered into by the Company is directly exposed to interest rate risk.

Insurance and reinsurance contracts are generally entered into annually. At the time of entering into the contract all terms and conditions are negotiable or, in the case of renewals, renegotiable.

5. Insurance contracts - risk management policies and procedures *(continued)*

(f) Credit risk

Financial assets and liabilities arising from insurance and reinsurance contracts are stated in the Balance Sheet at the amount that best represents the maximum credit risk exposure at balance date.

At balance date:

- 5.65% (2009: 4.58%) of reinsurance assets had a single third party reinsurer as a counter party; and
- 77.61% (2009: 81.72%) of reinsurance assets had other companies in the Zurich Group as a counter party.

There are no other significant concentrations of credit risk.

Reinsurance receivable on incurred claims disclosed in Note 13 are analysed in the table below using Standard and Poors (S&P) rating.

	2010 $'000	2009 $'000
AAA or AA	500,641	452,474
A	79,386	18,652
BBB or unrated	30,998	17,287
Below BBB	-	6
Total reinsurance receivable on incurred claims (excluding Risk Margin and other recoveries)	611,025	488,419

6. Investment income

	2010 $'000	2009 $'000
Dividends	94,953	121,735
Interest	2,212	1,568
Net realised/unrealised fair value gains/(losses) on financial assets at fair value through profit or loss	14,880	(28,081)
Other investment revenue	49	-
Total investment income	112,094	95,222

7. Other income

	2010 $'000	2009 $'000
Management fees	4,481	4,673
Other income	1,347	3,060
Total other income	5,828	7,734

8. Net claims incurred

	2010 $'000	2009 $'000
Gross claims incurred and related expenses:		
- Direct	964,596	853,580
- Inwards Reinsurance	27,955	12,367
- Discount	2,463	(78,468)
	995,014	787,479
Reinsurance and other recoveries:		
- Direct	397,035	352,126
- Inwards Reinsurance	27,116	11,379
- Discount	(786)	(53,938)
	423,365	309,567
Net incurred claims	571,649	477,912

Claims development
Current year claims relate to risks borne in the current financial year. Prior years' claims relate to a reassessment of the risks borne in all previous financial years.

	2010			2009		
	Current Year $'000	Prior Years $'000	Total $'000	Current Year $'000	Prior Years $'000	Total $'000
Gross claims expense						
- Undiscounted	1,163,377	(170,826)	992,551	1,086,734	(220,787)	865,947
- Discount	(48,389)	50,852	2,463	(88,246)	9,778	(78,468)
	1,114,988	(119,974)	995,014	998,488	(211,009)	787,479
Reinsurance and other recoveries:						
- Undiscounted	464,152	(40,001)	424,151	412,906	(49,401)	363,505
- Discount	(16,456)	15,670	(786)	(53,837)	(101)	(53,938)
	447,696	(24,331)	423,365	359,067	(49,502)	309,567
Net claims incurred – discounted	667,292	(95,643)	571,649	639,420	(161,507)	477,912

ZURICH AUSTRALIAN INSURANCE LIMITED

Notes to the Financial Statements *(continued)*
31 December 2010

9. Income tax

	2010 $'000	2009 $'000
(a) Income tax expense		
Current tax	20,355	42,167
Deferred tax	15,864	9,349
Under/(over) provision in prior years	(41)	241
Total income tax expense	36,178	51,757
Deferred income tax expense included in income tax expense comprises:		
Decrease in deferred tax asset (Note 16)	15,864	9,349
	15,864	9,349
(b) Numerical reconciliation of income tax to prima facie tax payable		
Profit before tax	70,913	157,031
Tax at the Australian tax rate of 30% (2009: 30%)	21,274	47,109
Tax effect of amounts which are not deductible/taxable in calculating taxable income:		
Tax offset for franked dividends	(410)	(374)
Withholding tax gross up	(1)	(72)
Non-taxable dividends	(1,026)	(7,042)
Non-deductible expense - realised loss on de-registration of controlled entities	-	1,372
Unrealised foreign exchange transaction	302	1,200
Unrealised book loss on investment in controlled entities	646	5,920
Unused tax losses not recognised	15,393	1,652
Other	-	1,750
	36,178	51,515
Under provision in prior year	-	242
Income tax expense	36,178	51,757

(c) Temporary differences relating to investment in controlled entities

As there is no intention of the Company to sell the investments in controlled entities, and it is expected that the controlled entities will remain in the tax consolidated group for the foreseeable future, the reversal of the temporary differences will have no income tax consequences for the Company. The transactions between a tax consolidated subsidiary and its parent, including the distribution of dividends from the subsidiary to the parent, are not taken into account for income tax purposes. Accordingly, the tax balance sheet value of the investment in the controlled entities is equal to its accounting carrying value and no temporary difference exists.

Similarly, with the investment in 100% owned unit trusts, the Company does not recognise any temporary differences with respect to its holdings in those trusts. As the 100% owned unit trusts are tax transparent entities, deferred taxes are recognised by the Company on temporary differences on the investments held in the unit trusts as if the investments are directly held by the Company.

9. Income tax *(continued)*

(d) Tax consolidation legislation

ZCM Asia Holdings Pty Limited (ZCM) and the members of the tax consolidated group implemented the tax consolidation legislation on 1 October 2003. The accounting policy in relation to this legislation is set out in Note 1(g).

The entities in the tax consolidated group have entered into a tax sharing agreement which, in the opinion of the directors, limits the joint and several liabilities of the entities within the group in the case of a default by the head entity, ZCM.

The tax sharing agreement is also a tax funding agreement. Under the tax funding agreement, the Company fully compensates ZCM for any current tax payable assumed and is compensated by ZCM for any current tax receivable and deferred tax assets relating to unused tax losses or unused tax credits that are transferred to ZCM under the tax consolidation legislation. The funding amounts are determined by reference to the amounts recognised (notional tax) in the Company's financial statements.

The amounts receivable/payable under the tax funding agreement are due upon receipt of the funding advice from the head entity, ZCM, which is issued as soon as practicable after the end of each financial year. The head entity may also require payment of interim funding amounts to assist with its obligations to pay tax instalments. The funding amounts are recognised as current intercompany receivables (see Note 11) or payables (see Note 17).

10. Cash and cash equivalents

	2010 $'000	2009 $'000
Current		
Cash at bank and on hand	10,901	66,657
Term deposit and cash equivalents	189,736	64,873
	200,637	131,530

Cash at bank was invested at floating interest rates between 3.0% and 5.5% (2009: 2.89% and 4.2%).

11. Receivables

	2010 $'000	2009 $'000
Current		
Premiums receivable	229,272	185,988
Unclosed premiums	104,819	95,277
	334,091	281,265
Provisions for impairment	(156)	(185)
	333,935	281,080
Investment income accrued and receivable	10,432	16,380
Due from related entities (Note 27)	2,148	45,531
Tax related receivables (Note 27)	--	8,318
Other trade debtors	212	79
Total current receivables	346,727	351,388

12. Financial assets at fair value through profit or loss

	2010 $'000	2009 $'000
Financial assets at fair value through profit or loss		
Current		
Unit trust - Equity securities	52,776	52,243
Unit trust - Debt securities	145,368	222,438
	198,144	274,681
Non-current		
Government and semi-government bonds	404	432
Unit trust - Debt securities	1,427,091	1,324,087
Shares in controlled entities (Note 28)	42,284	43,300
	1,469,779	1,367,819
Total financial assets at fair value through profit or loss	1,667,923	1,642,500

The classification of investment in unit trusts between current and non-current is based on a "look through" analysis of the liquidity of the underlying assets of the trusts.

13. Reinsurance and other recoveries

	2010 $'000	2009 $'000
Analysis of reinsurance and other recoveries		
Expected future reinsurance recoveries undiscounted		
- on claims paid	15,062	3,574
- on outstanding claims	650,376	544,669
	665,438	548,243
Discount to present value	(54,413)	(59,824)
Reinsurance receivable on incurred claims	611,025	488,419
Other recoveries undiscounted	189,306	106,878
Discount to present value	(15,986)	(9,892)
	173,320	96,986
Risk Margin	119,788	82,108
Discount to present value	(10,789)	(10,341)
	108,999	71,767
Reinsurance and other recoveries receivables on incurred claims	893,344	657,172
Expected future reinsurance recoveries on unexpired risk liability	30,800	17,986
Reinsurance and other recoveries receivable	924,144	675,158
Current	392,003	310,512
Non-current	532,141	364,646
	924,144	675,158

14. Deferred acquisition costs

	2010 $'000	2009 $'000
Deferred acquisitions costs as at 1 January	32,149	38,989
Acquisition costs deferred	111,180	104,325
Amortisation charged to income	(56,150)	(63,697)
Write down for premium deficiency (Note 20)	(45,630)	(47,468)
Deferred acquisitions costs as at 31 December	41,549	32,149
Current	40,916	32,025
Non-current	633	124
	41,549	32,149

15. Other assets

	2010 $'000	2009 $'000
Current		
Deferred outwards reinsurance expense	168,124	120,709
Fire service levy	21,877	21,030
	190,001	141,739

16. Deferred tax asset

	2010 $'000	2009 $'000
The balance comprises temporary differences attributable to:		
Amounts recognised in profit or loss		
Provisions for impairment	47	56
Accrued expenses	931	665
Provision for DAC write off and Unexpired Risk Liability	10,729	13,186
Indirect claim adjustment expense	9,924	15,878
Unused tax losses	2,002	4,962
Unrealised loss on investment assets	9,510	14,700
Net deferred tax asset	33,143	49,447
Deferred tax asset movements:		
Opening balance at 1 January	49,447	58,905
Currency translation difference	(440)	(109)
Charged to Statement of Comprehensive Income (Note 9)	(15,864)	(9,349)
Closing balance at 31 December	33,143	49,447

The Company has recognised deferred tax assets in respect of unused tax losses incurred by the New Zealand branch to the extent that it is probable that future taxable profit will be available against which the unused tax losses can be utilised. The Company has relied on the future business plans in determining that sufficient future taxable profits will be available to realise the deferred tax assets. Unused tax losses for which no deferred tax assets has been recognised at 31 December 2010 are $15,393,000 (2009: $1,652,289).

17. Payables

	2010 $'000	2009 $'000
Current		
Reinsurance creditors	42,732	26,164
Due to related entities (Note 28)	70,688	48,551
Tax related payable	2,821	-
Commission payable	19,686	18,248
Other payables	25,036	19,052
	160,963	112,015

18. Provisions

	2010 $'000	2009 $'000
Current		
Fire service levy	4,016	2,334
Stamp duty	5,589	5,813
Other	46	31
	9,651	8,178
Non-current		
Other	1,118	1,118
	1,118	1,118
Total	10,769	9,296

2009

Movements in provisions	Fire Service Levy $'000	Stamp Duty $'000	Other $'000	Total $'000
Current				
Carrying amount at start of year	3,427	4,413	(248)	7,592
Additional provision recognised	44,530	57,166	694	102,389
Payments/other sacrifices of economic benefits	(45,623)	(55,766)	(414)	(101,803)
Carrying amount at end of year	2,334	5,813	31	8,178
Non-current				
Carrying amount at start of year	-	-	1,118	1,118
Carrying amount at end of year	-	-	1,118	1,118
Total	2,334	5,813	1,149	9,296

18. Provisions *(continued)*

2010

Movements in provisions	Fire Service Levy $'000	Stamp Duty $'000	Other $'000	Total $'000
Current				
Carrying amount at start of year	2,334	5,813	31	8,178
Additional provision recognised	46,767	59,039	134	105,940
Payments/other sacrifices of economic benefits	(45,085)	(59,263)	(119)	(104,467)
Carrying amount at end of year	4,016	5,589	46	9,651
Non-current				
Carrying amount at start of year	-	-	1,118	1,118
Carrying amount at end of year	-	-	1,118	1,118
Total	4,016	5,589	1,164	10,769

19. Unearned premium liability

	2010 $'000	2009 $'000
Unearned premium liability as at 1 January	568,255	519,216
Currency translation difference	(1,939)	(807)
Premiums deferred during the period	1,140,035	1,073,596
Premiums earned during the period	(1,060,630)	(1,023,750)
Unearned premium liability as at 31 December	645,721	568,255
Current	608,300	529,709
Non-current	37,421	38,546
	645,721	568,255

20. Unexpired risk liability

	2010 $'000	2009 $'000
(a) Unexpired risk liability		
Unexpired risk liability as at 1 January	28,260	58,012
Currency transaction difference	(480)	-
Recognition of additional unexpired risk liability in the period	10,840	2,418
Release of unexpired risk liability recorded in previous periods	(2,344)	(32,170)
Unexpired risk liability as at 31 December	36,276	28,260
Unexpired risk liability - Current	36,276	28,260

20. Unexpired risk liability *(continued)*

(b) Deficiency recognised in the Statement of Comprehensive Income

	2010 $'000	2009 $'000
Gross movement in unexpired risk liability	8,495	(29,752)
Reinsurance recoveries on unexpired risk liability	(13,104)	15,075
Net movement in unexpired risk liability	(4,609)	(14,677)
Write down of deferred acquisition costs (Note 14)	45,630	47,468
Total deficiency recognised in the Statement of Comprehensive Income	41,021	32,791

(c) Calculation of deficiency

		2010 $'000	2009 $'000
Unearned premium liability		623,844	547,225
Related reinsurance asset		(168,124)	(120,709)
Related deferred acquisition costs		(74,380)	(71,677)
Total net unearned premium liability		381,340	354,839
Total net for business that has deficiency only	(A)	237,826	346,266
Central estimate of present value of expected future cash flows arising from future claims insurance contracts issued		518,468	458,716
Risk margin of 15.18% (2009: 15.04%)		53,040	52,227
Present value of expected future cash inflows arising from reinsurance recoveries		(113,855)	(74,596)
Present value of expected future cash inflows arising from non-reinsurance recoveries		(55,302)	(36,776)
Total net premium liability		402,351	399,571
Total net for business that has deficiency only	(B)	268,085	391,650
Net deficiency	(A) – (B)	(30,259)	(45,384)
Add back recoveries element of present value of expected future cash flows for future		(51,647)	(30,344)
Gross deficiency		(81,906)	(75,728)

The liability adequacy test is applied at a level of portfolios of contracts that are subject to broadly similar risks and that are managed together as a single portfolio. The test has been applied at a more detailed level than a split between long tail and short tail business.

The test has identified a deficiency for a few portfolios of contracts to which it was applied both at 31 December 2010 and 31 December 2009. This is primarily a consequence of inclusion of a risk margin in excess of the central estimate in performing the test.

The process for determining the overall risk margin, including the way in which diversification of risks has been allowed for is discussed in Note 21. As with outstanding claims, the overall risk margin is intended to achieve an 85% probability of adequacy in 2010. In 2009, this was also set to achieve an 85% probability of adequacy.

21. Outstanding claims

(a) Outstanding claims liability

	2010 $'000	2009 $'000
Central estimate	1,851,468	1,615,185
Discount to present value	(186,520)	(188,352)
	1,664,948	1,426,833
Claims handling costs	58,442	64,468
Discount to present value	(5,671)	(7,031)
	52,771	57,437
Risk margin	254,062	210,312
Discount to present value	(32,026)	(31,298)
	222,036	179,014
Gross outstanding claims liability	1,939,755	1,663,284
Undiscounted expected future claims payments	2,163,972	1,889,964
Discount to present value	(224,217)	(226,680)
Liability for outstanding claims	1,939,755	1,663,284
Current	765,134	667,313
Non-current	1,174,621	995,971
	1,939,755	1,663,284

(b) Risk Margin

Process for determining risk margin
The overall risk margin was determined allowing for diversification between the different portfolios and the relative uncertainty of the outstanding claims estimate for each portfolio. Uncertainty was analysed for each portfolio taking into account potential uncertainties relating to the actuarial models and assumptions, the quality of the underlying data used in the models, the general insurance environment, and the impact of legislative reform.

The estimate of uncertainty is greater for long tailed classes when compared to short tail classes due to the longer time until settlement of outstanding claims.

The assumptions regarding uncertainty for each class were applied to the net central estimates, and the results were aggregated, allowing for diversification in order to arrive at an overall provision which is intended to have an 85% probability of adequacy in 2010. In 2009, this was also set to achieve an 85% probability of adequacy.

21. Outstanding claims *(continued)*

(b) Risk margin *(continued)*

Risk Margins Applied

APRA Class	2010 Outstanding Claims Margin	2009 Outstanding Claims Margin
Short-tail		
Domestic Motor Vehicle	8.3%	8.2%
Commercial Motor Vehicle	9.2%	8.9%
Houseowners/Householders	8.3%	8.3%
Travel	8.3%	8.4%
Fire and ISR	12.4%	8.6%
Other	12.8%	11.6%
Marine & Aviation	11.6%	11.7%
Other Accident	11.4%	11.1%
Inward Treaty	45.7%	11.6%
Average short-tail	10.9%	9.6%
Long-tail		
Employers' Liability	11.6%	11.9%
Public & Product Liability	12.5%	13.5%
Professional Indemnity	20.2%	22.1%
CTP Motor Vehicle	11.4%	11.6%
Inward Treaty	34.8%	38.9%
Average long-tail	11.9%	12.4%
Overall	11.7%	11.8%

(c) Reconciliation of movement in discounted outstanding claims liability

	2010 Gross $'000	2010 Reinsurance $'000	2010 Net $'000	2009 Gross $'000	2009 Reinsurance $'000	2009 Net $'000
Brought forward	1,663,284	653,597	1,009,687	1,588,782	525,812	1,062,970
Effect of changes in assumptions	(119,974)	(24,331)	(95,643)	(211,009)	(49,451)	(161,558)
Increase in claims incurred/recoveries anticipated over the year	1,114,988	447,696	667,292	998,487	359,019	639,468
Incurred claims recognised in the Statement of Comprehensive Income	995,014	423,365	571,649	787,479	309,567	477,912
Exchange rate adjustment	(1,402)	(450)	(952)	(413)	(23)	(390)
Claim payments/recoveries during the year	(717,141)	(198,230)	(518,911)	(712,564)	(181,759)	(530,805)
Carried forward	1,939,755	878,282	1,061,473	1,663,284	653,597	1,009,687

21. Outstanding claims *(continued)*

(d) Claims development tables

The following tables show the development of gross and net ultimate undiscounted incurred claims for the five most recent accident years for classes of business that are typically resolved in more than one year. Gross outstanding claims include claims from inwards reinsurance.

(i) Gross incurred

Accident Year	2006 $'000	2007 $'000	2008 $'000	2009 $'000	2010 $'000	Total $'000
End of Accident Year	282,061	290,045	296,354	522,445	339,970	
One Year Later	235,698	284,770	292,621	519,876		
Two years later	207,765	271,400	265,716			
Three years later	190,977	265,634				
Four years later	186,697					
Current Estimate of Incurred	186,697	265,634	265,716	519,876	339,970	1,577,893
Cumulative Payments	117,002	117,553	83,799	55,583	20,663	394,600
Outstanding claims - Undiscounted	69,695	148,081	181,917	464,293	319,307	1,183,293
Discount						(153,734)
Claim Handling Expense						27,503
2005 and prior years						185,018
Outstanding claims - Discounted						1,242,080
Short Tail Outstanding Claims						697,675
Total Gross						1,939,755

(ii) Net incurred

Accident Year	2006 $'000	2007 $'000	2008 $'000	2009 $'000	2010 $'000	Total $'000
End of Accident Year	231,687	226,595	236,536	242,204	234,012	
One Year Later	198,366	212,220	218,984	225,934		
Two years later	178,660	194,163	203,985			
Three years later	162,688	187,304				
Four years later	161,574					
Current Estimate of Incurred	161,574	187,304	203,985	225,934	234,012	1,012,809
Cumulative Payments	109,866	87,532	68,383	46,176	18,813	330,770
Outstanding claims - Undiscounted	51,708	99,772	135,602	179,758	215,199	682,039
Discount						(75,815)
Claim Handling Expense						25,613
2005 and prior years						162,505
Outstanding claims - Discounted						794,342
Short Tail Outstanding Claims						267,131
Total Net						1,061,473

22. Contributed equity

	2010 $'000	2009 $'000
(a) Share capital		
Ordinary shares - fully paid	97,065	97,065

(b) Movements in ordinary share capital

Date	Details	No of Shares	$'000
1/01/2009	Opening balance	13,236	97,065
31/12/2009	Balance	13,236	97,065
31/12/2010	Closing balance	13,236	97,065

Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of and amounts paid on the shares held.

The Company manages its capital to ensure that it will be able to continue as a going concern including compliance with capital requirements imposed by relevant legislation and the industry regulators, Australian Prudential Regulation Authority (APRA) and Australian Securities and Investment Commission (ASIC). The Company aims to maintain capital beyond minimum requirements as described below.

The capital structure of the Company consists of issued capital, reserves and retained profits (Note 23). The Company's Capital and Investment Management Committee reviews the capital structure and makes recommendations to the Board on the appropriate level of capital.

The Company is required by APRA to maintain capital in excess of its minimum capital requirement (MCR). The MCR is intended to be broadly commensurate with the full range of risks to which an insurer is exposed (including risks relating to insurance claims, investments, counterparty default, asset-liability mismatches, catastrophic events and operational errors and problems). Certain assets (such as deferred tax assets, goodwill and other intangibles) cannot be used to meet the MCR. Refer Note 29 for calculation of capital base and MCR.

23. Reserves and Retained profits

	2010 $'000	2009 $'000
(a) Composition		
Foreign currency translation reserve	1,140	536
(b) Movements:		
Foreign currency translation reserve		
Balance at beginning of the year	536	52
Currency translation differences arising during the year	604	484
Balance at the end of the year	1,140	536
(c) Retained profits		
Retained profits at the beginning of the year	545,200	455,925
Profit attributable to the member of Zurich Australian Insurance Limited	34,735	105,275
Dividends provided or paid	(67,500)	(16,000)
Retained profits at the end of the year	512,435	545,200

24. Cash flow statement reconciliation

Reconciliation of profit after income tax to net cash inflows/(outflows) from operating activities

	2010 $'000	2009 $'000
Profit from operating activities after tax	34,735	105,275
Bad and doubtful debt provisions	(29)	-
Profit on sale of investments	(8,000)	(6,502)
Net purchase of investments	(8,047)	(25,319)
Net exchange difference	603	484
Disposal of controlled entities	-	7,073
Non-cash investments	(9,376)	(13,361)
(Increase)/decrease in operating assets:		
Premiums outstanding	(52,826)	(35,482)
Outstanding interest, dividends & rents	5,948	6,917
Deferred acquisition costs	(9,400)	6,840
Reinsurance and other recoveries	(248,986)	(107,700)
Other receivables	34,269	64,904
Deferred tax asset	16,304	9,458
Other assets	(48,262)	(20,418)
Increase/(decrease) in operating liabilities:		
Unexpired risk liability	8,016	49,039
Unearned premiums	77,466	(29,751)
Outstanding claims	276,471	74,501
Other provisions & payables	50,421	(46,568)
Net cash inflows from operating activities	119,307	39,390

25. Remuneration of auditors

	2010 $	2009 $
Remuneration for audit or review of the financial reports of the Company		
Statutory audit fees	429,195	256,341
	429,195	256,341
Remuneration for other services:		
Taxation compliance and assurance	18,000	-
Advisory service	-	20,845
Other regulatory and assurance services	241,309	253,989
Total other services	259,309	274,834

26. Contingent liabilities

	2010 $'000	2009 $'000
The Company had the following unsecured contingent liabilities for which no provision has been made in the financial statements:		
- State Transit Authority of NSW	50	50
	50	50

Details of significant contingent liabilities are as follows:

(a) The State Transit Authority NSW performance guarantee relates to an undertaking by the Company in respect of any failure by the Company in relation to its agreement with this entity.

27. Related parties

(a) Directors

The names of persons who were directors of Zurich Australian Insurance Limited at any time during the financial year are as follows:

Terence John Paradine
David James Parker Smith (Alternate Directors: Iain Campbell Howie, Robert Joseph Lehane)
Ian Clifton Carroll
Robert Olivier Dolk
Philip Wallace Smith
Michael Ronald Vos
Dirk Jan Celina De Nil
James Richard Sykes

(b) Key management personnel compensation

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

The key management personnel are all the directors of the Company and the following two executives (2009: two) with the authority and responsibility for planning, directing and controlling the activities of the entity:

- Andrew Paul Barrowman
- Shane Peter Doyle

All key management personnel compensation is paid by Zurich Financial Services Australia Limited. The amount disclosed below reflects the total compensation paid/attributable to the key management personnel in their duties as employees of ZFSA (and or directors of various entities) and is not able to be allocated to the individual entities whose affairs they manage or control.

	Notes	2010	2009
		$	$
Short term employee benefits		3,144,778	4,137,749
Termination benefits		938,066	601,694
Share-based payments/benefits	(i)	917,652	1,228,444
		5,000,496	5,967,887

(i) Share based payments/benefits

The Global Long Term Performance Share Plan and Global Share Option Plan are executive incentive plans administered globally by a central share holding vehicle. ZFSA purchases the right to shares from this holding vehicle for Australian resident executives who participate in the plans. When shares vest with the participants, the central share vehicle transfers those shares directly to the participants. ZFSA does not bear any exchange or price risk in relation to payments for these rights to shares.

27. Related parties *(continued)*

(c) Aggregate amounts receivable from related entities at balance date

	2010 $	2009 $
Current		
Controlling entity	98,680	16,404,238
Controlled entities	403,571	-
Other related entities	1,646,100	29,126,903
Head tax entity	-	8,317,829
	2,148,351	53,848,970

(d) Aggregate amounts payable to related entities at balance date

	2010 $	2009 $
Current		
Other related entities	70,687,778	48,550,935
Head tax entity	2,820,887	-
	73,508,665	48,550,935

27. Related parties *(continued)*

(e) Aggregate amounts recognised in respect of the following types of transactions and each class of related party involved were:

	2010 $	2009 $
Reinsurance claims received		
Other related entities	93,560,272	97,561,330
Reinsurance Claims Paid		
Other related entities	2,856,882	5,971,299
Reinsurance commission received		
Other related entities	16,551,423	11,307,530
Reinsurance premium expense		
Other related entities	186,159,363	173,930,536
Reinsurance premium receipts		
Other related entities	11,611,554	17,833,185
Investment expense		
Other related entities	1,114,520	1,302,507
Payment of other expenses		
Ultimate Australian controlling entity	160,556,563	152,057,243
Receipt of other income		
Other related entities	1,525,482	862,066
Dividend income		
Controlled entities	3,420,000	23,472,628
Dividend payment		
Ultimate Australian controlling entity	67,500,000	16,000,000

The above transactions were made on commercial terms and conditions at market rates.

Interest held in controlled entities and associates are included in Notes 28.

Investment income received from controlled entities and associates are included in Note 6.

27. Related parties *(continued)*

(f) Related parties of Zurich Australian Insurance Limited fall into the following categories:

(i) Controlling entities

The ultimate controlling entity is Zurich Financial Services (incorporated in Switzerland). The ultimate Australian controlling entity is Zurich Financial Services Australia Limited and is incorporated in Australia.

Information in relation to controlled entities is set out in Note 28.

(ii) Other related entities

Included in the reinsurance and other recoveries amounts in Note 13 is $291,326,682 (2009: $329,406,214) owing by related entities.

Included in other assets Note 15 is $90,019,165 (2009: $73,854,269) in respect of Deferred Outwards Reinsurance Expense by related entities.

The arrangements under which outward treaty reinsurance are ceded to related overseas reinsurers are approved by APRA.

(g) Other

The Company has a contractual agreement with Zurich Insurance Company (ZIC), the immediate controlling entity of Zurich Financial Services Australia (incorporated in Switzerland), under which ZIC will provide financial support to the Company in certain circumstances.

28. Investment in controlled entities

	Class of Shares	Equity Holding	
		2010	2009
Controlled Entities		%	%
Zurich Australian Insurance Properties Pty Limited	Ordinary	60.00	60.00
Zurich Properties Pty Limited	Ordinary	60.00	60.00
Zurich Investments Reserve Corporate Bond Pool		100.00	100.00
Zurich Investments Reserve Australian Share Pool		-	100.00
Zurich Investments Australian Indexed Bond Pool		67.01	62.47
Zurich Investments Reserve Long Term Maturities Fixed Interest Pool		-	75.78

Note: All entities are incorporated in Australia

The directors are satisfied that the carrying value of investments in controlled entities is not in excess of recoverable amount.

(a) Disposal of controlled entities

- On 31 January 2010, the Company disposed its holding in Zurich Investments Reserve Australian Share Pool.
- On 3 March 2010, the Company disposed its holding in Zurich Investments Reserve Long Term Maturities Fixed Interest Pool.

29. Capital adequacy for Zurich Australian Insurance Limited

	2010	2009
	$'000	$'000
Eligible Tier 1 Capital		
Paid-up ordinary shares	97,065	97,065
General reserves	(972)	(937)
Retained earnings brought forward	545,199	547,641
Current years earnings	(30,131)	68,693
Excess of technical provision – net of tax	32,177	-
Total	**643,338**	**712,462**
Less: Deductions from Tier 1 Capital		
Deferred tax assets (net of provisions for deferred income tax)	(33,143)	(49,447)
Reinsurance recoveries related to reinsurance contracts that do not meet the reinsurance documentation test	(3,320)	(3,655)
Reinsurance assets receivable under reinsurance contracts that do not meet governing law requirements	(13,698)	(11,145)
Total Capital Base	**593,177**	**648,215**
Minimum Capital Requirement	**382,174**	**570,291**
Capital Adequacy Multiple	**1.552**	**1.137**

The Company does not have any Tier 2 capital.

The liability required by GPS 210 for prudential reporting purposes differs from accounting purposes primarily because GPS 210 requires a prudential margin with a sufficiency of 75% for the outstanding claims and premium liabilities. The directors have adopted a provision that exceeds this requirement by $ 46.0 million (2009: $81.5 million).

The solvency position at 31 December 2009 reflects a retrospective adjustment to allow for the discovery during January 2010 that the catastrophe reinsurance programme was not adequate to provide cover for a 1 in 250 year event. Immediately this was realised, additional cover was bought to return to the intended position. On a pro-forma basis the capital adequacy multiple would be 1.878.

30. Events occurring after reporting date

Subsequent to the end of the financial year, there have been a number of catastrophes, which will impact the Company's 2011 results. These include

- Widespread flooding in Queensland and Victoria (gross and net claims are expected to be $160 million and $20 million respectively)
- Cyclone Yasi in North Queensland (gross and net claims are expected to be $35 million and $20 million respectively); and
- Earthquake in Christchurch, New Zealand (gross and net claims are expected to be $180 million and $20 million respectively).

The estimation of these amounts involves significant judgement and they are therefore subject to change as new information becomes available. As a consequence of these events, the Company has purchased additional catastrophe reinsurance cover (costing approximately $6 million) in 2011 to provide protection against future occurrences of other catastrophe events.

As a result of the earthquake in New Zealand in 2011, the Company may write off all or part of the deferred tax asset in respect of unused tax losses incurred by the New Zealand branch as recovery may no longer be probable.

Apart from the preceding disclosure, the directors have not become aware of any matter or circumstance not otherwise dealt with in the financial statements that has significantly affected or may significantly affect the operations of the Company, the results of those operations or the state of affairs of the Company in subsequent financial years.

ZURICH AUSTRALIAN INSURANCE LIMITED

Director's Declaration

In the directors' opinion:

(a) the financial statements and notes set out on pages 5 to 48 are in accordance with the *Corporations Act 2001*, including:

  (i) complying with Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements; and

  (ii) giving a true and fair view of the Company's financial position as at 31 December 2010 and of its performance, as represented by the results of its operations, changes in equity and its cash flows, for the financial year ended on that date; and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the directors.

T J Paradine Director	R O Dolk Director

Sydney
30 March 2011

pwc

Independent auditor's report to the members of Zurich Australian Insurance Limited

Report on the financial report

We have audited the accompanying financial report of Zurich Australian Insurance Limited (the company), which comprises the balance sheet as at 31 December 2010, and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with *International Financial Reporting Standards.*

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

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

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

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

PricewaterhouseCoopers, ABN 52 780 433 757
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pwc

Independent auditor's report to the members of Zurich Australian Insurance Limited (continued)

Independence

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

Auditor's opinion

In our opinion:

(a) the financial report of Zurich Australian Insurance Limited is in accordance with the *Corporations Act 2001*, including:

  (i) giving a true and fair view of the company's financial position as at 31 December 2010 and of its performance for the year ended on that date; and

  (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001;* and

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

PricewaterhouseCoopers

PricewaterhouseCoopers

V. Papageorgiou

Voula Papageorgiou
Partner

Sydney
30 March 2011

Liability limited by a scheme approved under Professional Standards Legislation

ZURICH AUSTRALIAN INSURANCE LIMITED
NEW ZEALAND BRANCH

ANNUAL FINANCIAL REPORT

For the year ended 31 December 2010

Contents	**Page Number**

This annual financial report covers Zurich Australian Insurance Limited New Zealand Branch as an individual entity only.

Zurich Australian Insurance Limited New Zealand Branch is a branch domiciled in New Zealand. Its registered office is:

55-65 Shortland Street
Auckland 1010

ZURICH AUSTRALIAN INSURANCE LIMITED
NEW ZEALAND BRANCH

Statement of Comprehensive Income
For the year ended 31 December 2010

	Notes	2010 $	2009 $
Premium revenue			
Direct premium revenue		79,208,668	73,623,996
Outwards reinsurance expense		(18,106,956)	(15,634,657)
Net premium revenue		61,101,712	57,989,339
Claims expense	8	(149,846,465)	(63,837,646)
Reinsurance and other recoveries revenue		64,097,381	14,778,251
Net claims incurred		(85,749,084)	(49,059,395)
Gross movement in unexpired risk liability		1,917,160	(10,157,080)
Reinsurance recoveries on unexpired risk liability		2,096,896	6,143,024
Net movement in unexpired risk liability		4,014,056	(4,014,056)
Acquisition costs		(8,238,889)	(13,164,583)
Other underwriting expenses		(15,595,861)	(15,498,001)
Total underwriting expenses		(23,834,750)	(28,662,584)
Underwriting result		(44,468,066)	(23,746,696)
Investment income		1,077,750	807,574
Other income		6,655	39,114
Net foreign exchange losses		(31,205)	(22,518)
Loss before income tax		(43,414,866)	(22,922,526)
Income tax (expense)/benefit	7 (a)	(7,210,238)	4,831,509
Total comprehensive expense for the year		**(50,625,104)**	**(18,091,017)**

The above Statement of Comprehensive Income should be read in conjunction with the accompanying notes.

The Board of Directors of Zurich Australian Insurance Limited authorised this Annual Financial Report for issue on 30 March 2011.

T J Paradine
Director

R O Dolk
Director

ZURICH AUSTRALIAN INSURANCE LIMITED
NEW ZEALAND BRANCH

Balance Sheet
For the year ended 31 December 2010

	Notes	2010	2009
		$	$
Head Office Account		(18,219,681)	(2,071,618)
Represented by:			
Assets			
Cash and cash equivalents	9	62,246,341	25,421,280
Receivables	10	31,394,461	29,462,020
Financial assets at fair value through profit or loss		530,714	533,598
Reinsurance and other recoveries	11	75,204,483	15,686,514
Deferred acquisition costs	12	750,740	521,048
Other assets	14	8,906,659	8,225,926
Deferred tax asset	13, 26	2,050,922	9,315,017
Total Assets		181,084,319	89,165,404
Liabilities			
Payables	15	14,145,604	9,381,259
Provisions	16	1,225,629	872,339
Unearned premium liability	17	44,646,879	41,070,139
Unexpired risk liability	18	8,239,920	10,157,080
Outstanding claims	19	131,045,969	29,756,204
Total Liabilities		199,304,001	91,237,022
Net Liabilities		(18,219,681)	(2,071,618)

The above Balance Sheet should be read in conjunction with the accompanying notes

ZURICH AUSTRALIAN INSURANCE LIMITED
NEW ZEALAND BRANCH

Statement of Changes in Head Office Account
For the year ended 31 December 2010

	Head Office Current Account $	Accumulated Losses $	Total $
Balance at 1 January 2009	-	(9,469,556)	(9,469,556)
Total comprehensive expense for the year	-	(18,091,017)	(18,091,017)
Transactions with head office:			
Contributions from head office, net of transaction costs	25,488,955	-	25,488,955
Balance as at 31 December 2009	25,488,955	(27,560,573)	(2,071,618)
Total comprehensive expense for the year		(50,625,104)	(50,625,104)
Transactions with head office:			
Contributions from head office, net of transaction costs	34,477,041	-	34,477,041
Balance as at 31 December 2010	59,965,996	(78,185,677)	(18,219,681)

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

Notes to the Financial Statements
For the year ended 31 December 2010

1. General information

This financial report includes the financial statements of Zurich Australian Insurance Limited New Zealand Branch ("the Branch"), as at 31 December 2010. The Branch results represent the general insurance activities in New Zealand that are underwritten by Zurich Australian Insurance Limited (ZAIL).

The Branch is domiciled in New Zealand. The financial statements of the Branch are presented in New Zealand dollars, which is the functional and presentation currency.

This financial report has been approved for issue by the Board of Directors on 30 March 2011. The Board has the power to amend and reissue the report.

2. Summary of significant accounting policies

The financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZGAAP). They comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), and other applicable New Zealand Financial Reporting Standards, as appropriate for profit-oriented entities.

(a) Basis of preparation

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

Statutory base
Zurich Australian Insurance Limited New Zealand Branch is a branch which is domiciled in New Zealand. It is registered under the Companies Act 1993.

The financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 1993 and the New Zealand Companies Act 1993.

Critical accounting estimates
The preparation of financial statements in conformity with NZ IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Branch's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 3.

It is prepared in accordance with the historical cost convention.

Differential reporting
The Branch is qualified within the Framework for Differential Reporting. The Branch qualifies on the basis that it is not publicly accountable and there is no separation between the owners and governing body of Zurich Australian Insurance Limited (ZAIL). The Branch has taken advantage of all differential reporting exemptions available to it except for NZIAS 12 Income Taxes with which it has complied fully.

(b) Principles of general insurance contracts

The general insurance operations of the Branch comprise the underwriting of various classes of direct insurance contracts. These contracts transfer significant insurance risk by agreeing to compensate the insured on the occurrence of a specified insured event, such as damage to property or the crystallisation of a third party liability within a given timeframe.

These contracts are defined as general insurance contracts.

2. Summary of significant accounting policies *(continued)*

(c) Insurance premium and related revenue

Direct premium comprises amounts charged to the policyholders or other insurers, excluding fire service levies and earthquake levies, and other amounts collected on behalf of third parties. The earned portion of premiums received and receivable, including bound but not incepted and unclosed business, is recognised as revenue. Premium is treated as earned from the date of attachment of risk. Premiums on unclosed business are brought to account by reference to the previous year's premium processing delays, with due allowance for any changes in the pattern of new business and renewals.

The pattern of recognition of income over the policy or indemnity periods is based on time, which closely approximates the pattern of risks underwritten. The proportion of premiums received and receivable but not earned in the Statement of Comprehensive Income at the reporting date is recognised in the Balance Sheet as an unearned premium liability. The unearned portion of commissions and other acquisition costs are also deferred and shown as deferred acquisition costs in the Balance Sheet.

(d) Insurance claims and related expenses

Claims expense represents payment for claims (and claims related expenses) and the movement in outstanding claims liabilities.

(e) Outwards reinsurance expense

Amounts paid to reinsurers under insurance contracts held by the Branch are recorded as outwards reinsurance expense and are recognised in the Statement of Comprehensive Income from the attachment date over the period of indemnity of the reinsurance contract in accordance with the expected pattern of the incidence of the risk ceded. Accordingly, a portion of outwards reinsurance expense is treated as a prepayment and presented as Deferred Outward Reinsurance Expense on the balance sheet as at reporting date.

(f) Income tax

The income tax expense or revenue for the period is the tax payable on the current period's taxable income based on the applicable income tax rate adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and unused tax losses.

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

Deferred tax assets and liabilities are recognised using the liability method for temporary differences at the tax rates expected to apply when the assets are recovered or liabilities are settled, based on those tax rates which are enacted or substantively enacted. The relevant tax rates are applied to the cumulative amounts of deductible and taxable temporary differences to measure the deferred tax asset or liability. An exception is made for certain temporary differences arising from the initial recognition of an asset or liability. No deferred tax asset or liability is recognised in relation to these temporary differences if they arose in a transaction, other than a business combination, that at the time of the transaction did not affect either accounting profit or taxable profit or loss.

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

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

2. Summary of significant accounting policies *(continued)*

(g) Goods and Services Tax (GST)

Revenues, expenses and assets, liabilities are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the New Zealand Inland Revenue. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from or payable to, the New Zealand Inland Revenue is included as an asset or liability in the Balance Sheet.

(h) Foreign currency translation

Foreign currency transactions are initially translated into New Zealand currency at the rate of exchange at the date of the transaction. At balance date, amounts payable and receivable in foreign currencies are translated into New Zealand currency at rates of exchange current at that date. Resulting exchange differences are brought to account in determining the profit or loss for the year.

(i) Cash and cash equivalents

Cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash which are subject to an insignificant risk of change in value, and bank overdrafts. Bank overdrafts are shown within interest bearing liabilities in liabilities on the balance sheet.

(j) Assets backing insurance liabilities

The assets of the Branch have been determined as being assets backing policy liabilities and are therefore valued at fair value through profit or loss.

It is considered that the use of fair value through profit or loss results in more relevant information because it eliminates or significantly reduces a measurement or recognition inconsistency.

(k) Reinsurance and other recoveries receivable

The benefits to which the Branch is entitled under its reinsurance contracts held are recognised as reinsurance receivable. Reinsurance and other recoveries receivable on paid claims, reported claims not yet paid, claims incurred but not reported (IBNR), claims incurred but not enough reported and unexpired risk liabilities are recognised as reinsurance and other recoveries revenue. Insurance recoveries receivable are assessed in a manner similar to the assessment of insurance outstanding claims. Recoveries receivable in relation to long-tail classes are measured as the present value of the expected future receipts, calculated on the same basis as the liability for insurance outstanding claims to which they relate.

(l) Deferred acquisition costs

The fixed and variable costs of acquiring new business, "the acquisition costs", include commission, advertising, policy issue and underwriting costs, agency expenses and other sales costs.

A portion of acquisition costs relating to unearned premium revenue is deferred and recognised as an asset, where it can be reliably measured and where it is probable that it will give rise to premium revenue that will be recognised in the Statement of Comprehensive Income in future periods. Deferred acquisition costs are measured at the lower of cost and recoverable amount and are amortised in accordance with the earning pattern of the corresponding premium revenue.

2. Summary of significant accounting policies *(continued)*

(m) Receivables

Receivables are recognised initially at fair value and subsequently subject to impairment testing. Impairment testing is based on collectibility of receivables and is reviewed on an ongoing basis. An impairment charge is recognised when there is objective evidence that the entity will not be able to collect all amounts due according to the original terms of the contracts. The impairment charge is recognised in the Statement of Comprehensive Income.

(n) Payables

These amounts represent liabilities for goods and services provided to the Branch prior to the end of the financial year and which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

(o) Provisions

Provisions are recognised when the Branch has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are not recognised for future operating losses.

(p) Outstanding claims

The liability for outstanding claims is measured as the central estimate of the present value of expected future payments against claims incurred at the reporting date under general insurance contracts issued by the Branch, with an additional risk margin to allow for the inherent uncertainty in the central estimate.

The expected future payments include those in relation to claims reported but not yet paid, claims incurred but not reported (IBNR), claims incurred but not enough reported (IBNER) and anticipated claims handling costs.

Claims handling costs include costs that can be associated directly with individual claims, such as legal and other professional fees, and costs that can only be indirectly associated with individual claims, such as claims administration costs.

The expected future payments are discounted to present value using a risk free rate.

(q) Unexpired risk liabilities

At each reporting date the Branch assesses whether the unearned premium liability is sufficient to cover all expected future cash flows relating to future claims against current insurance contracts. This assessment is referred to as the liability adequacy test and is performed separately for each group of contracts subject to broadly similar risks and managed together as a single portfolio.

If the present value of the expected future cash flows relating to future claims plus the additional risk margin to reflect the inherent uncertainty in the central estimate exceeds the unearned premium liability less related intangible assets and related deferred acquisition costs then the unearned premium liability is deemed to be deficient. The Branch applies a risk margin to achieve the same probability of sufficiency for future claims as is achieved by the estimate of the outstanding claims liability, see Note 4.

A write down to recoverable amount is recognised when the present value of expected future claims (including settlement costs) in relation to business written to the reporting date exceeds related unearned premium revenue. The entire deficiency, net of reinsurance, is recognised immediately in the Statement of Comprehensive Income. The deficiency is recognised first by writing down any related intangible assets and then related deferred acquisition costs, with any excess being recorded in the Balance Sheet as an unexpired risk liability.

(r) Equity

The Branch does not have any equity, however, the Total Head Office Account represents the value of any funding provided by Zurich Australian Insurance Limited (ZAIL) in support of the Branch operations.

2. Summary of significant accounting policies *(continued)*

(s) Financial assets

The investment assets of the Branch have been determined as being assets backing policy liabilities and are therefore valued at fair value through profit or loss.

It is considered that the use of fair value through profit or loss results in more relevant information because it eliminates or significantly reduces a measurement or recognition inconsistency.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Branch establishes fair value by using valuation techniques. These include reference to the fair values of recent arm's length transactions, involving the same instruments or other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

Purchases and sales of investments are recognised on trade-date – the date on which the Branch commits to purchase or sell the asset. Financial assets are initially recognised at cost. These assets are subsequently measured at fair value. Realised, unrealised gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the Statement of Comprehensive Income in the period in which they arise.

Financial assets are derecognised when the right to receive cash flows from the financial assets have expired or have been transferred and the Branch has transferred substantially all the risks and rewards of ownership.

(t) Impairment of assets

Financial assets measured at fair value, where changes in value are reflected in the Statement of Comprehensive Income, are not subject to impairment testing. Other assets such as receivables are subject to impairment testing.

Assets that have an indefinite useful life, such as identifiable intangible assets, are not subject to amortisation and are tested at least annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of an asset exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value (including realisation costs) and its value in use.

3. Critical accounting judgements and estimates

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

It has been determined that no critical accounting judgements have been made in the year.

(a) The ultimate liability arising from claims made under insurance contracts

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

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

The estimation of claims incurred but not reported (IBNR) is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Branch, where information about the claim event is generally available. IBNR claims may not be apparent to the insured until many years after the events giving rise to the claims has happened. The long-tailed classes of business will typically display greater variations between initial estimates and final outcomes because there is a greater degree of difficulty in estimating IBNR reserves. For the short-tailed classes, claims are typically reported soon after the claim event, and hence tend to display lower levels of volatility. In calculating the estimated cost of unpaid claims the Branch uses a variety of estimation techniques, generally based upon statistical analysis of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in the Branch's processes which might accelerate or slow down the development and/or recording of paid or incurred claims, compared with the statistics from previous periods
- changes in the legal environment
- the effects of inflation (both economic/wage and superimposed)
- changes in the mix of business
- the impact of large losses
- movements in industry benchmarks
- medical and technological developments
- changes in policyholder behaviour

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

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

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

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

3. Critical accounting judgements and estimates *(continued)*

(a) The ultimate liability arising from claims made under insurance contracts *(continued)*

Details of specific assumptions used in deriving the outstanding claims liability at year end are detailed in Note 4.

(b) Assets arising from reinsurance contracts

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

4. Actuarial assumptions and methods

The Branch writes both short-tailed and long-tailed business. The process for determining the value of outstanding claims liabilities is described below.

Case estimates are established by individual claims officers. The provision for large losses is reviewed by senior claims managers. The ultimate undiscounted cost of claims by year of accident and line of business is then established by actuaries using a variety of actuarial models at a line of business level. IBNR is then derived by subtracting from the ultimate cost, the amount of paid claims and case reserves. The estimation of IBNR is subject to a greater degree of uncertainty than the estimate of the cost of settling claims already notified and the estimate of the ultimate cost of long-tail lines is generally more uncertain than the estimate for short-tail lines where claims are often reported and settled within 1 year of occurrence.

The methods used to establish the ultimate cost of claims include the following:

- Projecting ultimate numbers of claims and multiplying by projected ultimate average cost
- Projecting ultimate claim payments
- Projecting ultimate incurred claim amounts
- Applying plan or expected loss ratios to earned premiums

Claims inflation is incorporated into the resulting projected payments, to allow for both general economic/wage inflation as well as any superimposed inflation detected in the modelling of payments experience. Superimposed inflation arises from non-economic factors such as legal developments. Future wage inflation is based on current levels and economic indicators. Future superimposed inflation is assessed based on current trends and industry information.

Projected reinsurance assets are derived using similar methods or applying net to gross ratios.

Projected payments are discounted to allow for the time value of money, based on current Government interest rates.

These methods assume that historical development is a reasonable basis on which to set assumptions about the future, and are thus subject to uncertainty surrounding changes to these patterns from whatever cause. In addition, there is uncertainty arising from the underlying assumptions for future wage inflation and superimposed inflation and of discount rates. Significant events, such as catastrophes, close to the balance sheet date also increase the level of uncertainty. The presence of asbestos claims in the portfolio and the potential emergence of new types of latent claim also increase the potential variability of the outcome.

For these reasons a risk margin is added to the central estimate established above. The establishment of the risk margin takes into account the variability of the outcome of each line of business and the diversification benefit of writing a number of lines of business. The Board and Management have decided that the level of risk margin shall be established to provide a probability of adequacy of 85% (2009: 85%).

(a) Selected key variables

The following indicators reflect the key variables that have been used in determining the outstanding claims liabilities.

	2010	2010	2009	2009
	Long-tail	Short-tail	Long-tail	Short-tail
Average weighted term to settlement	2.1 years	0.6 years	2.8 years	0.4 years
Discount rate	3.97%	N/A	4.59%	N/A
Wage inflation	4.00%	N/A	4.00%	N/A
Superimposed inflation	0 to 4.5%	N/A	0 to 4.5%	N/A

4. Actuarial assumptions and methods *(continued)*

(b) Sensitivity analysis – insurance contracts

The Branch conducts sensitivity analysis to quantify the exposure to risk of changes in the key underlying variables. The valuations included in the reported results are calculated using certain assumptions about these variables as disclosed above. The movement in any key variable will impact the performance and equity of the Branch. The tables below give an analysis of the sensitivity of the profit/(loss) and net assets/(liabilities), to changes in these assumptions both gross and net of reinsurance.

Impact of changes in key variables

December 2010		**Profit/(loss)**		
		Gross of reinsurance	**Net of reinsurance**	**Net Liabilities**
		$	$	$
Recognised amounts per the financial statements		(84,286,215)	(50,625,104)	(18,219,681)
Variable	**Movement in variable**	**Adjusted amounts**		
Long-tail				
Average weighted term to settlement - years	0.5	(84,135,449)	(50,561,806)	(18,156,384)
	-0.5	(84,430,322)	(50,684,590)	(18,279,168)
Discount rate	1%	(84,150,713)	(50,569,970)	(18,164,548)
	-1%	(84,426,567)	(50,682,235)	(18,276,813)
Wage inflation and superimposed inflation rates	1%	(84,431,096)	(50,684,085)	(18,278,663)
	-1%	(84,143,738)	(50,567,128)	(18,161,706)
Financial assets				
Shift in Yield Curve	1%	(85,041,750)	(51,380,639)	(18,975,217)
	-1%	(83,530,680)	(49,869,569)	(17,464,147)
Equity Prices	20%	(84,120,244)	(50,459,133)	(18,053,711)
	-20%	(84,452,186)	(50,791,075)	(18,385,653)

December 2009		**Profit/(loss)**		
		Gross of reinsurance	**Net of reinsurance**	**Net Liabilities**
		$	$	$
Recognised amounts per the financial statements		(10,381,576)	(18,091,017)	(2,071,618)
Variable	**Movement in variable**	**Adjusted amounts**		
Long-tail				
Average weighted term to settlement - years	0.5	(10,299,431)	(18,024,834)	(2,005,434)
	-0.5	(10,465,019)	(18,159,207)	(2,139,807)
Discount rate	1%	(10,305,232)	(18,014,975)	(1,995,575)
	-1%	(10,468,933)	(18,172,663)	(2,153,263)
Wage inflation and superimposed inflation rates	1%	(10,468,325)	(18,174,844)	(2,155,444)
	-1%	(10,296,851)	(18,009,374)	(1,989,974)
Financial assets				
Shift in Yield Curve	1%	(10,544,730)	(18,254,171)	(2,234,771)
	-1%	(10,218,422)	(17,927,863)	(1,908,463)
Equity Prices	+20%	(10,296,324)	(18,005,765)	(1,986,365)
	-20%	(10,466,828)	(18,176,269)	(2,156,869)

5. Financial risk management policies and procedures

The Branch's activities expose it to a variety of financial risks; market risk (including currency risk), credit risk and liquidity risk. The Branch's overall risk management focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Branch.

Risk management controls are outlined in the Risk Management Strategy (RMS). The objective of the RMS is to provide a summary of the policies and controls in place to address enterprise risks including certain operational and financial risks and the procedures for assessing compliance with these policies and controls. In addition, the Ultimate Controlling Entity, Zurich Financial Services's Zurich Risk Policy (ZRP) provides constraints on the mix of investment assets. The Branch has delegated its investment management responsibilities to Zurich Investment Management Limited (ZIM), which has in turn negotiated Investment Management Agreements (IMA) with external investment managers, with all funds managed in accordance with these IMAs. The overall investment strategy (and in particular the use of derivatives) is governed by the Zurich Investment Series Consolidated Constitution, the relevant IMAs, and the relevant funds offer documents and Product Disclosure Statements. The use of derivatives is consistent and subordinate to the investment strategy of each of the funds.

The RMS is subject to at least an annual review by the internal audit department. The internal audit department is independent of the day to day operational management of the Branch. The internal audit department prepares a report on compliance with the procedures outlined in the RMS.

The following list of factors are considered and addressed as part of the financial risk management policies and procedures.

a) Market risk

Market risk is the risk of diminution in value of the Branch's investment portfolio arising from adverse movements in the levels and volatility of interest rates, foreign exchange rates and equity prices. The Branch is not exposed to significant market risk. The exposure to changes in interest rate on cash holding is disclosed in Note 9.

b) Net fair value of financial assets and liabilities

On-Balance Sheet

The aggregate carrying values of financial assets and financial liabilities approximate their net fair values. The methods used to determine the carrying values of financial assets and liabilities are included in the Summary of significant accounting policies at Note 2.

Off-Balance Sheet

The Branch does not have potential financial liabilities which may arise from certain contingencies.

c) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Apart from reinsurance the Branch has no significant concentrations of credit risk. Where entities have a right of set-off and intend to settle on a net basis, this set-off has been reflected in the financial statements in accordance with accounting standards.

Reinsurance security is monitored continuously taking advantage of the, the Ultimate Controlling Entity, Zurich Financial Services's Security Committee analysis and there are strict controls around the use of individual reinsurers. Reinsurance accumulations are also monitored closely and used in deciding the appropriate placement programme at renewal.

The Branch does not hold listed equity, debt securities or deposits at call directly and has limited exposure to government bonds.

Standard and Poors (S&P) rating for Cash at bank disclosed in Note 9 is AA (2009: AA).

5. Financial risk management policies and procedures *(continued)*

c) Credit risk *(continued)*

The premiums receivable disclosed in Note 10 include amounts past due and not impaired which are analysed below.

	2010 $	2009 $
< 30 days	1,409,119	6,356,353
31 – 90 days	941,559	442,636
> 91 days	1,036,303	54,602
Total premiums receivable past due but not impaired	3,386,981	6,853,591

Refer to Note 6(f) for information on credit quality of reinsurance assets.

All other receivables do not include material amounts that are either past due or impaired.

d) Liquidity risk

Liquidity risk is the risk that the Branch will encounter difficulty in meeting obligations associated with financial liabilities.

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close-out market positions.

The risk is controlled by carefully monitoring cash flow, and maintaining suitable floats of readily realisable assets.

The table shows expected undiscounted cash flows from outstanding claims (notified claims, IBNR and claims handing costs) and premium liability (expected future claims). Both are net of reinsurance and non-insurance recoveries and before risk margin.

	Carrying amount (Undiscounted)	**Expected cash flows (undiscounted)**				
2010		0-1 yrs	1-5 yrs	5-10 yrs	10-15 yrs	>15yrs
	$	$	$	$	$	$
Insurance contracts						
Outstanding Claims (Note 11, 19)	54,881,171	49,451,776	5,372,167	57,228	-	-
Premium Liability	28,393,869	20,340,919	7,934,046	118,904	-	-
Total	83,275,040	69,792,695	13,306,213	176,132	-	-

	Carrying amount (Undiscounted)	**Expected cash flows (undiscounted)**				
2009		0-1 yrs	1-5 yrs	5-10 yrs	10-15 yrs	>15yrs
	$	$	$	$	$	$
Insurance contracts						
Outstanding Claims (Note 11, 19)	17,928,430	13,740,970	4,028,201	141,796	17,464	-
Premium Liability	29,786,873	20,377,508	9,059,020	343,409	6,936	-
Total	47,715,303	34,118,478	13,087,221	485,205	24,400	-

A contractual maturity analysis is not provided in respect of other financial liabilities as typically the credit terms for other financial liabilities are up to 31 days.

5. Financial risk management policies and procedures *(continued)*

e) Derivative holdings

A derivative transaction is a contract whose value is derived from the value of an underlying asset or index. The Branch does not hold any derivative contracts.

f) Fair value measurements

The Branch adopted the amendment to NZ IFRS 7 *Financial Instruments: Disclosures* which requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

a. quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
b. inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices) (level 2); and
c. inputs for the asset or liability that are not based on observable market data (unobservable inputs) (level 3).

The following tables present the Branch's assets measured and recognised at fair value at 31 December 2010 and 31 December 2009.

As at 31 December 2010	**Level 1**	**Level 2**	**Level 3**	**Total**
	$	**$**	**$**	
Financial assets at fair value through profit and loss	-	530,714	-	530,714
Total	**-**	**530,714**	**-**	**530,714**

As at 31 December 2009	**Level 1**	**Level 2**	**Level 3**	**Total**
	$	**$**	**$**	
Financial assets at fair value through profit and loss	-	533,598	-	533,598
Total	**-**	**533,598**	**-**	**533,598**

The fair value of financial instruments traded in active markets (such as trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Branch is the current bid price. These instruments are included in level 1.

The fair value of financial instruments that are not traded in an active market (such as New Zealand government bond) is determined using valuation techniques. The Branch uses a variety of methods and makes assumptions that are based on market conditions existing at the end of each reporting period. Estimated discounted cash flows, are used to determine fair value for the New Zealand government bond.

The Branch did not have any transfers between levels during the year.

6. Insurance contracts - risk management policies and procedures

The financial condition and operation of the Branch are affected by a number of key risks including insurance risk, investment market risk (including interest rate risk and currency risk), credit risk, liquidity risk, financial risk, compliance risk and operational risk. Notes on the policies and procedures in respect of managing these risks are set out in this note.

(a) Objectives in managing risks arising from insurance contracts and policies for mitigating those risks

The Branch has an objective to manage insurance risk thus reducing the volatility of operating profits. In addition to the inherent uncertainty of insurance risk, which can lead to significant variability in the loss experience, profits from insurance business are affected by market factors, particularly competition and movements in asset values. Short-term variability is, to some extent, a feature of insurance business.

The Risk Management Strategy (RMS) and Reinsurance Management Strategy (REMS) identify the policies and procedures, processes and controls that comprise the risk management and control systems. These systems address all material risks, financial and non-financial, likely to be faced.

Key aspects of the processes established in the RMS to mitigate risks arising from insurance contracts include:

- A formal annual high-level hazard assessment that focuses on key risks that impact the achievement of strategic and business objectives, including the development of action plans for the treatment and continuous monitoring of identified risks. This is bolstered by formal quarterly reviews of risk issues and progress against action plans.
- The maintenance and use of appropriate management information systems, which provide up to date, reliable data on the risks to which the business is exposed at any point in time.
- Actuarial models, using information from the management information systems, are used in calculating premiums and monitoring claims patterns. Past experience and statistical methods are used as part of the process.
- Formally delegated authorities and documented guidelines are followed for underwriting and accepting insurance risks.
- Natural disasters are more challenging to manage. Exposure to such risks is monitored through use of models involving the collation of our own exposure and wider environmental data, which support decisions on limiting exposure.
- Reinsurance is used to limit the exposure to large single claims and catastrophes. When selecting a reinsurer we only consider those companies on a list approved by Zurich Group head office, which assesses reinsurer security using rating information from the public domain or gathered through internal investigations. If the Branch selects a reinsurer not on the list approved by Zurich Group head office, a separate approval by Zurich Group head office is required before placing the risk.
- In order to limit concentrations of credit risk in purchasing reinsurance, the Branch has regard to existing reinsurance assets including the level of exposure to any single reinsurer or group of related reinsures. Placing reinsurance with other companies in the Zurich Group is used as an initial step on much of the reinsurance program to enable group-wide reinsurance purchasing efficiencies.
- The mix of investment assets is driven by the nature and term of the insurance liabilities. The management of assets and liabilities is closely monitored to broadly align the sensitivity of asset values to changes in interest rates with the equivalent sensitivity of the expected pattern of claim payments.
- The diversification of business over various classes of insurance and large numbers of uncorrelated individual risks reduces variability in loss experience.

(b) Terms and conditions of insurance business

The terms and conditions attaching to insurance contracts affect the level of insurance risk accepted by the Branch. The majority of direct insurance contracts written are entered into on a standard form basis. Any non standard terms and conditions are signed off by appropriately experienced underwriters within a framework, which includes delegated authorities, in line with the RMS.

6. Insurance contracts - risk management policies and procedures *(continued)*

(c) Concentration of insurance risk

The Branch's exposure to concentration of insurance risk is mitigated by a portfolio of diversified individual risks. Specific processes for monitoring identified key concentrations are set out below.

Risk	Source of concentration	Risk management measures
Natural catastrophes	Properties and motor vehicles concentrated in regions that are subject to: • Earthquakes • Cyclones • Hail storms • Other significant natural events	The Branch's underwriting strategy requires individual risk premiums to be differentiated in order to reflect the higher loss frequency in particular geographical segments. The Branch has modelled aggregated risk using commercially available catastrophe models. Based on the probable maximum loss per the models, the Branch purchases catastrophe reinsurance cover to limit exposure to any single event.

(d) Development of claims

There is a possibility that changes may occur in the estimate of the Branch's obligations at the end of a contract period. The tables in Note 19 show the Branch's estimates of total claims outstanding for each accident year at successive year ends for classes of businesses that are typically resolved in more than one year.

(e) Interest rate risk

None of the financial assets or liabilities arising from insurance or reinsurance contracts entered into by the Branch is directly exposed to interest rate risk.

Insurance and reinsurance contracts are generally entered into annually. At the time of entering into the contract all terms and conditions are negotiable or, in the case of renewals, renegotiable.

(f) Credit risk

Financial assets and liabilities arising from insurance and reinsurance contracts are stated in the Balance Sheet at the amount that best represents the maximum credit risk exposure at balance date.

At balance date:
- 7.15% (2009: 23.35%) of reinsurance assets had a single third party reinsurer as a counter party; and
- 78.19% (2009: 73.40%) of reinsurance assets had other companies in the Zurich Group as a counter party.

There are no other significant concentrations of credit risk.

Reinsurance receivable on incurred claims disclosed in Note 11 are analysed in the table below using Standard and Poors (S&P) rating.

	2010 $	2009 $
AAA or AA	32,536,264	4,926,192
A	4,477,339	202,892
BBB or unrated	1,902,752	187,620
Below BBB	-	56
Total reinsurance receivable on incurred claims (excluding Risk Margin and other recoveries)	38,916,355	5,316,760

7. Income tax

	2010 $	2009 $
(a) Income tax expense/(benefit)		
Current tax	-	-
Deferred tax (Note 13)	7,264,095	(4,831,509)
Under provision in prior years	*(53,857)*	-
Total income tax expense/(benefit)	7,210,238	(4,831,509)
(b) Numerical reconciliation of income tax expense to prima facie tax payable		
Loss before income tax	(43,414,866)	(22,922,526)
Tax at the New Zealand tax rate of 30% (2009 – 30%)	(13,024,460)	(6,876,758)
Value of deferred tax assets not recognised	20,234,698	2,045,249
Income tax expense/(benefit)	7,210,238	(4,831,509)

8. Net claims incurred

	2010 $	2009 $
Gross claims incurred and related expenses:		
- Direct	146,774,053	64,312,355
- Inwards Reinsurance	3,319,961	-
- Discount	(247,549)	(474,709)
	149,846,465	63,837,646
Reinsurance and other recoveries:		
- Direct	60,226,804	14,870,351
- Inwards Reinsurance	4,262,043	-
- Discount	(391,466)	(92,100)
	64,097,381	14,778,251
Net incurred claims	85,749,084	49,059,395

Claims Development

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

	2010			2009		
	Current Year $	Prior Years $	Total $	Current Year $	Prior Years $	Total $
Gross claims expense						
Undiscounted	162,549,344	(12,455,329)	150,094,015	68,791,077	(4,478,722)	64,312,355
Discount	(432,170)	184,620	(247,550)	(469,593)	(5,116)	(474,709)
	162,117,174	(12,270,709)	149,846,465	68,321,484	(4,483,838)	63,837,646
Reinsurance and other recoveries:						
Undiscounted	68,820,082	(4,331,235)	64,488,847	14,580,440	289,911	14,870,351
Discount	*(259,112)*	*(132,354)*	*(391,466)*	*(88,241)*	*(3,859)*	*(92,100)*
	68,560,970	(4,463,589)	64,097,381	14,492,199	286,052	14,778,251
Net claims incurred – discounted	93,556,204	(7,807,120)	85,749,084	53,829,285	(4,769,890)	49,059,395

9. Cash and cash equivalents

	2010 $	2009 $
Cash at bank and on hand	22,388,704	25,421,280
Term deposit and cash equivalents	39,857,637	-
	62,246,341	25,421,280

10. Receivables

	2010 $	2009 $
Premiums receivable	26,033,368	18,688,533
Unclosed premiums	2,250,630	5,515,737
	28,283,998	24,204;270
Due from related entities (Note 21)	2,193,315	4,595,364
Other trade debtors	868,466	655,637
Interest receivable	48,682	6,749
Total current receivables	31,394,461	29,462,020

11. Reinsurance and other recoveries

	2010 $	2009 $
Analysis of Reinsurance and other recoveries		
Expected future reinsurance recoveries undiscounted		
- on claims paid	53,659	-
- on outstanding claims	39,192,942	5,395,044
Discount to present value	(330,245)	(78,284)
Reinsurance receivable on incurred claims	38,916,356	5,316,760
Other recoveries undiscounted	19,032,453	3,280,645
Discount to present value	(81,785)	(240)
	18,950,668	3,280,405
Risk margin	9,169,585	960,363
Discount to present value	(72,046)	(14,037)
	9,097,539	946,326
Reinsurance and other recoveries receivables on incurred claims	66,964,563	9,543,491
Expected future reinsurance recoveries on unexpired risk liability	8,239,920	6,143,023
Reinsurance and other recoveries receivable	75,204,483	15,686,514
Current	70,882,264	15,345,336
Non-current	4,322,219	341,178
	75,204,483	15,686,514

12. Deferred acquisition costs

	2010 $	2009 $
Deferred acquisitions costs as at 1 January	521,048	4,383,976
Acquisition costs deferred	10,213,162	11,700,935
Amortisation charged to Statement of Comprehensive Income	(3,933,706)	(9,204,805)
Write down for premium deficiency	(6,049,764)	(6,359,058)
Deferred acquisitions costs as at 31 December	750,740	521,048
Current	750,242	521,016
Non-current	498	32
	750,740	521,048

13. Deferred tax asset

	2010 $	2009 $
The balance comprises temporary differences attributable to:		
Amounts recognised in profit or loss		
Provision for DAC write off and Unexpired Risk Liability	(581,078)	2,701,400
Indirect claim adjustment	-	471,941
Unused tax losses	2,632,000	6,141,676
Net deferred tax asset	2,050,922	9,315,017

Deferred tax asset movements:

	2010	2009
Opening balance at 1 January	9,315,017	4,483,508
Charged to Statement of Comprehensive Income (Note 7)	(7,264,095)	4,831,509
Closing balance at 31 December	2,050,922	9,315,017

The Branch has recognised deferred tax assets in respect of unused tax losses to the extent that it is probable that future taxable profit will be available against which the unused tax losses can be utilised. The Branch has relied on the business case establishing the business and future year business plans in determining that sufficient future taxable profits will be available to realise the deferred tax asset. Unused tax losses for which no deferred tax assets have been recognised at 31 December 2010 are $20,234,698 (2009: $2,045,249).

14. Other assets

	2010 $	2009 $
Current		
Deferred outward reinsurance expense	8,906,659	8,225,926
	8,906,659	8,255,926

Notes to the Financial Statements *(continued)*
For the year ended 31 December 2010

15. Payables

	2010 $	2009 $
Current		
Reinsurance creditors	3,947,926	2,675,439
Due to related entities (Note 21)	7,645,561	4,433,297
Commission payable	795,538	1,452,013
Other payables	1,756,579	820,510
	14,145,604	9,381,259

16. Provisions

	2010 $	2009 $
Current		
Fire service levy	1,140,762	834,476
Earthquake levy	84,767	37,863
Others	100	-
	1,225,629	872,339

Movements in provisions	Fire Service Levy	Earthquake Levy	Others	Total
2009				
Carrying amount at 1 January	1,285,451	26,709	91	1,312,251
Additional provision recognised	5,634,061	401,487	-	6,035,548
Payments/other sacrifices of economic benefits	(6,085,036)	(390,333)	(91)	(6,475,460)
Carrying amount 31 December	834,476	37,863	-	872,339
2010				
Carrying amount at 1 January	834,476	37,863	-	872,339
Additional provision recognised	6,784,390	422,402	100	7,206,892
Payments/other sacrifices of economic benefits	(6,478,104)	(375,498)	-	(6,853,602)
Carrying amount at 31 December	1,140,762	84,767	100	1,225,629

17. Unearned premium liability

	2010 $	2009 $
Unearned premium liability at 1 January	41,070,139	33,654,947
Premiums deferred during the period	82,785,409	83,621,751
Premiums earned during the period	(79,208,669)	(76,206,559)
Unearned premium liability at 31 December	44,646,879	41,070,139
Current	43,890,051	40,935,672
Non-current	756,828	134,467
	44,646,879	41,070,139

18. Unexpired risk liability

		2010 $	2009 $
(a) Unexpired risk liability			
Unexpired risk liability as at 1 January		10,157,080	-
Recognition of additional unexpired risk liability in the period		(1,917,160)	10,157,080
Unexpired risk liability at 31 December		8,239,920	10,157,080
Unexpired risk liability - Current		8,239,920	10,157,080
(b) Deficiency recognised in the Statement of Comprehensive Income			
Gross movement in unexpired risk liability		(1,917,160)	10,157,080
Reinsurance recoveries on unexpired risk liability		(2,096,896)	(6,143,024)
Net movement in unexpired risk liability		(4,014,056)	4,014,056
Write down of deferred acquisition cost (Note 12)		6,049,764	6,359,057
Total deficiency recognised in the Statement of Comprehensive Income		2,035,708	10,373,114
(c) Calculation of deficiency			
Unearned premium liability		44,646,879	41,070,139
Related reinsurance asset		(8,906,664)	(8,225,929)
Related deferred acquisition costs		(6,103,533)	(6,215,310)
Total net unearned premium liability		29,636,682	26,628,900
Total net for business that have deficiency only	(A)	29,258,797	26,628,900
Central estimate of present value of expected future cashflows arising from future claims on insurance contracts issued		43,435,035	41,998,038
Risk margin of 19.21% (2009: 20.38%)		5,432,265	6,033,771
Present Value of expected future cash inflows arising from reinsurance recoveries		(5,724,547)	(7,977,357)
Present Value of expected future cash inflows arising from non-reinsurance recoveries		(9,439,221)	(4,420,885)
Total net premium liability		33,703,532	35,633,567
Total net for business that have deficiency only	(B)	33,336,283	35,633,567
Net Deficiency	(A) – (B)	(4,077,486)	(9,004,667)
Add back recoveries element of present value of expected future cash flows for future		(10,212,198)	(7,511,470)
Gross deficiency		(14,289,684)	(16,516,137)

Notes to the Financial Statements *(continued)*
For the year ended 31 December 2010

19. Outstanding claims

(a) Outstanding claims liability

	2010	2009
	$	$
Central Estimate	104,898,131	24,980,808
Discount to present value	(651,429)	(411,671)
	104,246,702	24,569,137
Claims Handling Costs	8,208,404	1,623,311
Discount to present value	-	(30,412)
	8,208,404	1,592,899
Risk Margin	18,703,833	3,668,915
Discount to present value	(112,970)	(74,747)
	18,590,863	3,594,168
Gross outstanding claims liability	131,045,969	29,756,204

	2010	2009
	$	$
Undiscounted expected future claims payments	131,810,368	30,273,034
Discount to present value	(764,399)	(516,830)
Liability for outstanding claims	131,045,969	29,756,204
Current	123,300,937	27,881,361
Non-current	7,745,032	1,874,843
	131,045,969	29,756,204

(b) Risk margin

Process for determining risk margin
The overall risk margin was determined allowing for diversification between the different portfolios and the relative uncertainty of the outstanding claims estimate for each portfolio. Uncertainty was analysed for each portfolio taking into account potential uncertainties relating to the actuarial models and assumptions, the quality of the underlying data used in the models, the general insurance environment, and the impact of legislative reform.

The estimate of uncertainty is greater for long tailed classes when compared to short tail classes due to the longer time until settlement of outstanding claims.

The assumptions regarding uncertainty for each class were applied to the net central estimates, and the results were aggregated, allowing for diversification. These margins are consistent with those applied to Zurich Australian Insurance Limited as a whole in order to arrive at an overall provision which is intended to have an 85% (2009: 85%) probability of sufficiency.

19. Outstanding claims *(continued)*

(b) Risk margin *(continued)*

Risk Margins Applied

Class	2010 Outstanding Claims Margin	2009 Outstanding Claims Margin
Short Tail		
Commercial Motor Vehicle	16.1%	15.7%
Fire and Industrial Specialised Risk	22.6%	33.3%
Marine & Aviation	11.7%	11.8%
Other Accident	17.9%	17.9%
Inwards Treaty - ST	19.3%	N/A
Average Short Tail	19.7%	15.6%
Long Tail		
Public & Product Liability	3.0%	12.9%
Professional Indemnity	17.9%	17.9%
Inwards Treaty - LT	21.6%	N/A
Average Long Tail	4.8%	13.2%
Overall	17.3%	15.1%

(c) Reconciliation of movement in discounted outstanding claims liability

	2010 Gross $	2010 Reinsurance $	2010 Net $	2009 Gross $	2009 Reinsurance $	2009 Net $
Brought Forward	29,756,204	(9,543,491)	20,212,713	17,225,225	(974,839)	16,250,386
Effect of changes in assumptions	(12,270,709)	4,463,589	(7,807,120)	(4,423,689)	(406,349)	(4,830,038)
Increase in claims incurred/recoveries anticipated over the year	162,117,174	(68,560,970)	93,556,204	68,321,599	(14,432,050)	53,889,549
Incurred claims recognised in the Statement of Comprehensive Income	149,846,465	(64,097,381)	85,749,084	63,897,910	(14,838,399)	49,059,511
Claim payments / recoveries during the year	(48,556,700)	6,729,968	(41,826,770)	(51,366,931)	6,269,747	(45,097,184)
Carried Forward	131,045,969	(66,910,904)	64,135,065	29,756,204	(9,543,491)	20,212,713

19. Outstanding claims *(continued)*

(d) Claims development tables

The following tables show the development of gross and net undiscounted outstanding claims relative to the ultimate expected claims for the five most recent accident years for classes of business that are typically resolved in more than one year.

(i) Gross Incurred

Accident Year	**2006** $	**2007** $	**2008** $	**2009** $	**2010** $	**Total** $
End of Accident Year	390,342	211,667	273,549	5,034,300	5,809,730	
One Year Later	73,191	189,312	635,149	5,294,533		
Two years later	4,971	148,136	366,630			
Three years later	24,096	103,202				
Four years later	12,667					
Current Estimate of Incurred	12,667	103,202	366,630	5,294,533	5,809,730	11,586,762
Cumulative Payments	1,191	49,731	167,988	730,277	529,845	1,479,032
Outstanding claims - Undiscounted	11,476	53,471	198,642	4,564,256	5,279,885	10,107,730
Discount						(764,399)
Claim Handling Expense						379,286
2005 and prior years						-
Outstanding claims - Discounted						9,722,617
Short Tail Outstanding Claims						121,323,352
Total Gross						131,045,969

(ii) Net Incurred

Accident Year	**2006** $	**2007** $	**2008** $	**2009** $	**2010** $	**Total** $
End of Accident Year	105,715	200,667	269,027	3,647,090	2,434,884	
One Year Later	74,191	189,312	468,170	1,839,199		
Two years later	4,956	115,956	283,804			
Three years later	16,700	80,937				
Four years later	8,168					
Current Estimate of Incurred	8,168	80,937	283,804	1,839,199	2,434,884	4,646,991
Cumulative Payments	1,191	49,731	139,683	577,593	304,152	1,072,350
Outstanding claims - Undiscounted	6,977	31,206	144,121	1,261,605	2,130,732	3,574,642
Discount						(280,354)
Claim Handling Expense						378,718
2005 and prior years						-
Outstanding claims - Discounted						3,673,006
Short Tail Outstanding Claims						60,462,059
Total Net						64,135,066

20. Remuneration of auditors

	2010 $	2009 $
Remuneration for audit or review of the financial statements of the Branch:		
Statutory audit fees	37,802	21,542
	37,802	21,542

21. Related parties

(a) Aggregate amounts receivable from related entities at balance date

	2010 $	2009 $
Current		
Immediate controlling entity	624,910	1,472,775
Other related entities	1,568,405	3,122,589
	2,193,315	4,595,364

(b) Aggregate amounts payable to related entities at balance date

Current		
Controlling entity	1,348,516	786,937
Other related entities	6,297,045	3,646,360
	7,645,561	4,433,297

(c) Aggregate amounts recognised in respect of the following types of transactions and each class of related party involved were:

	2010 $	2009 $
Payment of reinsurance premium expenses		
Other related entities	15,424,703	13,348,942
Payment of reinsurance commission expense		
Other related entities	1,076,154	990,183
Reinsurance claims recoveries		
Other related entities	30,698,707	4,941,451

The above transactions were made on commercial terms and conditions at market rates.

(d) Aggregate amount of contributions received from/distribution payable to head office

	2010 $	2009 $
Head office account	(165,429)	2,061,611

The transaction with the head office is disclosed in the Statement of Changes in Head Office Account.

21. Related parties *(continued)*

(e) Related parties of Zurich Australian Insurance Limited New Zealand Branch fall into the following categories:

(i) **Head Office**

This branch is the New Zealand branch of an Australian operation, Zurich Australian Insurance Limited, which is an Australian registered insurance company.

(ii) **Holding company**

The immediate holding entity is Zurich Financial Services Australia Limited and is incorporated in Australia.

The ultimate holding company is Zurich Financial Services Limited, an entity incorporated in Switzerland.

(iii) **Other related entities**

Included in the reinsurance and other recoveries amounts in Note 11 is $74,511,725 (2009: $13,501,684) owing by related entities.

22. Credit rating of insurer

During 2010, Standard & Poors has rated the parent company, Zurich Australian Insurance Limited with an A+ credit rating. This rating was assigned on 16 December 2010.

23. Reinsurance programme

The reinsurance strategy chosen to protect Zurich Australian Insurance Limited's liabilities in New Zealand matches the Australian reinsurance strategy in 2010. It has the following characteristics:

- A maximum per risk net retention of NZD equivalent to AUD8 million, except for Associated Marine and property, which is NZD equivalent to AUD5 million, Motor TPPD which is NZD equivalent to AUD8 million, Motor Own Damage is various and Engineering is NZD equivalent to AUD6 million.
- A maximum per event retention of NZD equivalent to AUD20 million.

Reinsurance is purchased through a series of treaty and facultative contracts with external reinsures and with members of the Zurich Financial Services Limited group.

24. Capital management

While the Branch does not have any Capital of its own it does manage funds from the Head Office. When managing capital, management's objective is to ensure the Branch continues as a going concern as well as maintaining optimal returns to the holding company and benefits for other stakeholders. The investment strategy is conservative whereby investments are held in cash and fixed interest securities.

25. Going concern

The Branch has net liabilities of $18,219,681 at 31 December 2010. The current liabilities position includes unearned premium liability balance of $44,646,879 which does not require cash settlement. The Head Office has committed to provide funding to the branch to maintain its operations and will not request the repayment of the aggregate amounts due to the Head Office in the coming 12 months. As a result, the directors consider it is appropriate for the financial statements to be prepared on a going concern basis.

26. Events occurring after reporting date

Subsequent to the end of the financial year, an earthquake occurred in Christchurch New Zealand which will impact the Branch's 2011 results. Based on currently available information, the Branch is expecting net claims from the earthquake to be NZD equivalent of AUD20 million. This is equivalent to the Branch's maximum loss for such an event, net of amounts due from its reinsurers. The estimation of this amount involves significant judgement and it is therefore subject to change as new information becomes available. As a consequence of this event, ZAIL has purchased additional catastrophe reinsurance cover (costing the NZD equivalent of approximately AUD5 million) in 2011 to provide protection against future occurrences of other catastrophe events.

As a result of the earthquake in 2011, the Branch may write off all or part of the deferred tax asset in respect of unused tax losses as recovery may no longer be probable.

Apart from the preceding disclosure, the directors have not become aware of any matter or circumstance not otherwise dealt with in the financial statements that has significantly affected or may significantly affect the operations of the Branch, the results of those operations or the state of affairs of the Branch in subsequent financial years.

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Independent Auditors' Report to the Directors of Zurich Australian Insurance Limited

Report on the financial statements

We have audited the financial statements of Zurich Australian Insurance Limited New Zealand Branch (the New Zealand Branch) on pages 1 to 28, which comprise the balance sheet as at 31 December 2010, the statement of comprehensive income and statement of changes in head office account for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

The Directors of Zurich Australian Insurance Limited (the Company) are responsible for the preparation of these financial statements in accordance with generally accepted accounting practice in New Zealand and that present fairly the matters to which they relate and for such internal controls as the Directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

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

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

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

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

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Independent Auditors' Report to the Directors of Zurich Australian Insurance Limited (continued)

Opinion

In our opinion, the financial statements on pages 1 to 28:

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

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

Restriction on distribution or use

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

PricewaterhouseCoopers

Chartered Accountants Sydney

30 March 2011

I, Voula Papageorgiou, am currently a member of the Institute of Chartered Accountants In Australia and my membership number is 96318.

PricewaterhouseCoopers was the audit firm appointed to undertake the audit of Zurich Australian Insurance Limited for the year ended 31 December 2010. I was responsible for the execution of the audit and delivery of our firm's auditors' report. The audit work was completed on 30 March 2011 and an unqualified opinion was issued.

V Papageorgiou

Voula Papageorgiou